CRITICAL ASSESSMENT OF DG COMP CHIEF ECONOMIST'S CONTRIBUTION TO THE PROPOSED DIRECTIVE ON UTPS IN THE FOOD SUPPLY CHAIN[1]

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Executive Summary

The Chief Economist's views

- He admits that competition law is not suited to deal with buyers' UTPs in the food supply chain and regulation is necessary.
- He suggests a general approach to identifying UTPs: trading practices that are previously agreed between the parties (ex-ante) should generally be allowed, whereas trading practices that alter the terms of an existing contract for the benefit of an stronger party should generally not be allowed.
- He endorses the proposed UTPs but warns against the risks of (1) regulating efficiency-enhancing practices, most notably ex-ante hard bargaining on purchase prices, (2) extending the protection to large suppliers, (3) adopting general prohibitions.

Critical Assessment

- The failure of competition laws to address UTPs by non-dominant operators, suppliers' fear factor (in itself evidence of buyers' superior bargaining power) and the failure of competition rules to address buyer power and harm to innovation call for a comprehensive regulatory framework, not a limited one.
- The Chief Economist's ex-ante/ex-post approach is fatally flawed because it misses entirely the coercion factor associated with superior bargaining power and mixes the economic gain of the beneficiary with aggregate efficiency/welfare considerations. Indeed, he concedes that the blacklisted UTPs in Article 3.1 of the Proposed Directive are unfair and can lead to inefficiencies even though they can be ex-ante agreed. However, the same unfairness and efficiency consideration apply to the UTPs in Article

[1] Commission staff working document impact assessment -Initiative to improve the food supply chain (unfair trading practices), Accompanying the document Proposal for a Directive of the European parliament and of the Council on unfair trading practices in business-to-business relationships in the food supply chain, SWD/2018/092 final - 2018/082 (COD), Annex H - "Economic Impact of unfair trading practices regulation in the food supply chain", prepared by the Chief Economist of DG Comp, pp. 260-268 (hereinafter, "Opinion of DG COMP's Chief Economist").

3.2 and the Commission's Explanatory Memorandum assumes that payments must respond "to objective and reasonable cost estimates". For example, the agreed return of unsold items may afford the buyer a short-term economic gain but transfers all the retailing risk to the supplier, undermining its productive efficiency, and even undermines the retailer's incentive to compete. The concept of "unfair practice" defined and developed for many years in the Member States is the right approach and the efficiency considerations that should guide its interpretation are those reflecting the society welfare and not those of the party requesting and benefitting from a trade practice. For example, a prior agreement allowing the buyer to use the trade secrets of its suppliers to compete against them may be efficient for one party (and even for both, if the access to the buyer depends on accepting this clause) but would fail both a society/consumer welfare and a fairness test: the society is better off if companies face the right innovation incentives – the supplier will innovate without the fear of being copycatted and the buyer will be pushed to innovate its private label.

- The Chief Economist's three unsubstantiated concerns are contradicted by the substantial experience gained in the 20 Member States that have regulated UTPs for many years. These UTPs also include general prohibitions (e.g., in France), and protect all suppliers, regardless of their size, without preventing ex-ante hard bargaining on purchase prices. Understandably, the Commission's Joint Research Centre has evidenced that comprehensive laws on UTPs protecting all suppliers have no or deflationary impact on retail prices. Moreover, the regulation of UTPs also produces positive effects on upstream innovation, quality and volume. Shockingly, DG COMP's views would have afforded impunity to the prohibited UTPs of Edeka against 500 of its suppliers in Germany, DIA and Eroski against 45 of its suppliers in Spain, Tesco against hundreds of its suppliers in the UK and several retailers against dozens of its suppliers in France. Last, but not least, these UTPs on manufacturing companies stress the supply chain up to the primary producers according to a basic principle of corporate management: if sales margins go down, the procurement costs must follow suit. The Chief Economist seems to imply that this principle applies to all economic sectors except to the food supply chain.

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1. The Chief Economist rightly admits that competition law cannot address UTPs because no buyer holds a dominant position in the procurement markets across the food

supply chain and, therefore, regulation of UTPs is justified[2]. Two other factors call for regulation in the food supply chain. First, suppliers' fear factor (fear of losing a client following a complaint or legal action) not only evidences buyers' superior bargaining power, it also justifies the existence of independent authorities with comprehensive powers. Second, competition rules have consistently failed to address abuse of buyer power and harm to innovation[3], despite recent attempts to advance theories of harm to innovation in the context of merger control, not applicable to unilateral practices[4]. Not surprisingly, no competition authority in the EU has ever fined a buyer under traditional competition rules for committing UTPs against its suppliers in the food supply chain.

2. The Chief Economist exposes the principle that regulated UTPs should tackle economically inefficient practices, without preventing fair negotiation and the exercise of bargaining power to obtain better terms such as lower purchasing prices[5]. Then he

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[2] Opinion of DG COMP's Chief Economist, p. 260: "*Competition policy can help to mitigate (some of) these problems only in few cases. Indeed competition law only deals with situations where a particular seller/buyer possesses a "dominant position" in that it has some power over buyers/suppliers in general, and not only over one or few particular firm(s), and where there are likely anti-competitive effects. Therefore, unequal bargaining power and resulting imbalances in trading relationships rarely imply an infringement of competition law.468 Such issues may be, where appropriate, addressed by other policy tools, such as contract and unfair commercial practices law.469 General contract law may not be enforceable in a number of situations. In such situations, a well-targeted regulation of certain trading practices aiming at ensuring fairness between actors in the food supply chain could help to resolve specific issues*."

[3] See, as an example of the growing criticism against the price-centric focus of competition laws, Kevin Caves and Hal Singer, "*When the Econometrician Shrugged: Identifying and Plugging Gaps in the Consumer Welfare Standard*" (June 29, 2018), George Mason Law Review, 2018, available at SSRN: https://ssrn.com/abstract=3205518

[4] DG COMP's novel focus on harm to innovation in the Dow/Dupont case has been criticised by mainstream doctrine, despite the efforts of the Chief Economist to provide theoretical support for it. See Giulio Federico, Gregor Langus and Tommaso Valletti, "*Horizontal Mergers and Product Innovation*" (February 26, 2018), available at SSRN: https://ssrn.com/abstract=2999178 or http://dx.doi.org/10.2139/ssrn.2999178. The theoretical model exposed by the Chief Economist rests on the suppression of innovation efforts of two firms post-merger, therefore, it does not apply to UTPs by a downstream buyer and competitor that undermine the innovation incentives and outcomes of an upstream supplier.

[5] Opinion of DG COMP's Chief Economist, p. 261:"*As mentioned by Swinnen and Vandervelde, it is important to "clearly define UTPs and provide an exhaustive list of what can be considered as such. "The main risk in having a broad or vague definition of UTPs, according to Richard Sexton, is that it*

proposes a novel flawed evaluation approach that distinguishes between previously agreed (ex ante) practices, which "*typically lead to efficiencies for both parties*" and those that occur subsequently (ex-post), which "*reduce or eliminate the efficiencies for the weaker party*"[6]. This approach misses entirely the (economic) coercion factor associated with superior bargaining power (i.e., coerced agreements) and mixes the economic gain of the beneficiary with aggregate efficiency/welfare considerations[7]. Indeed, he concedes that the blacklisted UTPs in Article 3.1 of the Proposed Directive are unfair and can lead to inefficiencies even though they are agreed[8]. However, the same unfairness and efficiency consideration apply to the UTPs in Article 3.2 and would call for additional controls to avoid coerced agreements. For example, the coerced agreement on return of unsold items may afford the buyer a short-term economic gain but transfers all the retailing risk to the supplier and undermines the retailers' incentive to compete. The same goes for the coerced agreement on disproportionate payments to the buyer for maybe unwanted services. Indeed, the Commission's Explanatory Memorandum assumed that agreed payments under Article 3.2 should respond to objective and reasonable cost estimates, a restriction that does not

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could prevent efficiency-enhancing behaviours and commercial practices from taking place. (...). This means that the aim of regulation of UTPs should be to prevent trading partners with strong bargaining power to engage into some clearly identified "unfair" practices, but not to prevent these trading partners from exercising their bargaining power in a "fair" manner when negotiating, e.g. obtain low purchase prices."

6 Opinion of DG COMP's Chief Economist, pp. 261-262: *"This Annex presents a brief summary of the economic impact of regulating UTPs in the food supply chain, and introduces an approach that in general distinguishes practices agreed between parties ex-ante (i.e. before the commercial agreement is concluded, or before sales are realised) and those which occur ex-post (after the commercial agreement has been concluded or sales have materialised)."*

7 Frédéric Jenny, "*The "Coming Out" of Abuse of Superior Bargaining Power in the Antitrust World*", Paris, July 1st 2008 builds on the works of the International competition Network in this field and identifies coercion as the critical element of the abuse of superior bargaining power. Mr. Jenny is Professor of Economics at ESSEC Business School in Paris, Judge at the Supreme Court of France (Cour de Cassation) and Chairman of the OECD Competition Law and Policy Committee.

8 Opinion of DG COMP's Chief Economist, p. 262: *"This being said, there are certain well-defined exceptions to this general rule regarding the presumed lawfulness of ex-ante agreed conditions. Certain contractual provisions or trading conditions agreed ex-ante could still be regarded as unlawful or unfair where it is generally accepted that they do not lead to efficiencies for both parties in the transaction.".*

seem to be reflected in the wording of Article 3.2[9]. This is why Article 3.2 may open the door to agreed practices that are unfair for one party and socially undesirable[10]. For example, a prior agreement allowing the buyer to use the trade secrets of its suppliers to compete against them may be efficient for one party (and even for both, if the access to the buyer depends on accepting this clause) but would fail both a society/consumer welfare and a fairness test: the society is better off if companies face the right innovation incentives – the supplier will innovate without the fear of being copycatted and the buyer will be pushed to innovate its private label.

Overall, the concept of "unfair practice" defined and developed for many years in the Member States is the right approach and the efficiency considerations that should guide its interpretation are those reflecting the society welfare and not those of the party requesting and benefitting from a trade practice. Indeed, even the Chief Economist concludes that the prohibited UTPs in Articles 3.1 and 3.2 of the Proposed Directive enhance efficiency without preventing buyers from negotiating and agreeing upfront the lowest possible purchasing prices[11]. However, his suggested approach is in open

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[9] Commission's Explanatory Memorandum to the Directive: "*This second group of UTPs includes the return of unsold or wasted products. Payments for stocking, displaying or listing food products of the supplier may yield efficiencies in favour of both contract partners and thus lead to win-win situations. This also applies to promotion and marketing activities. The buyer must provide the supplier with a payment estimate if so requested. In the case of marketing and stocking, displaying or listing activities the buyer must - on request - also provide the supplier with a cost estimate. They are acceptable if agreed by the parties and if objective and reasonable cost estimates are at the basis of the payment for stocking and listing products. Suppliers' contributions to the promotion of products or the buyers' marketing can also be efficient if agreed by the parties.*"

[10] Indeed, the definition of abuse of superior bargaining power offered by the International Competition Network focuses on the unfairness of the practice, regardless of its ex-ante or ex-post agreed nature. See ICN Special Program for Kyoto Annual Conference, "Report on Abuse of Superior Bargaining Position", Prepared by Task Force for Abuse of Superior Bargaining Position, footnote 1: "*ASBP here typically includes, but is not limited to, a situation in which a party makes use of its superior bargaining position relative to another party with whom it maintains a continuous business relationship to take any act such as to unjustly, in light of normal business practices, cause the other party to provide money, service or other economic benefits*".

[11] Opinion of DG COMP's Chief Economist, section 3.4 (Application to specific UTPs), pp. 266-267.

contradiction with the worldwide consensus on UTP legislation in this field and even the works of the International Competition Network[12].

3. The Chief Economist states that "*there may be questions about the frontier between "ex-post" and "ex-ante" in the case, for instance, of regular negotiations or arrangements between two trading partners*" and wrongly argues that delisting under an existing contract in order to obtain better terms in a future contract should be considered an ex-ante practice[13]. He overlooks that this practice is inefficient and substantially alters the balance of rights and obligations of the existing contract. It is inefficient for the supplier because the delisting is unrelated to the economic performance of the product under the applicable trading terms, and occurs at short or no notice depriving the supplier of the chance to adapt its production and commercialisation process. Indeed, the goal of the practice is to inflict a sudden and unbearable economic harm to the supplier replacing the natural bargaining process that would occur in the future. It is inefficient for customers who were buying the product and may find it delisted or out of stock in some shops. Furthermore, it alters the balance of the existing contract because even if no fixed volume is negotiated, the services paid to the retailer upfront and their amount depend on turnover expectations (regularly discussed and to some extent agreed between the parties) than cannot anticipate an inefficient delisting. This, in turn, hinders

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[12] Frédéric Jenny, "The "Coming Out" of Abuse of Superior Bargaining Power in the Antitrust World", Paris, July 1st 2008: "*Even though competition authorities in developed countries have traditionally considered that they should not deal with problems of " abuse of dependency" or "abuse of superior bargaining power" because such practices had a distributional effect and should, therefore, be handled through civil courts, one must acknowledge that coercive practices may also have at least indirect efficiency effects, both positive in the short run and negative in the longer run, and that in certain circumstances civil courts may not be in the best position to handle claims of coercive practices. (...). The only sensible response to questions raised by abuses of superior bargaining power seems to be that it is up to public authorities in each country, depending on their perception of the extent of such practices and the importance of externalities imposed by coercive practices and on their knowledge of the characteristics of the legal system of their country, to decide whether or not public enforcement against such practices is warranted and whether the competition authority should deal with those practices."*

[13] Opinion of DG COMP's Chief Economist, p. 266: "*This is the case, for instance, when a large customer uses "delisting" as part of its recurring negotiations with a large manufacturer, such practice would typically be categorized as an ex-ante practice, as this corresponds to the case where the retailer simply stops ordering products from the manufacturer and thus affects future orders. Hence, this should generally be allowed.484*".

future deals due to expected contract breaches. Even the competition authorities gathered at the International Competition Network discussed a similar case provided as an example of an abuse of superior bargaining power[14].

4. The Chief Economist wrongly opposes the regulation of trading relationships between large manufacturers and large retailers on two unsubstantiated claims: "*because of their broad impact on the market and, ultimately, on consumer prices*" and because a large supplier "*is unlikely to share with its own suppliers the extra benefits it would obtain from such regulation*"[15]. He is wrong for the following 8 reasons:

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[14] Frédéric Jenny, "The "Coming Out" of Abuse of Superior Bargaining Power in the Antitrust World", Paris, July 1st 2008: "It is interesting to relate this discussion of what a threat is and what coercion is to the hypotheticals which were chosen by the organizers of a panel on abuse of superior bargaining power which was held during the 2008 annual ICN conference in Kyoto4. Those hypotheticals were simplified renditions of cases which had been dealt with by the Japanese competition authority (JFTC). *In the first hypothetical case, small suppliers were asked by a large retailer to dispatch their employees to assist the retailer in product display and routine stocktaking, at the supplier's cost and without any contract, and/or they were asked to offer monetary contributions towards the opening of new stores by the retailer.*

Although in this case the precise nature of the threat was not spelled out in the hypotheticals, we can assume that the nature of the offer of the retailer was the following:

R (the retailer) wants S (the suppliers) to contribute financially to the cost of displaying the products and / or the cost of opening a new store. R communicates a conditional proposal:

A) If S does not contribute financially, R will cease (partially or completely) to carry S's products on its shelves.

B) If S does contribute, R will not cease to carry S's products

Let us then assume that the supplier prefers not to be delisted and therefore chooses to make a financial contribution. This means that the least preferred alternative for the supplier is A. In order to decide whether the supplier(s) have been given a proposal or a threat (and therefore have been coerced into choosing B), we must ask whether the least preferred alternative (A) would have made tehm worse off compared to what would have been normal (or compared to what would have happened had the offer not existed). The answer to this question is clearly positive. The suppliers would not have expected to be delisted in normal circumstances and the prospect of being eliminated from the shelves of R makes them worse off than they would have been in "normal" circumstances.

[15] Opinion of the Chief Economist of DG COMP, pp. 262-263: *"Moreover, there can be unintended negative consequences of regulating practices in the food supply chain. This concerns notably regulating the trading relationships between (mostly brand) manufacturers holding a significant share of the market of the sales of food products in a particular product category in a given Member State (hereafter designated in a simplified way as "large manufacturers") and their "large customers" (e.g.*

4.1 He seems to assume wrongly that a high market share in a product market affords the supplier a bargaining power comparable to that of a retailer with a high retail market share. This assumption was first made in the "*The economic impact of choice and innovation in the EU food sector*" study, commissioned by DG COMP in 2014 (DG COMP's Innovation Study)". Leaving aside that the Innovation Study did not cover highly concentrated retail markets, that it wrongly excluded private labels from the product market (thereby artificially inflating the market share of branded suppliers) and it also wrongly excluded retail alliances from retail market shares (three flaws that fatally biased the results in favour of retailers), the fact is that economic theory (e.g., Nash Bargaining Theory) and competition authorities (even DG COMP itself, e.g., merger cases such as Rewe/Meinl and Carrefour/Promodès) hold that superior bargaining power in a trading relationship reflects the higher outside/replacement options (lower opportunity cost of no deal) enjoyed by one of the trading partners[16].

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modern retailers holding a significant share of the food retail sales in a given Member State). Regulating commercial transactions between such large players could reduce the pressure that large customers can exert on large manufacturers to reduce their margins and imply significant market disturbance because of their broad impact on the market and, ultimately, on consumer prices.475 Besides, it is not obvious that farmers or other parties higher up in the supply chain would benefit from a regulation of UTPs that would give large processors or manufacturers greater margins. A large manufacturer that would leverage a regulation of UTPs to pressurize the retailers to increase prices at which retailers buy from the manufacturer has no obligation or incentives and is unlikely to share with its own suppliers the extra benefits it would obtain from such regulation."

[16] The link of superior bargaining power to the outside options available to each trading party is unanimous whereas the product market share of each trading party has never been mentioned. See, for example, OECD, "Monopsony and Buyer Power", 2008, Background Note, p.22: *"Bargaining is likely to be over the incremental surplus available to a buyer and seller. Incremental surplus is the gain over and above the gains the buyer and seller could realize relative to their outside options. The greater the effectiveness of a buyer at bargaining, the larger the buyer's outside option, and the smaller the outside option of the seller, the greater the share of incremental surplus captured by the buyer. The value of the buyer's outside option depends on its ability and willingness to substitute to alternative suppliers. Similarly, the value of the seller's outside option depends on its ability and willingness to substitute to alternative buyers. A buyer will have substantial buying power if (i) it can easily switch to alternative suppliers, sponsor new entry or self supply without incurring substantial sunk costs and (ii) it is a gateway to the downstream market. In the conception of the buyer as a gate-keeper and the role of market power downstream, it is useful to recognize that the buyer is providing ―distribution services‖ to the seller."* Many authors quote a preliminary draft Background Note of the OECD Secretariat for the OECD

4.2 Retailers have become gatekeepers and hold more bargaining power than even their largest suppliers because of their multi-product business, the multi-product nature of consumers' purchase and their one-stop shopping pattern. Each large retailers often accounts for more than 10% of their suppliers' sales whereas each supplier accounts for 0-2% of the retailer's sales. Even so called must stock items (a category which a Bundeskartellamt study found to comprise barely 6% of the goods[17]) are confronted with "must be" retailers and the risk of losing and not recouping significant sales if partial/temporary delisting occurs. This bargaining asymmetry explains the growing number of national cases against retailers for imposing UTPs on all their suppliers, including the largest ones (e.g., the *Edeka* case in Germany[18], the *Dia/Eroski* case in Spain[19], the *Tesko* case in the UK[20] and several judgments against retailers in France[21]).

Roundtable Buyer Power of Large Scale Multiproduct Retailers: "*A retailer is defined to have buyer power if, in relation to at least one supplier, it can credibly threaten to impose a long term opportunity cost (i.e. harm or withheld benefit) which, were the threat carried out, would be significantly disproportionate to any resulting long term opportunity cost to itself. By disproportionate, we intend a difference in relative rather than absolute opportunity cost, e.g. Retailer A has buyer power over Supplier B if a decision to delist B's products would cause A's profit to decline by 0.1 percent and B's to decline by 10 percent*".

[17] Bundeskartellamt, "Summary of the Final Report of the Sector Inquiry into the food retail sector", courtesy translation, http://www.bundeskartellamt.de/SharedDocs/Publikation/EN/Sector%20Inquiries/Summary_Sector_Inquiry_food_retail_sector.pdf?__blob=publicationFile&v=3See%20full%20report%20(only%20available%20in%20German, p.11: *"One should take into account, however, that only a few products have the potential to be considered so-called "must-have" items. Only 6% of the products from the representative sample were identified as strong branded goods with a "must-have character""*

[18] See press release of the German competition authority (Bundeskartellamt), "*Bundeskartellamt takes decision of principle in food retail case - EDEKA's demands on suppliers were abusive*", 3.7.2014, https://www.bundeskartellamt.de/SharedDocs/Meldung/EN/Pressemitteilungen/2014/03_07_2014_edeka.html?nn=3591568, confirmed by the Federal Court in 2018.

[19] Both retailers were sanctioned for jointly committing UTPs prohibited by the Spanish Food Chain Law (unpublished decision), see press article from El Economista referring to the infringement, "*La guerra con los proveedores obliga a Dia y Eroski a dejar de comprar juntos*", 12.4.2018, https://www.eleconomista.es/empresas-finanzas/noticias/9068070/04/18/La-guerra-con-los-proveedores-obliga-a-Dia-y-Eroski-a-dejar-de-comprar-juntos.html

[20] Groceries Code Adjudicator Investigation into Tesco plc, 26 January 2016, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/494840/GCA_Tesco_plc_final_report_26012016_-_version_for_download.pdf

4.3 The Innovation Study in 2014 and the Chief Economist now overlook the role that retailers' private labels and retail alliances (often also focused on private label sourcing) play in promoting bargaining power and increasing retailers' incentives to engage in UTPs against brand manufacturers (the incentives to extract rents from a supplier are reinforced with the incentives to expel a competitor from the market). The conventional wisdom among competition authorities that a buyer will not abuse so much its supplier so as to expel it from the market and lose its supply was never solid in light of the presence of alternative suppliers but definitely collapsed several years ago when leading retailers launched their own competing grocery labels.

4.4 The Chief Economist's unsupported claim that the protection of large suppliers against UTPs will reduce the pressure that large customers can exert on large manufacturers to reduce their margins and ultimately lead to higher retail prices flagrantly contradicts its own approach to the assessment of justified/unjustified UTPs. The proposed UTPs, as well as those in force in the Member States address unfair/inefficient practices and do not prevent retailers from exercising hard bargaining and negotiating the lowest prices ex-ante from suppliers, irrespective of their size. The Chief Economist's claim obviates all the negative effects of the UTPs in the food supply chain, regardless of the suppliers affected, identified by the Bundeskartellamt in the Edeka case[22].

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[21] See, for example, Tribunal de commerce de Créteil, System U contre Ministre de l'Économie, 24 octobre 2006, upheld by the Cour d'Appel de Paris: https://groupes.renater.fr/sympa/d_read/creda-concurrence/CaP/29juin2016/systemeU.pdf; and Cour d'Appel de Paris, 1 Juillet 2015, Monsieur le Ministre de l'Economie, du Redressement Productif et du Numérique c. Société GALEC Société Coopérative Groupement d'Achats des Centres LECLERC, https://groupes.renater.fr/sympa/d_read/creda-concurrence/CaP/1juillet2015/Galec.pdf

[22] Bundeskartellamt, Case summary, "Food retailer EDEKA violates prohibition to demand unjustified benefits from dependent suppliers", 28.8.2018, https://www.bundeskartellamt.de/SharedDocs/Entscheidung/EN/Fallberichte/Missbrauchsaufsicht/2014/B2-52-14.pdf?__blob=publicationFile&v=3: *"In the Bundeskartellamt's view the current proceedings help to define the line between (admissible) hard bargaining on the one hand and the abusive exploitation of buyer power on the other. In view of the increasing concentration in the German food retail sector and the resulting pooling of demand for branded products in the hands of a few large food retailers it is mandatory that the prohibition of inducing dependent suppliers to grant benefits without an objective justification (so-called "Anzapfverbot") be rigorously enforced. For the assessment of whether the relevant criteria "dependent" and "benefit without objective justification" are fulfilled, the individual*

4.5 The Chief Economist's stance is not only contradicted by his endorsement of the proposed UTPs on efficiency grounds, but also by the econometric evidence found by the economists of the European Commission's Joint Research Centre, duly reported in Annex C.6 (Rules on UTPs and price evolution, pp. 111-113) of the Impact Assessment[23]: Member States with more stringent rules have enjoyed lower food price increases than Member States with less stringent rules on UTPs in the 2005-2016 period. The Chief Economist has neglected this evidence even though he claims to have built his note on the Technical Report of the Joint Research Centre, whose authors also authored Annex C.6. The 20 Member States which have regulated UTPs in the food supply chain to a larger or lesser extent have not excluded large suppliers from their scope. Therefore, evidence at the national level confirms that stringent UTP rules

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market conditions of the markets affected need to be taken into account. Abusively induced benefits not only harm the suppliers directly affected but are also harmful to small and mediumsized food retail companies. Their conditions are further weakened in comparison to their large competitors and they are unlikely to be granted better conditions in the future by their suppliers (who are afraid that in the case of a subsequent takeover they will have to also grant these conditions to the acquiring company). Consumers also suffer in the medium and long term from lower product quality, a decline in innovation activity, less product diversity and the risk of price increases caused by lower competition intensity in the German food retail sector. Distinguishing between admissible hard bargaining and illegal demands by powerful companies is also an issue of major current importance for other EU Member States. There are various European initiatives on this subject".

[23] Commission staff working document impact assessment, Annex C.6 - Rules on UTPs and price evolution, pp. 111-113: *"One concern about regulating UTPs that is often referred to is that they could result in increased prices for consumers, in particular if they result in legislating practices which may result in efficiency gains at the chain level. Other views are that they could lead to efficiency gains and lower consumer prices if such regulation results in the building of trust and decreased transaction costs. Swinnen and Vandevelde (2017)367 group Member States based on how they have undertaken action to combat UTPs by considering two criteria (i) the type of legislation used (legal treatment of UTPs) and (ii) the coverage of UTPs in their legislation. Then using these two criteria, they develop a ranking of MS on the base of the stringency of their UTP regulatory framework. A preliminary work by the JRC compared this ranking of Member States with the evolution of (deflated) consumer price for food for 2010-2016 (see Figure 11). The comparison shows that the correlation between the stringency of UTP rules (1) and consumer food prices is weak (Member States with the more stringent rules on the left in figure 10). Many factors other than rules on UTPs are at play in the determination of the evolution of food consumer prices. If anything, the poor correlation shows that Member States with more stringent rules seem to enjoyed lower food price increases than Member States with less stringent UTP rules. There are similar results for longer periods (2005-2016; see figure 11).*

protecting all suppliers have no or a deflationary impact on retail prices. Furthermore, some Member States (e.g., France) have enforced successfully an overarching UTP based on general principles such as "the imbalance of contractual rights and obligations" (other similar principle being "the transfer of economic risks inherent to the buyer"). The Chief Economist's claim that this "rule of reason" approach raises the risk of over-enforcement[24] is shocking because it is the prevailing principle in competition law enforcement. Ultimately, the courts must rule on the legality of UTPs (as they do on competition law cases), guaranteeing legal certainty and defence rights.

4.6 The Chief Economist's price-centric claim is not only rebutted by empiric evidence but also incomplete because omits the critical role of product innovation in this sector and the damage to all suppliers' innovative efforts that these UTPs may cause. DG COMP's Innovation Study revealed a decline in innovation across the assessed retail markets despite the overly broad definition of innovation used, that included copycat products (i.e., not first-to-market products)[25]. Furthermore, the study also found a progressive negative effect of private labels on innovation and choice once a certain combined market share threshold had been reached in the market (approximately 35%)[26]. These findings should have been sufficient to justify the protection of all suppliers and the inclusion of specific per se/objective UTPs such as the unfair use by retailers of the trade secrets of their suppliers. All food retailers in the world receive advance notice of their suppliers innovation launches and all the accompanying trade secrets and not a single supplier has shown sufficient bargaining power to protect its trade secrets and, conversely, all the retailers have relied on their bargaining power to

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[24] Opinion of the Chief Economist of DG COMP, pp. 268: *"In contrast, other approaches such as a "rule-of-reason" as advocated by Sexton could prove more complex and challenging to implement in practice. Such rule-of-reason type of approach may lead to over-enforcement of the regulation and risks affecting efficiencies linked to commercial transactions in the supply chain.485"*

[25] Commission press release, "Commission publishes results of retail food study", 2 October 2014, http://europa.eu/rapid/press-release_IP-14-1080_en.htm: "*However, the number of innovations reaching the consumer each year has decreased since 2008 by 6.5%. In 2004 innovation essentially consisted of new-to-the-world products and range extensions (e.g. new flavour), whereas in 2012, roughly a third of all innovations merely concerned the packaging of a product".*

[26] Commission press release, "Commission publishes results of retail food study", 2 October 2014: "*Moreover, the share of private labels in the assortment does not have a significant impact until it reaches a high level (depending on the category) at which it may become detrimental for choice and innovation*".

avoid adopting any internal measure designed to prevent the spillover of these trade secrets to their private label activities.

4.7 The Chief Economist's claim that the protection of large suppliers will not benefit farmers is unsupported by any evidence and runs against the most basic principle of business management. A large supplier exposed to an inefficient UTPs in the food supply chain reacts as any other economic operator experiencing a turnover/margin reduction. It will bargain even harder with its input suppliers, presumably less powerful, to reduce its procurement costs. The dairy sector exemplifies this basic principle: retailers have sold processed milk at low prices/below cost as a traffic builder and this has hard-pressed procurement prices up the milk supply chain to the farmers. It is shocking that the Chief Economist relies on the wrong counterfactual (the effects of an increase of margins instead of a reduction of margins) to try to distance himself from this basic principle and claims DG COMP has made in other scenarios that required regulation of trading practices. For example, Regulation 2015/751 of the European Parliament and of the Council of 29 April 2015 on interchange fees for card-based payment transactions capped these fees because merchants passed them on to consumers[27].

4.8 Overall, EU regulatory measures addressing fair dealing in different economic sectors have never excluded large operators from their scope. This is coherent with the principle of equal treatment and DG COMP has never voiced concerns. Computer Reservation Systems (now known as GDS), credit card networks, Internet access providers and financial institutions are subject to fair dealing rules in their trading relationships with other operators regardless of their size. The proposed Regulation on promoting fairness and transparency for business users of online intermediation services does not limit the scope of the protected business users either.

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[27] Commission press release, "Antitrust: Regulation on Interchange Fees", 9 June 2016, http://europa.eu/rapid/press-release_MEMO-16-2162_en.htm: "*If a retailer refuses commonly-used cards, there is a risk that consumers would choose to go to its competitors. Individual retailers tend thus to accept high costs for card payments to keep and grow their sales. Retailers recover higher costs due to ever increasing interchange fees by increasing retail prices. As a result, the prices increase for all consumers, including those who pay cash or use cheaper payment cards, because the higher fees of more expensive cards are spread out and passed on to all. The Regulation on interchange fees for card-based payment transactions aims at changing this situation to the benefit of retailers and consumers.*"