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COMPETITION COMMITTEE****Hub-and-spoke arrangements – Note by the United Kingdom**

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More documents related to this discussion can be found at
<http://www.oecd.org/daf/competition/hub-and-spoke-arrangements.htm>

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1. Introduction

1. Hub and Spoke (or A to B to C) infringements arise where anti-competitive behaviour between two competitors or ‘spokes’ (A and C) is co-ordinated or facilitated by a third party ‘hub’ (B) which typically acts at a different level of the supply chain. The experience in the UK has been that the ‘spokes’ are generally competing retailers while the ‘hub’ will be a common supplier.

2. Where established, hub and spoke infringements constitute breaches of the Chapter I prohibition of the UK’s Competition Act 1998 as either anticompetitive agreements and/or concerted practices¹.

3. In terms of the UK experience, the OFT (the CMA’s predecessor) reached infringement decisions in three hub and spoke investigations. They are *Replica Kit*²; *Toys*³ and *Dairy*⁴. All three decisions were appealed to the UK’s Competition Appeal’s Tribunal⁵ (the Tribunal), with the Tribunal’s judgments in *Replica Kit* and *Toys* being further appealed to the Court of Appeal⁶. After the conclusion of all relevant appeals these cases have resulted in aggregate fines of over £80 million.

4. Although the UK authorities haven’t reached an infringement decision in respect of this form of behaviour since the OFT’s *Dairy* decision of July 2011, both the OFT and the CMA have conducted several other investigations which have uncovered evidence consistent with hub and spoke contacts. However, neither organisation decided to prioritise enforcement action. These decisions were taken for a number of reasons. In some cases, there was insufficient evidence to meet the legal test necessary to demonstrate the infringement with enforcement action instead addressing other infringing behaviour (such as RPM). Other cases involved suspected infringements which pre-dated earlier enforcement action in the relevant sector and where there was also evidence of effective compliance programmes having been put in place as a result.

5. Despite the lack of recent enforcement activity in this area, the CMA is committed to investigating and, where appropriate, taking enforcement action against hub and spoke conduct which it believes meets its prioritisation criteria. Accordingly, any such decision will principally rest on the strength of the evidence in any such investigation, the harm to

¹ The Chapter I prohibition is found at section 2 Competition Act 1998 and mirrors Article 101(1) of the Treaty for the functioning of the European Union

² See OFT infringement decision CA98/06/2003, 1 August 2003.

³ See OFT infringement decision CA98/8/2003, 21 November 2003

⁴ See OFT infringement decision CA/03/2011, 26 July 2011

⁵ See [2004] CAT 17 (*Replica Kit*); [2005] CAT 13 (*Toys*); and [2012] CAT 31 (*Dairy*). Hereafter respectively referred to as *Tribunal’s judgment in Replica Kit*; *Tribunal’s judgment in Toys*; and *Tribunal’s judgment in Dairy*.

⁶ See *Argos Limited and Littlewoods Limited v the OFT and JJB Sports PLC v the OFT* [2006] EWCA Civ 1318. Case No: 2005/1071, 1074 and 1623. Hereafter referred to as the *Court of Appeal’s judgment*.

consumers and the likely impact of any CMA intervention. In 2019 the CMA investigated suspected hub and spoke behaviour in the online retail sector but subsequently closed the case on the grounds of insufficient evidence.

2. Case Facts and Context

6. The *Replica Kit* and *Toys* infringements took place in the early years of the Competition Act 1998 (which came into force in 1 March 2000).

7. In both cases, a major supplier (Umbro in the case of *Replica Kit* and Hasbro in the case of *Toys*) were keen to avoid retailer discounting on their products⁷. In both cases there was a price leader in the market (JJB Sports in *Replica Kit* and Argos in *Toys*) and keen price competition existed between them and other retailers. In *Replica Kit*, JJB Sports was particularly concerned about the discounting behaviour of Sports Direct, while in *Toys* Argos was principally concerned about its competitive position against Littlewoods.

8. These various circumstances led to a position where in both cases retailers were not prepared to commit to price at recommended levels without receiving assurances that their competitors were going to do the same. This resulted in suppliers (Umbro in the case of *Replica Kit* and Hasbro in the case of *Toys*) acting as an intermediary for the disclosure and exchange of retail pricing intentions between their retailer customers with the aim of ensuring that there was no discounting from recommended retail prices in the respect markets.

9. Although it has many similarities to the *Replica Kit* and *Toys* cases, the *Dairy* case took place in slightly different circumstances. Here there was no suggestion of historical RPM, instead grocery retailers and their supplying dairy processors were subject to a campaign to increase the farmgate price (the price farmers are paid for raw, unprocessed milk) following a very significant drop in its level. The pressure placed on retailers and their supplying processors was substantial – and included the blockade of supply depots. This placed both processors and retailers under potentially substantial margin pressures in the very competitive grocery retail sector and involved goods (fresh liquid milk and cheese) which consumers were particularly price sensitive on given their staple nature and which retailers did not therefore wish to be more expensive than their competitors on.

10. In response to this pressure, retailers and processors organised a number of price initiatives involving various dairy products (including fresh liquid milk and cheese) which were designed to increase the farmgate price by 2 pence per litre and subsidising that increase through increased wholesale and retail price of various dairy products. The OFT investigated a number of these initiatives before issuing an infringement decision concluding that three of them (in relation to cheese in 2002 and 2003 and in relation to fresh liquid milk in 2003) were illegal hub and spoke infringements and breached the Chapter I prohibition.

11. In particular, the OFT found that certain grocery retailers coordinated the implementation of retail price increases in respect of these products by disclosing and exchanging information concerning their retail pricing intentions to each other via their supplying processors. The CMA imposed aggregate fines of close on £45 million.

⁷ See paragraph 119 of the Court of Appeal judgment

12. Tesco (which the OFT did not find to be party to the 2003 fresh liquid milk infringement) appealed the infringement findings the OFT made against it in respect of cheese in both 2002 and 2003 to the Tribunal. The Tribunal partially allowed Tesco's appeal, overturning the OFT's infringement findings in respect of the 2003 initiative in full and also overturned some of the infringement findings that had been made in respect of the 2002 initiative. This resulted in Tesco's fine being reduced from £10.43 million to £6.5 million.

3. The legal test and its evolution

13. Although the premise that indirect disclosures and exchanges of pricing intentions between competitors is a breach of Article 101 (and the Chapter I prohibition) is well established in law, at the time of these cases the circumstances under which such an infringement would be demonstrated were less clear⁸.

14. The challenge to the UK competition authorities and courts have grappled with is creating a test which places both spokes (i.e. retailers A and C) in the position they would have been if they had directly disclosed their retail pricing intentions to each other⁹ (an obvious breach of the law) whilst also recognising that retailers may have robust commercial discussions and disclose information without envisaging that their suppliers would pass that information on to their competitors¹⁰. This challenge has been resolved by introducing a requirement to demonstrate intent on the part of A and C.

15. In its *Replica Kit* and *Toys* appeal judgements, the Tribunal established that an indirect concerted practice between retailers A and C and supplier B would be formed where (i) A disclosed information regarding its retail pricing intentions to B in circumstances where it would have been *reasonably foreseeable* to A that B would make use of its information to influence conditions on the retail market by disclosing it to A's competitors; and (ii) B does pass A's pricing intentions on to C; and (iii) C uses A's information in determining its pricing behaviour¹¹.

16. The Tribunal also held that demonstrating C's reliance on A's pricing intentions in determining its own conduct on the market can, if necessary, be demonstrated by reliance on the rebuttable presumption established by the Court of Justice in the *Polypropylene* cases. The presumption means that where a firm remains active on the market after having received information regarding its competitors pricing intentions it is presumed to have taken account of that information (this is often referred to as the *Anic* presumption)¹².

⁸ See *Suiker Unie v Commission* [1975] ECR 1663 which established that a concerted practice could arise where there is 'any direct or indirect contact between operators, the object or effect whereof is to influence the conduct on the market of an actual or potential competitor or to disclose to such a competitor the course of conduct which they themselves have decided to adopt or contemplate adopting on the market.' See also *Cimenteries CBR v Commission* [2000] ECR II-491 at 1852.

⁹ See paragraph 66 of the *Tribunal judgment in Dairy*

¹⁰ See paragraph 106 of the *Court of Appeal judgment*

¹¹ See paragraph 659 of the *Tribunal judgment in Replica Kit*

¹² See *Commission of the European Communities v Anic Partecipazioni SpA (C-49/92P)* [1999] E.C.R I 425 at [121]

17. The Tribunal additionally held that an infringement could be demonstrated where there is a unilateral disclosure of pricing intentions (i.e. by A to B to C) without there being any need for reciprocity on the part of C. In other words, there was no need to demonstrate that C, having received A's pricing intentions, made a reciprocal disclosure of its own to B which B then passed on to A etc. However, where reciprocity of this nature was established, the infringement would obviously be all the stronger.

18. Both the Tribunal's judgments were appealed to the Court of Appeal and, although the infringements were upheld, the Court developed a more stringent and nuanced test to establish intent.

19. First, the Court of Appeal held that the Tribunal '*may have gone too far*' in its *Replica Kit* judgment in concluding that it only needed to be '*reasonably foreseeable*' to A that B would make use of its retail pricing intentions by passing them on to A's competitors. Instead, the Court of Appeal established that it was necessary to demonstrate that A '*may be taken to have intended or did, in fact, foresee*' that B would its information in that way¹³.

20. Second, the Court of Appeal held that it was also necessary to demonstrate that C '*may be taken to know the circumstances in which the information was disclosed by A to B.*' The Tribunal's test had not created the need to demonstrate any understanding on the part of C¹⁴.

21. Besides these adjustments, the remaining parts of the Tribunal's test were upheld. Accordingly, it remains the case that there is no need for reciprocity to demonstrate a hub and spoke infringement and that C's reliance on A's intentions can be demonstrated by applying the *Anic* presumption.

4. Challenges in establishing hub and spoke infringements

22. Establishing the existence of hub and spoke infringements provides several evidential challenges: there is a need to demonstrate at least two disclosures of information (from A to B and from B to C) and then also demonstrate that A and C have the requisite intent in their respective roles.

4.1. Demonstrating disclosures

23. Disclosures can be demonstrated by direct evidence – i.e. an email from retailer A to supplier B in which A discloses its pricing intentions and a subsequent email in which B discloses A's information to retailer C. can be demonstrated by direct evidence – i.e. an email from retailer A to supplier B in which A discloses its pricing intentions and a subsequent email in which B discloses A's information to retailer C.

24. However, as with any hardcore infringement evidence chains will often be fragmentary and inchoate. For example, it is not unusual to find evidence of just one of the requisite disclosures without the other.

¹³ See paragraphs 91 and 140 of the *Court of Appeal judgment*

¹⁴ See paragraphs 91, 140 and 141 of the *Court of Appeal judgment*

25. In circumstances where there is evidence of A disclosing its pricing intentions to B but no evidence that B has passed that information on to C there is limited scope to fill the evidential gap by inference.

26. The picture is different where there is evidence demonstrating B apparently passing on A's pricing intentions to C without any evidence of A first disclosing its information to B. In these circumstances there is more scope to make an inference that A disclosed commercially sensitive information to B because B is telling C that it is informing it of A's pricing intentions.

27. However, it is still necessary to demonstrate that the information B purports to come from A did in fact do so and that B is not bluffing – in order to do this much will depend on what inference can be drawn from indirect evidence. For example, is there evidence in B's internal records showing that it was in possession of A's pricing intentions at the time of the disclosure and/or is there anything in A's internal records which suggest that the information B passed on was consistent with what it was planning to do in the market place.

28. It may be possible to infer the disclosure from A to B if what B discloses to C turns out to be accurate - however, such an inference may need to be corroborated because in some markets it is possible for B to make a reasonably informed prediction as to what A was likely to do.

4.2. Demonstrating A and C's intent

29. As set out above, the Court of Appeal's judgment in *Replica Kit* and *Toys* established a more stringent and nuanced test to determine the issue of intent in hub and spoke investigations than had previously been developed by the Tribunal.

30. First, it is necessary to show that retailer A disclosed its pricing intentions to supplier B in circumstances where A may be taken to have intended (or did in fact foresee) that B would make use of that information to influence market conditions by passing that information to other retailers¹⁵. It is not sufficient for A to 'have a pretty good idea' how B would act¹⁶.

31. Second, it is necessary to demonstrate that, when receiving A's pricing intentions from B, retailer C may be taken to have known the circumstances in which A disclosed its information to B.

32. Since there is 'no window into the mind of another' person, absent an admission from an individual, intent will principally be established by drawing inferences from what an individual knew, said and did, both at the time of the disclosures and later in evidence¹⁷. The remainder of this section assesses the ways intent has been inferred in previous cases.

33. *Complaints and threats.* Both A's and C's state of mind can be established to the requisite standard if they have made a complaint to B or made a threat to B (for example threatened to drop their retail prices and reject a cost price increase unless their competitors also increase their prices). In *Replica Kit*, JJB asked Umbro to "do something about" Sports

¹⁵ See paragraph 141 of the *Court of Appeal judgment*

¹⁶ See paragraph 71 of the *Tribunal judgment in Dairy*

¹⁷ See paragraph 69 of the *Tribunal judgment in Dairy*

Direct's discounting.¹⁸ In this situation the Tribunal found that JJB may be taken to have intended that Umbro would use its information to influence conditions on the market – principally by seeking a price increase by Sport's Direct.

34. Similarly, if C receives information from B regarding A's pricing intentions (such as being assured A would be increasing its prices on a particular day) having previously complained to B about A's discounting, C may be taken to have known the circumstances in which A disclosed its information to B.

35. *Conditional commitments.* Another way to demonstrate retailer A's intent is where it makes some form of conditional commitment to B regarding its own future pricing behaviour. For example, by committing to increase its retail prices on condition that its competitors also increase their prices. In the Dairy judgment, the Tribunal established that one of the grocery retailers (Sainsbury's) had made a conditional commitment to increase its cheese retail prices '*provided other retailers also*' did so and that this evidenced the conditional nature of its retail pricing intentions¹⁹.

36. Conditional commitments can also be used to demonstrate C's intent as the recipient of the information. If C has previously made a conditional commitment to B that it would increase its retail prices only if A increased its prices and subsequently receives information regarding A's pricing intentions from B reassuring C that A would be increasing its retail prices then it is also reasonable to infer that C understood the circumstances under which A disclosed its pricing intentions to B.

37. *Disclosure having received.* A's intent can also be established to the requisite standard where it discloses its pricing intentions to its supplier B, in circumstances where it has previously received information from B regarding its competitors' pricing intentions²⁰. In these circumstances, A is aware from the information it has received regarding its competitors that B is disclosing sensitive information regarding its retailer customers' pricing intentions across the market and therefore may be taken to have intended that B would make use of that information to influence market conditions by passing disclose it on to other retailers.

38. *Absence of a legitimate commercial reason for a disclosure.* Finally, the absence of any legitimate commercial reason for a disclosure by retailer A of its pricing intentions to supplier B may also be indicative of a requisite state of mind. This factor is unlikely to be determinative on its own, however where there is no legitimate reason for a disclosure it is likely to be consider in the context of what else was known to A at the time it made the disclosure²¹.

39. When considering this issue it is important to distinguish between disclosures by Retailer A that it will reduce its price, from disclosure that it will maintain or increase its price. In its judgment in *Dairy*, the Tribunal stated that there may fewer '*may be fewer legitimate commercial reasons*' for a retailer to disclose information that it planned to

¹⁸ See paragraph 53 of the *Court of Appeal's judgment*

¹⁹ See paragraph 311 of the *Tribunal judgment in Dairy*

²⁰ See paragraphs 303, 312 and 369 of the *Tribunal Dairy judgment*

²¹ See also *Tribunal judgment in Dairy* paragraphs 72, 300 and 368

increase its retail price when compared to a reduction in retail prices²². Although there may be circumstances where such disclosures are necessary and legitimate.²³

5. Conclusion

40. Hub and spoke behaviour can give rise to anti-competitive agreements and concerted practices.

41. The experience in the UK suggests that, when hub and spoke behaviour occurs, it is likely to be in circumstances where there is margin pressure in the supply chain which is resolved by the coordination of retail price increases.

42. Transparency in the retail market seems an important feature of the infringements that have been enforced in the UK as retailers do not wish to be more expensive than their competitors and are able to identify when they are. In these circumstances, a retailer is more likely to complain to its suppliers about the pricing behaviour of its competitors.

43. In these circumstances a supplier may become concerned about its own margins – if its retailer customers are not making as much money from the products it supplies as they had hoped as a result of discounting in the market then they are likely to seek cost price reductions or other favourable terms which require investment from suppliers (such as more substantial promotional budgets).

44. This situation can give rise to incentives to coordinate – with both suppliers and retailers having the incentive to co-ordinate retail price levels as a means of relieving the margin pressures they are experiencing.

45. The UK has developed a test to establish hub and spoke infringements. The central challenge that courts have grappled with is distinguishing legitimate vertical discussions between a supplier and a retailer from those which have a horizontal dimension. In order to address this issue, the courts have established a requirement that enforcers demonstrate some form of anti-competitive intent on the part of the retailers involved.

46. Although demonstrating hub and spoke infringements is evidentially challenging the CMA will prioritise enforcement action against where it fits with its prioritisation criteria.

47. Even where the hub and spoke infringement itself cannot be demonstrated, the evidence retrieved in that investigation may be used to allege or find other infringements of the Chapter I prohibition – most notably RPM.

48. For example, in a situation where the hub (B) has disclosed A's future pricing intentions to C with the aim of influencing C's pricing behaviour, but it is not possible to establish A's intent then it may be possible to establish that B's disclosure of A's information to C is an vertical infringement between B and C.

²² See paragraph 72 *Tribunal judgment in Dairy*

²³ See paragraphs 300 to 302 of the *Tribunal Dairy judgment*