# Compecon - Competition & Regulatory Economics E-Zine.

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**Editorial.**

Welcome to the latest issue of Compecon's Competition and Regulatory Economics EZine. The E-Zine provides regular updates on economic aspects of competition and regulation. In this issue we consider some economic aspects of the ECJ's judgment of 4th March which ruled that Ireland's minimum price regime for tobacco products was in breach of EU law. Our second article analyses the report of the Oireachtas Joint Committee on Enterprise, Trade and Employment on supplier-retailer relationships in the grocery sector. Our third article reviews the UK OFT's decision fining Royal Bank of Scotland £28.6 m for information sharing with its competitors.

In our January issue we reported on the CER's Consultation Paper on the possible removal of regulatory controls on ESB prices to households and SMEs and highlighted evidence of significant inefficiencies in the Dublin Bus route network in an article reviewing the Public Transport Regulation Act, 2009. The CER announced on 21st April that price controls will remain in the case of households until the ESB's market share falls to 60%. The ESB will also be required to re-brand its supply business. On 22nd April Dublin Bus announced a major reform of its route network.

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# ECJ Strikes Down Ireland's Minimum Price Regime for Tobacco.

**Introduction.**

On 4th March the European Court of Justice (ECJ) ruled that Irish legislation fixing minimum retail prices for tobacco products was in breach of EU law. The judgment triggered calls by anti-smoking groups for the Government to increase taxes on tobacco products to keep cigarette prices high in order to discouraging smoking. The Labour Party's health spokesperson, Ms Jan O'Sullivan TD was quoted as describing the Court's judgment as a *"prime example of competition law gone mad"*. Ms. O'Sullivan also reportedly stated:

> *"Competition law is all well and good, but when it starts to get in the way of reasonable measures, which are put in place in the greater public interest, it is clear that something has gone wrong."*[1]

The case did not actually involve the competition rules of the EU Treaty but involved a breach of EU Directive 95/59/EC which *inter alia* provides that manufacturers and importers of manufactured tobacco products must be free to determine the maximum retail selling prices of their products. This perhaps raises the question of why there is specific EU legislation guaranteeing such a right in the case of a particular industry.

**The Relevant Legislation**

Section 2(1) of the Tobacco Products (Control of Advertising, Sponsorship and Sales Promotion) Act 1978, provided that the Minister for Health could make regulations for the control and regulation of advertising of tobacco products, sponsorship and any other activities which are intended or are likely to promote the sales of tobacco products. Section 2(2)(i) provided that such regulations could provide for *"the prohibition of the sale of tobacco products at prices which are so much lower than those at which tobacco products of a similar type or character are at the material time being sold that the sale at the lower prices constitutes in the opinion of the Minister a sales promotion device"*.

Article 16(1) of the Tobacco Products (Control of Advertising, Sponsorship and Sales Promotion) Regulations 1991, provided:

> *"A person shall not sell by retail a tobacco product of a particular brand at a price lower than that otherwise obtaining for that brand."*[2]

Subsections 2 prohibited the selling of tobacco brands at a price lower than otherwise obtaining for that brand by making available to persons a coupon or similar document. Section 3 prohibited offers of vouchers, trading stamps, coupons, premia, tokens or gifts (including gifts of tobacco products) in relation to the sale of tobacco products.

Article 17 of the 1991 regulations provided:

> *"1. A person shall not sell by retail a tobacco product at a price as respects which the Minister…has formed an*

*opinion that the sale of that product at such a price constitutes a sales promotion device."*

In 1986, the Minister for Health issued a Memorandum of Clarification concerning the previous 1986 regulations which provided that:

*"a sales promotion device will occur if the recommended retail price of a brand of cigarettes falls to a price which is more than 3% below the weighted average price for its category".*

EU Directive 95/59 lays down specific rules governing the conditions of sale of manufactured tobacco products and for the imposition of taxes on such products by the Member States. Article 9(1) of the directive states:

*"Manufacturers, or, where appropriate, their representatives or authorised agents in the Community and importers of tobacco from nonmember countries shall be free to determine the maximum retail selling price for each of their products for each Member State for which the products in question are to be released for consumption."*

**Facts of the Case.**

Following a series of letters to the Irish authorities requesting information on the relevant Irish legislation, which the authorities failed to adequately respond to, the EU Commission issued proceedings against Ireland claiming that the legislation was in breach of Article 9(1) of Directive 95/59. The Commission also claimed that Ireland was in breach of Article 10 EC as a result of its failure to provide information necessary to enable the Commission to fulfil its task of monitoring compliance with Directive 95/59.

According to the judgment, the Irish authorities argued *inter alia* that:

- the regulations were justified on public health grounds;
- they did not set a maximum price; and
- the setting of minimum prices did not affect the ability of suppliers to determine a maximum price.

The Irish authorities also contended that increased excise taxes on their own were insufficient to achieve the public health objective of discouraging smoking because suppliers could choose to absorb some or all of such taxes.

**The Court Judgment**

The Court referred to recital 3 in the preamble to the Directive which made clear that the directive was part of a policy for the harmonisation of the structures of excise duty on manufactured tobacco, the objective of which was to prevent the distortion of competition between different categories of manufactured tobacco and to open the national markets of the Member States.

The Court pointed out that Article 9(1) of Directive 95/59 provides that suppliers of tobacco products must be free to determine the maximum retail selling price for each of their products, the aim being to ensure effective competition between them It indicated that this provision seeks to ensure that the determination of the tax base of the proportional excise duty on tobacco products is subject to the same rules in all of the Member States. It also aims to maintain the freedom of economic operators to make effective use of the competitive advantage resulting from lower costs.

The Court held that:

*"The imposition of a minimum retail selling price by the public authorities thus means that the maximum retail selling price determined by manufacturers and importers cannot, in any event, be lower than that obligatory minimum price. Legislation imposing such a minimum price is therefore capable of undermining competition by preventing some of those producers or importers from taking advantage of lower cost prices so as to offer more attractive retail selling prices."* (Para 40).

It went on to state that "a system of minimum retail selling prices for tobacco products cannot be regarded as compatible with Article 9(1) of Directive 95/59 unless it is structured in such a way as to ensure, in any event, that the competitive advantage which could result for some producers and importers of those products from lower cost prices is not impaired and, thus, competition is not distorted." [3]

The Court found that the Irish legislation imposed on tobacco suppliers a minimum retail selling price for cigarettes equal to 97% of the weighted Irish average price for each category of cigarettes. It noted that the Commission had not established that the system imposed a maximum retail selling price for cigarettes.

The Court went on to state:

*"That system therefore undermines the freedom of producers and importers to determine their maximum retail selling price, guaranteed by the second paragraph of Article 9(1) of Directive 95/59."* (Para 45).

The Court also found that Ireland had failed to respond adequately to the Commission's requests for information and was thus also in breach of Article 10 EC.

**Economic Analysis.**

As previously pointed out, the case did not involve a breach of the EU Treaty competition rules but rather a breach of a Directive which clearly provides that suppliers of tobacco products *"shall be free to determine the maximum retail selling price for each of their products"*.

The judgment is not therefore an example *"of competition law gone mad"*. The focus should rather, be on the relevant EU legislation. Neither the Commission nor Ireland appears to have advanced any economic evidence on the question of whether or not the Irish legislation adversely affected competition.

The judgment, nevertheless, expressed certain views regarding the effect of the Regulations on competition, perhaps because the stated aim of the Directive is to ensure effective competition.

The judgment, referring to recital 7 of the preamble to the Directive, states that *"the imperative needs of competition imply a system of freely formed prices for all groups of manufactured tobacco."* Such language, while admittedly reflecting that used in the Directive, seems to imply that competition is an end in itself.

Economists generally strongly favour competition, but as a means to an end, not as an end in itself. They regard competition as desirable because, as a general rule, it increases the overall welfare of society.

Economists also recognise, however, that market failures may give rise to distortions which may prevent competitive markets working properly so as to maximise welfare. For example, it is widely recognised in the economic literature that there are negative externalities associated with pollution because it imposes a cost on society. In a free market such costs are not borne by those producing pollution and will thus not be reflected in the price of their products. Consumers will thus buy more of those products than they would if their prices reflected the true cost of production, where such costs include the cost of pollution. Perhaps the Directive needs to be considered in the context of overall economic welfare. There is no provision in the Directive that would allow a Member State that any restriction on competition was actually beneficial, i.e. it contains no equivalent of the former Article 81(3) under which agreements which are deemed anticompetitive may nevertheless be permitted.

The judgment accepted that it was legitimate for Member States to impose high taxes on tobacco products in order to keep prices high and thereby discourage consumption.[4] *"the excise duty increases sooner or later being reflected in an increase in the retail selling price, without undermining the freedom to determine prices"*[5]

This seems to confirm that the Government is free to increase taxation on tobacco products, although it implies an acceptance by the Court that such measures might be frustrated by suppliers absorbing some or all of the cost of such taxes in the short-run, as it argues that such taxes will be reflected in the retail price *"sooner or later"*. It may be worth recalling John Maynard Keynes famous dictum that: *"In the long-run we are all dead"*.

The Court went on to state that

> *"if the Member States wish to exclude once and for all any possibility for producers or importers to absorb, even temporarily, the impact of taxes on the retail selling price of manufactured tobacco products by selling them at a loss, it is inter alia open to them, while allowing those producers and importers to make effective use of the competitive advantage resulting from any lower cost prices, to prohibit the sale of manufactured tobacco products at a price below the sum of the cost price and all taxes."*[6]

Theoretically this may be correct but such a regime seems totally impractical, given the difficulties involved in accurately estimating costs for each and every supplier.

The judgment also states that the Regulations prevented lower cost suppliers from competing by offering lower prices to consumers. Firms in oligopolistic markets frequently tend not to compete on price for reasons which are discussed in the third article in this issue. This may or may not be the result of anti-competitive behaviour. In such markets the emphasis is often on nonprice competition. Thus, the judgment reflects a theoretical view of how firms might compete rather than any assessment of the form that competition between suppliers might actually take in the absence of the Regulations.

1 Call for cigarette taxes to be raised after Europe ruling, *Irish Times,* 5th March 2010.
2 S.I. No 326/1991. These regulations revoked the earlier Tobacco Products (Control of Advertising, Sponsorship and Sales Promotion) (No 2) Regulations 1986, S.I. No 107/1986. Article 16 of the 1991 regulations corresponded to Article 18 of the 1986 regulations.
3 The Court cited Case C-197/08 *Commission* v *France* [2010], paragraph 38, and Case C-198/08 *Commission* v *Austria* [2010], paragraph 30 in support of this finding.
4 Case C-140/05 *Valeško* [2006] ECR I-10025, para 58
5 Case C-140/05 *Valeško* [2006] ECR I-10025, paragraph 58
6 Case C-197/08 *Commission* v *France*, para 53, and *Commission* v *Austria*, para 43.

## No Hill of Beans - Oireachtas Committee Report on Grocery Sector.

**Introduction.**

The Oireachtas Joint Committee on Enterprise, Trade and Employment published a report on supplier-retailer relationships in the grocery sector in March.[1] The Report claims that it:

> *"(a) clearly highlights the disproportionate market power that large retailers retain in the Irish retail market and the disadvantages that this places suppliers and other retailers in, when seeking to conduct their businesses"; and*
> *(b) clearly highlights that some of these large retailers are using their disproportionate share of market power to impose unfair conditions on suppliers."*

The report contains little or no evidence to support such conclusions.

According to the Report Irish consumers are paying too high a price for grocery products which it states is partly due to inefficiencies within the supply chain, "but is mainly caused by retailers retaining profit margins three times greater in Ireland than in their operations elsewhere." Again, however, the Report contains no evidence to support such claims.

The Report is based on the results of interviews with just seven suppliers and in many instances does little more than quote a statement by an individual supplier. Buyer power may or may not constitute a problem in the Irish grocery market but the report sheds little light on this question. It therefore represents a highly unsatisfactory basis on which to formulate policy.

The Report goes on to claim that:

> *"It provides a strong case for introducing a statutory Code of Practice and the appointment of an Ombudsman to oversee its implementation and strict adherence to its terms by all participants."*

It is difficult to agree with such a conclusion given the lack of any evidence to support many of the claims made in the Report.

**Background.**

The continued growth and expansion of multiple supermarkets has given rise to numerous complaints about alleged anti-competitive behaviour by such groups in various countries.

The report states that the Committee has been conducting investigations into matters concerning the retail trade in Ireland over the last year or so. The Committee's report states that it had heard evidence from a wide number of organisations and companies engaged in the retail trade indicating that certain companies were abusing their strong position within the market to exert undue pressures on other commercial companies with whom they had business relations The Committee was informed that both primary producers and retailers had applied such methods in their business dealings but it was unable to verify all the assertions made because *"nearly all the suppliers and producers who were invited to appear before the Committee declined to do so."* The report states that:

> *"It documents the experience of a representative share of suppliers in the Irish grocery sector. It gives rise to serious concerns as it draws attention to assertions that some retailers engage in 'gross misconduct', 'bullying and intimidation' and even 'illegal practices' against suppliers. Many of the respondents state that they had been subjected to practices by retailers that include unreasonable demands for financial 'contributions' being made with implied threats for non-compliance."* (p.9)

According to the report the Committee wrote to 50 firms seeking their views. Eight replied expressing concerns about participating and in the end seven agreed to be interviewed on a confidential basis. It is hard to see how seven firms can be described as a representative share of suppliers.

According to the Report the seven suppliers who participated included two manufacturers, two primary producers; two processors/packers; and one importer all of whom supplied the main retail outlets in Ireland. It also stated that, in most cases, the respondents supplied at least 90% of their total produce to supermarkets and wholesalers within Ireland.

**The Report's Main Findings.**

Each interview was conducted by asking suppliers to comment on the following topics with respect to their dealings with retailers:-

1. Relationships – Power in the Market;
2. Strengths and Weaknesses in the market;
3. Gross Margins
4. Pricing;
5. Market Distortions;
6. Negotiations;
7. Payments;
8. Services Required;
9. Unfair practices.

According to the report the majority of respondents believed retailers held the buying power in the Irish grocery market, the only exception to this being those suppliers that had strong brand recognition. Respondents claimed that this power imbalance in favour of retailers allowed them to impose extortionate prices on the products they sell, to the disadvantage of consumers.

All of the participants reported a decline in their gross margins over the last five years, particularly in recent months. This was due to factors such as increased production and labour costs and currency fluctuations, but unreasonable demands made by retailers were seen to be the main cause of this.

Five respondents acknowledged that prices had fallen significantly in recent months but claimed that it was producers and suppliers who had absorbed the cost of these decreases rather than retailers.

Despite these decreases respondents remained gravely concerned that prices were still much higher in Ireland than elsewhere due to:

- Low population density;
- Pricing policy; and
- Inefficiency and distortions.

According to the report low population density meant that retailers in many parts of the country did not have the same level of footfall as retailers in other countries with much larger population densities. This might perhaps indicate that prices are likely to be higher in rural areas, but it is hardly a general explanation for high prices.

As far as pricing policy is concerned the Report simply quotes the view of one respondent who stated:

*"Multiples being quite bullish in their pricing, therefore making smaller stores [such as independent stores] appear more expensive."*

The respondents blamed retailers for inefficiencies and distortions and claimed that they were due to the high margins sought by retailers. The Report quotes on respondent as stating:

*"The main reason why prices are so different here [in Ireland] is a result of the high margins retailers make on their stock ... there are logistic issues and currency issues as well, but realistically it is the supermarkets and their high margins which add on the high prices to products."*

It quoted another as claiming that retail margins were higher in Ireland than in the UK.

*"The margin a retailer enjoys on some of our products in the Republic of Ireland is significantly more compared to [that in the] UK. In [the] UK it is 32%-35% and in the Republic of Ireland [it] is 45-50%. This is before VAT [Value Added Tax], exchange rates and logistics. Some retailers enjoy three times more profit here than in the UK."*

No evidence is advanced to support such claims.

All of the respondents claimed that *"unfair"* practices were widespread in the industry. The report claims that smaller firms were more likely to suffer such abuses, although it is difficult to draw any definitive conclusions given the small numbers involved.

Respondents complained most frequently about *'Hello Money'*, which was camouflaged by retailers under the title *'marketing support'*. The report listed a large number of variants under which retailers sought payments from suppliers.

The majority of respondent's stated that they were satisfied with the frequency of price negotiations. A majority also reported that they had been asked by retailers to enter into exclusivity agreements which they viewed as good commercial business and were to the advantage of both retailers and suppliers with some stating that they would like to see more of these agreements.

The report fails to elaborate on the nature of such exclusive arrangements. A commitment to supply a particular retailer on an exclusive basis would appear to weaken the supplier's bargaining position vis-à-vis that retailer. Such exclusive arrangements may also raise competition issues, a point which is returned to below.

Suppliers were asked to provide retailers with various services including:

1. Help with marketing;
2. Provision of staff in busy periods;
3. Adapting packaging to meet retailers' standards;
4. Delivering on pallets which meet retailers' standards etc. In general suppliers had little difficulty with such requests.

Six of the seven respondents had been supplied with standard terms of business when they requested them from retailers. Respondents reported that they had experience of payment delays.

**Retailer Buyer Power.**

There is an inevitable degree of tension in the relationship between supermarkets and suppliers. By definition suppliers seek to obtain the highest possible price for their products while supermarkets want to buy at as low a price as possible.

There is evidence that grocery prices in the Republic were higher than in Northern Ireland. This prompted consumers to vote with their feet and go North for their shopping. Inevitably this put pressure on retailers in the Republic to lower their prices. This was compounded by the downturn in the economy and the related growth of discount outlets. One of the major complaints of the suppliers interviewed was that they, rather than the retailers, had borne much of the cost of any price cuts. This is a general refrain with many groups currently complaining that they are suffering more than other sectors in the current downturn. The public sector unions are a good example.

High levels of concentration at the retail level provide little insight into the phenomenon of buyer power. After all if large retailers face large suppliers, buyer power is unlikely to constitute a problem. Nevertheless, it is clear that the relative position of suppliers and retailers has altered over time. Traditionally competition agencies focused on the relative power of suppliers vis-à-vis retailers. The large multiple groups have now evolved well beyond being mere undifferentiated channels to the consumer. Changes in the structure of the retail sector mean that the issue of buyer power may require closer examination.

The growth in the size of multiple supermarkets reflects a number of factors. These include:

1. Changes in consumer shopping habits due to demographic, transport, and

income changes which tend to favour one-stop weekly shopping especially for fast moving consumer goods. A UK survey found that 43% of consumers indicated that the main factor influencing their choice of store was "the ability to get most of the weekly shop done under one roof." Only 18% identified location and 16% pricing as the main factors influencing their choice of store.[2]

2. Changes in computer technology, especially the introduction of point of scale scanning contributed to increased scale economies, improved stock management and provided retailers with unique access to valuable information on consumer spending patterns.
3. Changes in the marketing sophistication and capability of large retailers, including a greater willingness and ability to sell own label brands.

The move by consumers towards one stop shopping may enhance buyer power in a number of ways. For example, if consumers find that a particular brand is not stocked in their preferred store, they may buy an alternative brand rather than go to another retailer. If enough consumers behave in this fashion then it may enhance the retailer's buyer power. In particular it means that a manufacturer may have no choice but to concede to the demands of a large buyer in the face of a threat to de-list the manufacturer's products. There is a limit to the extent to which a large buyer can make such threats. If it delists too many products, it runs the risk that consumers will switch to other outlets. The individual manufacturer, however, is not in a position to know how close to that point the buyer may be.

The potential impact of a threat by a major retailer to delist a supplier's products can be devastating if that retailer accounts for a significant share of the supplier's total sales. If a retailer accounted for, say 30% of a supplier's sales, it would be very difficult for the supplier to replace that volume of sales especially if they were already selling as much as they could through other retailers. Even if it could replace such lost sales with sales to smaller retailers this would be likely to raise the supplier's transaction and distribution costs. It is probably not unusual for one retailer to account for such a proportion of many suppliers' sales.

Buying power does not stem just from the ability to place large orders, but from a retailer's ability to withhold orders if it is unhappy with the terms offered by a supplier. In order to exert buyer power, a large buyer must either be able to source the product concerned elsewhere or be able to do without it.

Enhanced computer technology means that retailers have access to a great deal of information about consumer spending patterns. This means they may have far more information than manufacturers about consumer preferences and spending patterns. Similarly, the emergence of retailers as brands in their own right means that traditional forms of advertising by manufacturers may have become less effective. Gaining access to particular outlets may be more important than traditional forms of advertising. This means that manufacturers may have become more dependent on promotions by retailers in order to sell their products and may thus have to offer better terms in order to benefit from such promotional efforts.

Growth in sales of own label brands is another possible factor behind the increase in buyer power although the evidence on this point is somewhat mixed. It probably enhances the position of buyers vis-à-vis manufacturers of weaker or secondary brands. The Competition Authority's decision in *Kerry/Breeo* noted that some of the major retailers had reduced the proportion of shelf space allocated to branded goods and increased the proportion for own label over the past few years.[3]

Buyer power may also arise in situations where suppliers face "sunk" costs, or where there are switching or transactions costs. Sunk costs arise where manufacturers undertake customer specific investments to supply a particular customer. This may arise in the case of contracts to supply own brand products, where the investment is product specific. Once the supplier has undertaken such an investment, there may be opportunities for the buyer to seek to renegotiate contractual terms as the manufacturer is unable to recoup the cost of the investment if it looses the contract. This phenomenon is referred to in the economics literature as a "holdup" problem. Such a manufacturer could find itself forced to sell some or even all of its output at a price exceeding average variable cost but below average total cost. In the long-run such a captive supplier must exit the industry.

**Is Buyer Power a Problem?**

Buyer power may lead to efficiencies, i.e., sales to a large buyer may enable a manufacturer to achieve economies of scale. Thus, a buyer may obtain lower prices as a result of such economies thereby raising no competition concerns. Consequently, where lower prices are accompanied by increased purchases by the buyer, there is unlikely to be any competition problem.

Alternatively, a large buyer may be able to force prices down through the use of monopsony power. In order to force down the buying price the buyer must reduce its purchases. This, in turn, means that it will be able to sell less in the downstream retail market. If the retail market is competitive, the firm will lose market share. While the buyer might benefit from extracting lower prices from its suppliers, there is no adverse effect on consumers and other suppliers benefit from higher sales. For this reason it is argued that, in the absence of market power in the downstream retail market, the exercise of buyer power is unlikely to pose any serious problems.

Where the retailer has downstream market power, however, then it can reduce its purchases from suppliers to drive down purchase prices without any loss in downstream market share, i.e. total sales fall with a consequent decline in welfare of both consumers and suppliers. Thus where lower purchase prices paid to a supplier are accompanied by a fall in purchases from the supplier, it may reflect anticompetitive behaviour by the buyer.

Powerful retailers may seek to use exclusive supply agreements as a means of "raising rivals costs". They may seek to enter into agreements with suppliers to withhold supplies from price cutting rivals. Where a strong buyer enters into such arrangements with a number of suppliers it may facilitate the operation of an upstream (supplier) cartel, which is policed by the retailer.

In the US *ToysRUs* threatened suppliers with delisting if they supplied warehouse clubs with identical toys to those they supplied to it. This made price comparisons more difficult and raised the cost of toys supplied to warehouse clubs because of the more expensive packaging of the goods they were restricted to purchasing. It appears that manufacturers only agreed to cooperate in light of assurances that their competitors would be subject to similar delisting sanctions if they failed to cooperate. The latter aspect of the case suggests that buyer power may have been used to facilitate horizontal agreements among suppliers.

In Australia, *Safeway*, a subsidiary of the Woolworth group, engaged in the retail grocery sector, sold its own bread along with bread produced by an independent baker *Tip Top*. When another smaller retailer began discounting *Tip Top* bread, *Safeway* pressured the firm to institute resale price maintenance to put an end to discounting. Both *Tip top* and *Safeway* were prosecuted for breaches of Australian competition legislation.

In Tredegar in Wales an independent retailer began undercutting a nearby Tesco store on the price of bread supplied to both outlets by a local bakery. The Tesco store manager allegedly threatened the bakery that it would cancel its contract with it, unless the bakery persuaded the rival store to raise its prices. The store subsequently ceased trading. Tesco stated that it appeared that its store manager had spoken directly to the bakery but that its buying manager had subsequently assured the bakery that Tesco would continue to carry its products and would in no way seek to dictate its trading terms with other retailers. It also stated that the store manager in question was no longer employed by Tesco and that such behaviour was against company policy.[4]

Buyer power frequently gives rise to some form of discrimination in the treatment of different buyers. Price and non-price discrimination arise where suppliers offer more advantageous terms to certain buyers than can be justified on cost grounds. Economic theory indicates that price discrimination is not necessarily harmful as it may lead to higher levels of output and, consequently, increase overall economic welfare. Price discrimination by a supplier may confer an advantage on large incumbent retailers that is unrelated to the relative efficiency of such retailers. In those circumstances it may act to keep the market shares of smaller, equally efficient, retailers small and limit their ability to compete with larger retailers. The potential for buyer power to result in this type of discrimination may be a concern in the grocery sector.

***"Hello Money".***

This is the name given to the practice of supermarkets seeking payments from suppliers in order to have their products stocked by the multiple. In other jurisdictions such payment are referred to as *"slotting allowances"*.

Whether such payments are anticompetitive or not requires a case-by-case analysis. They reduce retailers' inventory costs and represent a mechanism by which retailers may ration limited supermarket shelf space. Payment for access by a supplier also signals to the retailer that a manufacturer is confident that a product will be successful. If retailers were to discriminate between suppliers, seeking hello money from some but not others, then questions of exclusion could arise.

There are also problems in defining such payments. It is common for retailers to require suppliers' delivery staff to take responsibility for stocking shelves and arranging displays. As noted above, the Oireachtas report indicated that the suppliers interviewed generally had no difficulty in providing such services. Clearly providing such services involves an implicit payment by the supplier to the retailer. Similarly, if the supplier runs an in-store promotion at the request of the multiple, it is difficult to see why that should be treated differently to a situation where a retailer seeks payments and then pays some other entity to organise the promotion.

**Conclusions.**

The Oireachtas Committee Report on supplier-retailer relations concludes that retailer buyer power constitutes a problem in the Irish grocery trade. The Report, however, contains no economic analysis of buyer power. In addition, the views expressed in the report can hardly be considered representative as only seven suppliers were interviewed. The Report contains no evidence to support many of the claims advanced. The State has used its buyer power to drive down prices in recent years in the case of pharmacies and other professions. It has justified this as ensuring better value for money for taxpayers. I

Buyer power and practices such as "hello money" may be anti-competitive in certain circumstances but a more indepth assessment of the situation in Ireland is required before any meaningful policy conclusions can be drawn.

1 Joint Committee on Enterprise, Trade and Employment, *Supplier-Retailer Relationships in the Irish Grocery Market*, March 2010.

2 Competition Commission (2000): *Supermarkets A Report on the Supply of Groceries from Multiple Stores in the United Kingdom.*

3 Competition Authority Determination in Merger Notification M/08/009 – Proposed acquisition by Kerry Group plc of Breeo Foods Limited, 28th August 2008.

4 W. Young, *Sold Out The True Cost of Supermarket Shopping,* 2004, p.49.

# Royal Bank of Scotland Fined for Information Sharing.

**Introduction.**

On 30th March, the Office of Fair Trading (OFT) announced that the Royal Bank of Scotland (RBS) had agreed to pay a fine of £28.59 million after admitting breaches of competition law between October 2007 and February or March 2008. Specifically, employees in one of the bank's divisions had disclosed confidential future pricing information to their counterparts at Barclays Bank. According to the OFT, there was evidence that Barclays had taken this information into account in determining its own pricing.

**Background to the Case.**

The case resulted from an OFT investigation which found that individual employees in RBS's Professional Practices Coverage Team had unilaterally disclosed generic as well as specific confidential future pricing information to their counterparts at Barclays Bank. The matter was brought to the OFT's attention by Barclays under the OFT's leniency policy, where a company which is the first to report its participation in an infringement may qualify for immunity from penalties. The OFT has stated that Barclays is not expected to pay a fine in this case, provided it continues to co-operate.

The information disclosures by the RBS employees took place in the course of a number of contacts on the fringes of social, client or industry events or through telephone conversations. The information concerned the pricing of loan products to large professional services firms, such as solicitors, accountancy and real estate firms. As well as general disclosures on future pricing, the investigation found that RBS had supplied specific confidential future pricing information in relation to two proposed loan facilities. The OFT also stated that it had found evidence that the information was taken into account by Barclays in determining its own pricing.

**Economic Analysis.**

It is widely recognised that there is a constant risk of collusion in oligopolistic markets. In many countries competition law prohibits and provides for serious sanctions for such behaviour. This means that firms may seek to collude without entering into any formal or informal agreement or understanding that would fall foul of competition law, i.e. they engage in tacit collusion.

In oligopolistic markets with a relatively small number of competitors firms will recognise that their commercial actions will likely trigger a response from their rivals. Any attempt by one firm to increase its market share will impact on the sales of the remaining firms and they are likely to respond. Such interdependence means that firms will consider how their rivals are likely to respond to any commercial move that they make. The mutual recognition by firms of such interdependence may blunt competition in oligopolistic markets.

It would be irrational of firms in such circumstances to ignore the likely reactions of their competitors when making commercial decisions. Nevertheless, even though no firm actively fights its competitors the outcome in such markets may be competitive in the sense that it results in profit levels that are below those that would be achieved under collusion. Tacit collusion thus involves raising prices and profits above their "non-cooperative equilibrium level".

Information sharing is thus widely regarded as a facilitating practice for tacit collusion. Information sharing is not proof of collusion given the difficulties in preventing cheating but, according to Phlips, it indicates collusive conduct "in the sense that the oligopolists are *trying* to achieve a collusive outcome." [1] (Emphasis in original). Competition law in Ireland and the UK mirror the EU competition rules which prohibit agreements, decisions or concerted practices which have as their object or effect the prevention, restriction or distortion of competition. Thus if one accepts the economic argument that information sharing represents an attempt to achieve a collusive outcome then arguably it represents a concerted practice which has the object of preventing, restricting or distorting competition.

**Comment.**

On the face of it the fine of £28.6 million imposed in this case appears fairly substantial. Of course, it cannot be judged in isolation, but must be viewed against any increased profits generated as a result of the behaviour deemed anti-competitive but the OFT announcement contains no information on this. The case demonstrates that sharing confidential information about pricing and other sensitive issues is prohibited by competition law. It has been a costly lesson for RBS.

[1] L. Phlips, (1995), *Competition Policy: A GameTheoretic Perspective*, p.83.