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Purchasing Power and Buyers' Cartels – Note by Finland

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More documents related to this discussion can be found at
<https://www.oecd.org/daf/competition/purchasing-power-and-buyers-cartels.htm>

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1. The Finnish Competition and Consumer Authority (FCCA) has been involved in several cases connected to buyer power and other closely comparable phenomena like monopsony and bargaining/countervailing power (hereinafter buyer power). Some of the cases have related to merger enforcement applied to Finnish companies either by the FCCA or by the European Commission or European Union (EU) courts. In addition, number of the major Finnish cartel cases have concerned purchasing cartels (buyer's cartels), especially in the raw wood purchasing markets. Although there is a relatively rich national case law in the area, the focus of this contribution is to present a special provision in the national Competition Act which was enacted to eliminate buyer power distortions particularly in the domestic grocery markets.

1. Specific grocery sector ban

2. The Finnish Competition Act has traditionally contained a general provision prohibiting the abuse of dominant position (hereinafter, general ban on abuse of dominant position). This ban corresponds to article 102 of the Treaty on Functioning of the European Union (TFEU) and it applies to all potential market operators (undertakings) in all sectors of the economy provided that a dominant position and an abuse of that position can be detected.

3. However, in January 2014, to boost the effectiveness of dominance-related enforcement, a special provision was added to the Finnish Competition Act which supplements the traditional general ban on abuse of dominant position. This new provision is applicable only to the abusive conduct in the grocery markets and designed to mitigate harmful effects of buyer power in that industry (hereinafter, specific ban on grocery sector abuse of dominant position).

4. According to this provision, buyer power refers to conditions in which

- the buyer purchases such a large share of the seller's production that the seller has limited possibilities to exploit alternative distribution channels of other buyers; and
- the seller – if its business contract is terminated with the buyer and by the buyer for the goods in question – incurs relatively higher losses from the disruption of deliveries compared to losses of the buyer.

2. Automatic dominance

5. After the 2014 amendment, an undertaking or an association of undertakings whose market share in grocery retail sales in Finland is at least 30% of the national total is considered to be in a dominant position in the grocery market.¹ The point is that if the 30% market share is exceeded, the grocery sector retail chain is automatically in a dominant position, and therefore also the ban on abuse of dominant position can be applied to its conduct and practices. In terms of calculating the market share threshold, the retail sales of

¹ Markets include foods, beverages, tobacco, some technochemistry products (e.g., cleaning supplies), household paper products, magazines and cosmetics.

groceries by all undertakings part of that particular retail chain are taken into account. The market share threshold is not rebuttable by any evidence submitted in rebuttal if the market share threshold is otherwise exceeded. As to grocery markets, both consumer level retail markets (downstream markets) and supplier level purchasing markets (upstream markets) are included.²

6. As exceeding the market share threshold automatically equals to a dominant position, market power associated with a dominant position is not determined on the basis of the same market analysis that is used when the general ban on abuse of dominant position is applied. In this respect, the analyses differ from each other although both – general ban and specific grocery sector ban – deal with abuse of dominance. Under the specific ban, the market power of a grocery chain would not, for example, be examined by defining relevant markets or barriers to entry into the sector, or by examining other (economic) factors that normally are considered when assessing the existence of market power. A national market share more than 30% alone, without other factors, would be sufficient as such to establish a dominant position.³ As a comparison, when the general ban on abuse of dominant position is applied, a market share of 30% does not alone demonstrate the existence of a dominant position, but rather an additional and more comprehensive analysis is required before any such conclusion. For this reason, the specific grocery sector ban is stricter and more severe than the general ban.

3. Carefully considered threshold

7. The market share threshold was set at 30% particularly to ensure that the two largest retail chains in the grocery market would be subject to the new regulation. When the amendment entered into force, their total market share was approx. 80% at that time and has changed little since then. According to the preambles of the new provision both two retail chains

”[–] have significant buying power, and the distribution channels offered by their competitors cannot be regarded as alternatives that would essentially offset the buying power of the large chains for the suppliers.”

8. The new provision was largely enacted to pre-emptively eliminate market distortions resulting from buyer power. As the specific provision automatically defines both retail chains as being in a dominant position purely on the basis of their market share they must comply with the obligations that come with this position.

² The amendment does not affect merger enforcement in the grocery sector. Similarly to other sectors, grocery sector mergers are subject to the general merger enforcement rules under the Competition Act.

³ Whereas the new provision applies to only nationwide markets, the competition authority may, by applying other provisions of the Competition Act, also intervene in non-nationwide i.e., regional or local competition restrictions. In principle, it is possible that a national retail chain also includes independent local and regional grocery sector entrepreneurs and groupings. As a main rule, the specific ban (on grocery sector abuse of dominant position) does not apply to the market conduct of these local and regional entrepreneurs and groupings, even if their local market share would exceed 30%. An exception to this main rule is the situation in which the conduct of a local or regional grocery retailer is the result of compliance with the decisions or instructions of the central body of the grocery chain or compliance with practices facilitated by the central body.

9. The retail chains themselves have the primary duty to remedy their market practices to avoid any violations of the ban on abuse of dominant position. This means that they must carry out a self-assessment, to monitor their trading practices and potentially make changes to them, ensuring that since January 2014 their conduct and contractual terms have been consistent also with the new sector-specific ban.

4. Reason for the reform

10. The objective of the 2014 amendment was to ensure effective market function in the highly concentrated national grocery market, and more specifically to

- prevent the use of unfair and discriminatory trading practices based on a strong market position as well as practices that clearly exclude competition and exploit trading partners or consumers;
- ensure that large traders do not exclude their competitors from the market by other means besides competing on their merits and using normal and objectively acceptable means of competition without unfair exploitation of market power; and to
- bring the competitive conduct of the two key players in the grocery trade under the control of abuse of dominant market position.

11. An important backdrop to the amendment was the fact that Finland had one of the most concentrated grocery markets in Europe. Since then, the total market share of the two largest national retail chains has remained relatively stable at around 80%. The Finnish grocery sector has also constantly been assessed by the European Commission and the OECD, which have found that competition in the sector has not been working optimally and Finland has been urged to remedy the situation.

12. Furthermore, a report prepared by the Finnish Competition Authority (the predecessor of the FCCA) in 2012 on the potential competition issues in the sector and particularly on the impact of harmful buyer power on relations between the trade and industry in the grocery sector also influenced the adoption of the new sector-specific abuse provision. According to this report, large retail chains had a very strong negotiating and buying power, which could lead to market distortions when they purchased products for their ranges. In the report, some of the harmful practices which were incompatible with healthy competition. For example, the following practices were mentioned:

- introduction of questionable marketing subsidies;
- passing on unreasonable business risks to suppliers;
- imposing manifestly unfair contractual terms on suppliers; and
- preventing new products from entering the market.

13. The last-mentioned practice refers to a conduct where the grocery sector retail chain uses its buyer power to unjustifiably prevent suppliers' products from being included in the retail chain's product range. This way, they are considered to also hamper the market entry of new products and to restrict consumer choice. An underlying reason might be the chain's attempt to protect their own brands, or so-called private label products. Consequently, buyer power is believed to give large retail chains the power to decide which products will ultimately enter the market and become available to consumers. As the preambles of the law note:

"[--] products that concentrated grocery retail sector refuses to include in their ranges have little chance of reaching the consumer, as the suppliers do not have access to alternative distribution channels. This leads to a situation where concentrated grocery retail sector largely determines whether or not products can succeed in the market."

14. It is worth stressing that the 2014 reform was carefully designed not to suppress horizontal competition between large chains or their competition against other grocery outlets. The aim was not to balance negotiating power of various parties to the grocery trade as such, but rather to focus on harmful buyer power only and to ensure that the grocery markets would function without unnecessary competition restraints.⁴

5. Abuse and justifications

15. The specific provision only prohibits the abuse of a dominant position, not the dominant position as such. This way the approach is the same as with general ban on abuse of a dominant position. Although the specific ban concerns abuse of a dominant position in cases where the market share of the grocery sector undertaking exceeds 30%, the ban does not prevent undertakings from increasing their market share even beyond 30%, as long as this is achieved by competing on merits and without abusive conduct.

16. As for the abuse itself, in all cases the potential abusive conduct is assessed on a case-by-case basis and particularly analysing the market effects of the investigated conduct. Therefore, the specific grocery sector ban is strongly linked to effects-based analysis of a unilateral conduct. Given that Finland is a member state of the EU, the relevant jurisprudence of EU competition rules must also be followed when abusive conduct is assessed. While all cases are assessed individually and any conduct may face enforcement actions, the preambles of the sector specific ban argue that particularly abusive price discrimination, predatory pricing, number of loyalty rebates and certain tying/bundling practices are most likely practices that may require the competition authority to intervene.

17. The notion of advantageous terms of trade is an important concept of the specific grocery sector ban. It is linked to an assumption according to which the higher the retail market share of a grocery sector undertaking is, the better its terms of purchase usually are. The point here is that for many suppliers in Finland both largest grocery sector retail chains – given their large market share in the retail business – are so important distribution channels that these buyers will always be offered, or that they are successfully able to demand, more advantageous terms of trade compared to other buyers the suppliers are dealing with. Furthermore, as the law sees it, advantageous terms of purchase can be used in different ways to develop the chain's business and to further increase its market share, which in turn may lead to even better purchase terms. According to the reformed Act, all this could lead to a competitive edge vis-à-vis their competitors in the grocery retail markets which ultimately only will only increase powerful buyers' importance in the sector. The law predicts that this spiral of advantageous terms may be apt to lead to a continuous increase in concentration both in retailing and in purchasing markets. According to the preambles of the specific provision:

⁴ The national competition authority was initially critical adopting the sector specific ban due that the problems between the suppliers and buyers were merely of contractual nature and hence legal reforms to remedy the situation should not be included in the Competition Act (and to cause tensions with the general ban).

"[--] for a while, this trend may be beneficial for consumers if market positions are defended by means of tough price competition, but in the longer term, it can easily result in a situation where competition will have significantly declined. At this point, the chain no longer needs to take consumer reactions into account, as there are no competing options for the consumers".

18. However, the 2014 amendment recognises also potential positive aspects of buyer power. In fact, the law acknowledges that exploiting buyer power in the purchasing activities is not necessarily reprehensible from the perspective of the Competition Act. This is because buyers can face effective competition in their downstream sales markets (retail markets), which means that the benefits from upstream purchasing markets are also passed on to end consumers. On the other hand, if buyers do not face sufficient competition in the downstream sales market, it is uncertain whether the benefits of buyer power will be passed on to end consumers. This passing-on argument is naturally challenging and complex, but in any case, the amendment is not entirely hostile to buying power. This very same passing-on logic has been occasionally applied in the case law of EU competition rules as well.

19. In the end, a retail chain has the right to put forward arguments (objective justifications) in its defence that may refute the unlawfulness of a conduct. Whereas a particular practice could in principle be interpreted as an abuse of dominant position, it may be acceptable if:

- the practice can be objectively justified as being essential; or
- it is a reasonable response to the actions of competitors; or
- the practice produces efficiency gains in a manner that does not put consumer interests at risk.

6. Conclusions.

20. When the Finnish Competition Authority's report on the grocery trade was published in 2012, the law in force at the time and the general prohibitions laid down in it were not considered an effective instrument. It was argued that the law lacked instruments to address the continuing concentration of the grocery markets and the welfare losses incurred by consumers and suppliers because of gradually diminishing competition. This development led to the drafting of the specific ban, as the strong market position of the two largest grocery chains in the sector and in the purchasing of grocery products was considered a specific concern to these markets.

21. The 2014 reform of the Competition Act was justified by the fact that, with the backing of their market power, the two largest grocery chains were able to secure for themselves favourable and advantageous terms of trade with suppliers without being restricted by competition or other restraints in the market mechanism. The reform obliged the two largest retail chains to comply with the duties of a dominant undertaking and to abandon abusive practices once the reform came into force. Above all, the objective was to influence the market conditions in the sector before the buyer power would lead to further concentration in it.

22. At the same time there is need to put the specific grocery sector ban into a perspective; in practice this grocery market provision is applicable to the two largest chains in the sector only. Thus far, the FCCA has not issued a single decision in which it would, by applying this specific provision, have prohibited any practices as abuse of dominant position under the sector specific ban. However, the sector specific provision has otherwise

been applied in few cases relating to a customer loyalty scheme and to a data sharing arrangement of grocery sector sales. No evidence of unlawful conduct could be found, however, and cases were closed without further actions.

23. While the number of decisions issued pursuant to the sector specific ban is limited, it should be stressed that the ban has most likely had pre-emptively positive effects on grocery markets when the two main grocery sector market players have re-evaluated their purchasing operations in order to eliminate abusive practices even in the case that they might dispute that a market share over 30% automatically equals to a dominant position.