



# **Submission to Department of Business, Enterprise and Innovation**

## **Draft EU Directive on Unfair Trading Practices in Business to Business Relationships in the Food Supply Chain (COM(2018) 173 Final – 2018/0082 (COD))**

**May 2018**

## Introduction and opening comments

Food Drink Ireland (FDI) welcomes the publication of the draft EU Directive and [the opportunity to submit our views](#) to the Department of Business, Enterprise and Innovation. The draft Directive has the potential to improve relations in the food chain and to address complaints between major grocery retailers and suppliers across Europe. Unfair practices faced by a number of food and drink companies include a failure to respect contractual terms, de-listing threats and unilateral deductions off-invoice without sound business reasons. In the short-term these demands impact on individual suppliers, but ultimately, they are also bad for consumers.

Consumers are best served by a grocery market that is both fair and competitive, one that offers choice and convenience, and provides an outlet for new products and suppliers. The new rules have the potential to help to address some of the unfair pressures currently put on suppliers by major retailers.

The Irish food and drink sector plays a central role in Irish society. It generates economic growth, provides hundreds of thousands of jobs and provides a market for over 90% of agricultural output. The majority (68%) of our food and drink exports go to the European Union:

- €4.5bn to the UK (35%)
- €4.1bn to the rest of the EU (33%)

However, a number of grocery retailer-supplier relationships across the EU are dysfunctional. This occurs when the imbalance of buying power between a larger retailer and their suppliers is abused. This can manifest itself as unfair practices such as a failure to respect contractual terms, delisting threats to obtain unjustified advantages and unilateral deductions off invoices without sound or mutually agreed business reasons. These unfair practices lead to lower profitability for food companies, difficulties with business planning and cash management, an inability to reinvest in plant, equipment and innovation and costly inefficiencies along the supply chain. The problem is more evident in countries, like Ireland, where many food companies lack scale relative to the scale of the domestic market thus necessitating access to other EU single markets. Left unchecked, this will have profoundly negative long-term consequences for both the food chain and consumers across the EU.

Effective EU legislation can prevent retailers transferring excessive risks and costs of doing business onto suppliers without placing undue burdens on retailers or impinging the passing on of lower prices to consumers. Rather, it should ensure that the risks and costs of responding to changing consumer demands are shared equitably between supplier and retailer, allowing both to grow sustainable businesses. FDI has consistently supported grocery sector legislation. FDI retains its belief that only legislation that (i) outlaw's retrospective demands for arbitrary payments; (ii) insists on principles of fair dealing between retailer and supplier and (iii) is monitored effectively and proactively by a third party focused exclusively on relationships in the sector, will result in the best outcome for the consumer. The legislation should have no remit in assessing the genuine commercial negotiations of suppliers and retailers. Such a level of intervention would negatively affect the dynamic in the sector to deliver on consumer demands for value, quality and convenience.

## Scope of the Regulations

FDII believes that the draft EU Directive should apply to the full food chain. Unfair trading practices by retailers do not discriminate by size of supplier. The scope of the Directive must be applicable to

all businesses in the food supply chain and not just farmers and SMEs as currently proposed. Such an extension would align with the scope of the Irish Grocery Goods Regulations 2016 which covers the relationship between Regulated Grocery Goods Undertakings and suppliers regardless of size. The European Commission acknowledges that suppliers of all sizes are affected by UTPs in the proposal for legislation COM (2018) 173 – but has decided to exclude many players in the supply chain by focusing only on SMEs and farmers despite the integrated nature of the supply chain. It acknowledges the cost to manufacturers in the proposal, and quotes evidence regarding the negative impact of UTPs (pg. 10, explanatory memorandum) - *In 2011, “UTP-related costs amounted to 0.5% of turnover [...] would be the equivalent of EUR 4.4 billion per year of overall food industry turnover”*. There is legislation in 20 Member States in the EU (EC Impact Assessment, April 2018) – none focus on SME-only legislation. This exclusion is contrary to the evidence that exists through the sanctions laid down by the Courts in Member States which prove larger players are subject to UTPs.

## **Buyer power**

High levels of concentration in the grocery retail sector have resulted in cases of an abuse of power between suppliers (food suppliers) and their customers (retailers). This imbalance in bargaining power has led to many manifestly unfair commercial practices such as:

- retrospective unilateral changes to contracts
- late payments / undue delays over minor queries
- demands for unexpected and undue contributions;
- cancellation of promotions at short notice and a lack of willingness to deal with resultant stocks in place.

### **(See Appendix 1 for more detail)**

The key issue the Directive must address is the transfer of excessive risks or unexpected costs from grocery retailers to suppliers. These practices include a failure to respect contractual terms, de-listing threats to obtain unjustified advantages and unilateral deductions off invoices without sound business reasons.

There is buying concentration at the grocery end of the supply chain – retailers are the gatekeepers to the consumer and can use that buying concentration in a grossly unfair trading practices e.g. through de-listing/products removal from shelves. If the retailer delists products, manufacturers lose access to consumers – and likewise, consumers lose on choice.

The imbalance of supply chain power has become stronger with the growth of European retail alliances, which opens the prospect, amongst others, of co-ordinated de-listing across Member States. This could directly impact consumers’ choice of products in several Member States; it could affect the single free market for goods and could negatively affect the revenues of the manufacturers and of their suppliers who are targeted with these UTPs-thus consequently affecting negatively employment at the processor level as the Commission acknowledged already due to the costs of late payments.

## Unfair Trading Practices

In 2011 AIM and FoodDrinkEurope published the findings of a survey of 686 manufacturers (a mix of SMEs and larger players) in 15 European countries on retailers UTPs. The survey found that practically all companies (96.4%) had been exposed to on average six UTPs in 2009. The six most frequent UTPs imposed on producers were:

- Non-respect of contractual terms (84%).
- De-listing threat to obtain unjustified advantages (77%).
- Unilateral deduction on invoices without sound business reasons (63%).
- Paying for no reason (60%).
- Providing payments clearly in no relation to the level of service provided (60%).
- Paying retrospectively for items not foreseen in the contract (55%).

This trend has not changed. A 2017 survey reveals that 97% of brand manufacturers were exposed to UTPs in Europe in 2016, confirming the 2011 report as well as the Commission own surveys The UK Grocery Code Adjudicator following her 2017 annual survey of grocery suppliers<sup>1</sup> identified following as the top priority issues:

- Delays in payments
- Forecasting and promotions
- Payments for better positioning
- Pay to stay

Therefore, the four trading practices in the draft legislation must be extended to reflect the provisions in the Grocery Foods Undertakings Regulations 2016 namely:

- Variation, termination or renewal of grocery goods contracts
- Goods or services from third party
- Non-performance due to factors beyond reasonable control of party to contract
- Forecasts of supply of grocery goods
- Payment from supplier as a condition of stocking, displaying or listing
- Payment terms and conditions
- Promotions
- Payment for marketing costs
- Payment for retention, increased allocation or better positioning of shelf space
- Payment for advertising or display of grocery goods
- Payment for wastage
- Payment for shrinkage

## Enforcement

A fair-trading environment will require effective and efficient enforcement of the rules. Strong enforcement by the enforcement authority is key to success and this includes the ability to proactively investigate compliance e.g. to conduct general supervision of the supply chain, including random requests of information to buyers and suppliers, without it being necessary to open

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<sup>1</sup> <https://www.gov.uk/government/news/tacon-marks-end-of-first-term-with-survey-showing-significant-progress-for-groceries-suppliers>

infringement proceedings. This is essential to the effectiveness of enforcement as is a complaints process for suppliers that ensures anonymity.

## **Conclusions**

The draft directive presents a unique opportunity to create a fair-trading environment in the EU food chain.

The scope of the legislation and the UTPs listed therein is not enough to eliminate the unfair practices which are too prevalent in the supply chain.

For a sustainable and well-functioning supply chain, the scope must include all players, big and small, as well as all products. Only then will the EU have a fair supply chain for our farmers, SMEs, suppliers and consumers.

## **Appendix 1 – Buyer power**

High levels of concentration in the grocery retail sector have resulted in an imbalance of power between suppliers (food suppliers) and their customers (retailers). The picture is relatively similar across Europe. The three largest retailers have more than 50% of the market share in the majority of EU member states and up to 80% market share in some countries. Therefore, across Europe even the largest food companies account for only 1 -2 % of a retailer's business at national level, while conversely a retailer may represent 20 – 30% of those company's business<sup>2</sup>.

- Buyer power
  - “Retailer A has buyer power over Supplier B if a decision to delist B’s product could cause A’s profit to decline by 0.1 per cent and B’s to decline by 10 per cent” (OECD, 1998)<sup>3</sup>
- Economic Dependence
  - A supplier is deemed to be “economically dependent” on one buyer if the latter accounted for more than 22% of the supplier’s total revenues (European Commission - DG COMP, 2000)<sup>4</sup>
  - This imbalance of power should be viewed considering the concentration of the retail market, which further demonstrates just how powerful this position is. This was acknowledged by the German Bundeskartellamt<sup>5</sup> in its Food Sector enquiry published in December 2014 - *“Purchasing volumes have a decisive impact on the negotiated conditions, which is why the structural advantages of large retail companies are also reflected in the purchasing conditions granted to them”* and *“In negotiations with the food industry the leading retailers are largely able to use their strong market positions to their advantage. Consequently, they are in a stronger bargaining position than the manufacturers”*.
  - The UK Competition Commission's presented similar findings in its Supermarket Enquiry (2000)<sup>6</sup>. Grocery retailers' buyer power is linked to relative economic dependence, which has nothing to do with the size of a supplier. It concluded that **even the largest suppliers were economically dependent on large retailers**. In his article on the enquiry, "Exploiting buyer power: lessons from the British grocery trade" (link)<sup>7</sup>, Mr. Dobson states that ***“Even the very largest suppliers usually account for only 1–3 percent of a major grocery retailer’s sales, while losing a single contract with one of the top four grocery retailers in the UK would likely mean a loss of sales for the supplier of around ten times this level (i.e., of between 10 and 30 percent) if it cannot find alternative routes to market.”*** (p. 534 and footnote 17)
  - A French government enquiry from 31 March 2015 stated: *“The data collected, ... are indicative of an imbalance in the forces in this sector: the share of the main*

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<sup>2</sup> CIAA Competitiveness Report 2010

<sup>3</sup> Buying Power of Multiproduct Retailers, OECD Competition Committee, 1998

<sup>4</sup> Case No COMP/M.1684, Carrefour/Promodès Art. 6 & Art. 9 Decisions (Jan. 2000). The threshold was chosen as survey evidence indicated that this was the most suppliers could afford to lose without risking bankruptcy.

<sup>5</sup> Summary of the Final Report of the Sector Inquiry into the food retail sector, 24/09/2014:

[https://www.bundeskartellamt.de/SharedDocs/Publikation/EN/Sector%20Inquiries/Summary\\_Sector\\_Inquiry\\_food\\_retail\\_sector.pdf?\\_\\_blob=publicationFile&v=3](https://www.bundeskartellamt.de/SharedDocs/Publikation/EN/Sector%20Inquiries/Summary_Sector_Inquiry_food_retail_sector.pdf?__blob=publicationFile&v=3)

<sup>6</sup> <http://researchbriefings.files.parliament.uk/documents/SN03653/SN03653.pdf>

<sup>7</sup> <http://www.antitrustinstitute.org/files/384.pdf>

*retailers, or retail alliances, in the turnover of the suppliers interviewed would be on average in the order of 20% ... In comparison, in several product markets, even the most important suppliers represent only a small share of the overall turnover of retailers.”*

- Unfair Trading Practices
  - “practices which distort the relationship between suppliers and retailers should be discouraged. This is for example the case for late payments, unjustified or excessive fees paid by suppliers for services provided by retailers or tempting consumers with misleading offers. In this context, the introduction of Codes of conduct would be welcome as an expression of retailers' social responsibility and national Codes of conduct should be reviewed.” (European Commission, 2008)<sup>8</sup>
  - “One of the features that adversely affected competition in the market was the exercise of buyer power by certain grocery retailers with respect to their suppliers of groceries, through the adoption of supply chain practices that transfer excessive risks and unexpected costs to those suppliers.” (UK Competition Commission)<sup>9</sup>
  - Significant imbalances in bargaining power between contracting parties are a common occurrence.....this asymmetry in bargaining power may lead to unfair trading practices.....for example, late payments, unilateral changes in contracts, ad-hoc changes to contractual terms, upfront payments as entry fees to negotiations...” (European Commission, 2009)<sup>10</sup>

This imbalance in bargaining power has led to the proliferation of many manifestly unfair commercial practices such as retrospective changes to contracts, late payments and demands for unexpected and undue contributions.

At the EU Council of Agriculture Ministers in May 2009, Minister for Agriculture, Fisheries and Food, Brendan Smith T.D. and other EU Ministers for Agriculture highlighted the difficulties caused in the food sector by the control multiples had on the food supply chain. Minister Smith said<sup>11</sup> “Underlying this recent European debate is the increasing concentration of retail power in the hands of a few large supermarket chains. This is an international phenomenon that fundamentally changes the balance of market negotiating power in the food chain. And this is one factor, although not the only one, behind the declining share of retail prices which is passed back to producers. While fully recognising that retailers must strike a reasonable balance between granting price reductions to consumers and giving a fair return to suppliers and producers, this should not be done at the expense of a viable European agri-food sector”.

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<sup>8</sup> COM (2008) 821 Food Prices in Europe

<sup>9</sup> The Groceries (Supply Chain Practices) Market Investigation Order 2009

<sup>10</sup> COM (2009) 591 A better functioning food supply chain in Europe

<sup>11</sup> Press Release, Department of Agriculture, Fisheries and Food, May 27<sup>th</sup> 2009

