Capturing the Anticompetitive Effects of Private Labels in the Grocery Sector: A Consumer Welfare Approach in EU Competition Law

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Contents
Capturing the Anticompetitive Effects of Private Labels in the Grocery Sector: A Consumer Welfare Approach in EU Competition Law ................................................................. 1

Chapter 1: Buyer Power, Private Labels and Consumer Welfare in the Grocery Retail Sector .......... 5
   1 A shift in power ........................................................................................................................................... 5
   2 Private Label Concerns ............................................................................................................................... 6
   3 The Response of Competition Authorities .............................................................................................. 8
   4 Why a Consumer Welfare Focus? ........................................................................................................... 9
   5 Structure of this Paper .............................................................................................................................. 11

Chapter 2: The Effects of PL Introduction on Price, Quality and Choice on the Grocery Market .......... 12
   1 Consumer welfare in EU Competition Law .............................................................................................. 12
   2 Interbrand Price Competition in the Context of PLs ............................................................................... 13
      2.1 Theoretically speaking: PLs may stimulate interbrand price competition ...................................... 14
      2.2 In practice: PLs may soften interbrand competition ....................................................................... 16
   3 Reasons to worry about retailer competition in a concentrated grocery retail sector? .................... 18
   4 Implications for Choice and Quality ....................................................................................................... 20
   5 Procompetitive Effects of PLs .................................................................................................................. 21
   6 Collusive Outcomes as a result of PL introduction? .............................................................................. 24
   7 Conclusions ............................................................................................................................................... 27

Chapter 3: Anticompetitive Effects Resulting from Private Label Offering – A Role for EU Competition Law? ......................................................................................... 28
   1 A Role for EU Competition Law ............................................................................................................. 28
   2 A Difficult Relationship ......................................................................................................................... 29
   3 Unwritten Contracts ................................................................................................................................. 31
   4 Uncertainty about bringing a successful challenge ............................................................................... 31

Chapter 4: Private Label-Related Concerns in the Framework of Art. 101 TFEU ................................. 33
   1 The Exchange of Commercially Sensitive Information between Competitors and Art. 101 TFEU ..... 33
      1.1 Exchange of information in EU competition Law ............................................................................ 33
      1.2 A Retailer carrying PLs: a competitor? ............................................................................................ 35
| Table 3 Who owns the shelves in Britain? | .......................................................... | 71 |
| Bibliography | ......................................................................................... | 72 |
| Books and Book Chapters | .................................................................................. | 72 |
| Journal Articles | .................................................................................. | 74 |
| Reports | ......................................................................................... | 76 |
| EU Legislation | .................................................................................. | 78 |
| Other EU Publications | .................................................................................. | 79 |
| EU Case Law | ......................................................................................... | 80 |
| EU Merger Decisions | .................................................................................. | 81 |
| Case Law from Other Jurisdictions | ................................................................................. | 81 |
| Press Releases | ......................................................................................... | 81 |
| Web Sites Sources | .................................................................................. | 83 |
Chapter 1: Buyer Power, Private Labels and Consumer Welfare in the Grocery Retail Sector

1 A shift in power

Historically, or at least since the time of the industrial revolution, it has been the case that producers were able to set the terms of the game in their dealings with retailers. Producers achieved economies of scale and production became concentrated in fewer and fewer hands, while retailers remained dispersed and powerless. Over time, however, the balance of power between the market participants started to shift and the rules of the game changed as well. Fears about the power of large retailers led to the introduction of the Robinson-Patman Act in the US in 1936 which served to protect the interests of smaller stores by prohibiting suppliers from offering different prices, services and allowances to different (i.e. larger) retailers. The growth of retailers, however, did not come to a halt. Big retailer chains continued to attain a high level of bargaining power, enabling them to impose conditions on producers.

Over the XXth century, stores became larger and larger, with supermarkets and department stores being dwarfed by hypermarkets offering thousands of products. The process of physical growth in retail has also been accompanied by concentration of ownership. The grocery retail sector in North-Western Europe in particular, has been concentrated with a tendency of becoming even more concentrated.

People’s grocery shopping habits have also changed: shopping trips nowadays may take longer (in terms of driving to the store, spending time shopping and waiting to checkout) but they have also become less frequent, with many families doing their shopping at a large chain once a week; the volume of purchases from one single place, however, has increased. The power of large retail chains has manifested itself in their ability to, among other things, introduce successfully copies of branded products (private labels), sold at a lower price and thus become competitors to their suppliers.

Private Labels (PLs) are not a recent development, though they currently are more powerful than they have ever been, and are likely to continue to grow. The first supermarket private labels were

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2 See Annex
3 Also encountered as private label brands, own brands, store brands or own labels
introduced by Sainsbury’s in Great Britain in 1869, and the model was eventually replicated by other European grocers including the Dutch Albert Heijn in 1895 and the French company Coop in 1923. Already in the 1940s, one of the most influential advertising scholars, Neil Borden, studied the effects of own label introduction on the success of branded goods in the US. It was not until recently, however, that PLs have caught the attention of competition law scholars, practitioners, and policy makers.

PLs may be defined as goods produced by a manufacturer at the request of a retailer. They are sold under the brand name of the retailer and distributed exclusively by the retailer that ordered them. These products are most often, though not always, lower-price imitations of successful brand-name products. PLs are characteristic of large retail chains and Limited Assortment Discounters (LADs) as small retailers do not have the capacity and financial strength to develop a private label program. The main difference between PLs sold in LADs and the ones sold in supermarkets, is that in LADs almost all products are private labels. Retail chains, on the other hand, sell both branded and own label goods. The EU grocery market has the highest market shares for private label products in the world notwithstanding their laggardly introduction in Eastern Europe.

2 Private Label Concerns

PL introduction has spurred complaints by branded firms about several issues. According to the brand suppliers, the retailers use PLs as a threat in order to obtain lower prices or other contributions (i.e. “If I don’t get a good deal from you, I may introduce a PL version”) thus further increasing their buyer power. Brand firms also noted that with the advent of PLs, the competition for shelf space has become very intense - the PL almost always brings the retailers higher margins than the brand and so is guaranteed

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4 The Private Label Manufacturers website acknowledges this fact: “Private label market share stands at its highest ever. The future promises even more private label as retailers expand internationally and take a larger role in marketing themselves and the products that they sell” (emphasis added). See <http://www.plmainternational.com/en/show_information_en2.htm> accessed 4 November 2009


7 Defined by the Commission as “products made by third parties upstream in the supply chain and sold under retailers’ brand”, see table on p.10 of European Commission “Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on food prices in Europe” (Communication on Food Prices) (2008) <http://ec.europa.eu/economy_finance/publications/publication13571_en.pdf> accessed 24 May 2010


9 There are also innovative PLs as well as PLs that are more expensive than brands, though this has not been the norm and is a fairly recent phenomenon.

10 LADs are for example Aldi, Lidl, and Netto

11 See for example the statistics provided by marketing research firm AC Nielsen at <http://uk.nielsen.com/insights/PrivateLabel.shtml> accessed 12 June, 2010
advantageous placement. Also, PLs are sold in packaging very similar to a certain brand product yet there has not been an avalanche of lawsuits on the basis of an Intellectual Property right (i.e. trademark or design) violation.12 The combined result of these practices, the brands claim is that the margins in the grocery production industry as a whole are being driven down, and thus incentives for innovation and maintenance of quality are being eroded.

But even more disturbing for the brands seems the fact that PLs transform the customer into a competitor13, and one who is in a position (and legally entitled)14 to fix the prices for both branded and private label goods, and to determine which product gets to sit on which shelf. The real losers of PL growth, however, seem have been the smaller brand producers – those whose brands were not “must-stock” items, and who have been and will be, over time, dropped by the retailers in favor of the own brand.15

There have been responses to buyer power concerns, including (though more limited) to private label concern on the part of competition authorities. The exercise of buyer power in the food industry has been on the Commission’s radar for some time now. In the late 1990s, the Commission hired Dobson Consulting, owned by Prof. Paul Dobson, an economist renowned for his expertise in buyer power, to study the grocery sector. The Report “Buyer Power and Its Impact on Competition In the Food Retail Distribution Sector of the European Union” was released in May 1999. In 2006, a separate study called “Report on Competitiveness of the European Food Industry: An economic and legal assessment”, ordered by DG Enterprise, was published. In 2008 the Commission issued a roadmap for future action in its Communication to the European Parliament, the Council, the Economic and Social Committee and the Committee of the Regions on Food Prices in Europe. In this concise document, accompanied by the more detailed Commission Staff Working Document, the Commission identified the following concerns with

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12 Pieter Kuipers, Deputy General Counsel of Unilever for Europe explains that while a brand firm would not think twice about launching a lawsuit against a competitor who is copying its products, it would be more wary to attack a retailer who is a major customer and owner of an essential grid of shelves. See P Kuipers, “Retailer and Private Labels: Asymmetry of Information, In-store Competition and Control of Shelf Space” in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009), p. 198


14 Resale price maintenance is still a hard-core restriction on competition. See European Commission Guidelines on Vertical Restraints (Guidelines on Vertical Restraints) [2010] OJ C 130/1, [223-229]

respect to private labels: “possible foreclosure of suppliers’ competing goods [and] restriction of in-store inter-brand competition”\textsuperscript{16}.

3 The Response of Competition Authorities

The European Commission has acknowledged that PLs “may lead to foreclosure effects as supplier of branded products become[s] a direct competitor to the retailer”\textsuperscript{17}. As a whole, its position toward PLs seems ambivalent: the Commission notes that PLs “widen the range of available products and thus represent an additional source of competition” but also recognized that the PL impact on price is ambiguous in the long-term.\textsuperscript{18} The Commission’s conclusion has been that “the effects of private labels on buyer power and on innovation in the food industry will continue to deserve attention”\textsuperscript{19}. Most recently, a High Level Group was appointed to study issues in the grocery supply chain and this group issued a report on \textit{The Competitiveness of the European Agro-Food Industry} which was published On 17 March 2009. The High Level Group consisted of ministers of agriculture, representatives from the industry, and of consumer associations and contains some recommendations for action to be taken. This report also mentions PLs, but fairly briefly. It confirmed the suspicions regarding private labels that had already been expressed by the Commission, and added several, mostly vague recommendations.\textsuperscript{20}

The grocery sector has also been eyed suspiciously by EU Member States’ competition authorities. In the UK, the Office of Fair Trading prompted the UK Competition Commission (UK CC) to investigate the grocery market twice in less than a decade (in 1999 and in 2006-2007). Grocery market investigations were carried out in Scandinavia\textsuperscript{21}, in the Baltic republics\textsuperscript{22}, and recently in Romania\textsuperscript{23}. The legislative responses to these investigations have been different. In the UK, the Supermarket Code of Practice (SCOP) intended for grocery retailers was adopted as a result of the 1999 market investigation; this code was replaced by an enhanced Groceries Supply Code of Practice in 2009. These reports discuss PLs but not extensively, with the notable exception of the Own-label Appendix to the 2008 Report on the UK market investigation.

\textsuperscript{16} Communication on Food Prices (above), p.10
\textsuperscript{17} Accompanying Document to the Commission’s Communication from 16 December 2008 (above), p.35
\textsuperscript{18} Accompanying Document to the Commission’s Communication from 16 December 2008 (above), p.35
\textsuperscript{19} Accompanying Document to the Commission’s Communication from 16 December 2008 (above), p. 32
\textsuperscript{20} For instance, the High Level Group noted that printing the actual producer’s name on the package of a PL product may result in fairer competition.
\textsuperscript{21} In September 2004 representatives from the national competition authorities from Denmark, Greenland, Iceland, Norway, Sweden, Finland and the Faroe islands formed a working group to study the competitiveness of food markets in the Nordic countries. The report, titled “Nordic Food Markets – A Taste for Competition” was published in November 2005 (above)
\textsuperscript{23} Cristina Mihai, “Romania: anti-competitive practices – food retailing” (2010) 31(4) ECLR, 48
Despite the complaints from brands, there is little case law related to PLs and despite the attention from authorities, there is little action undertaken to control PLs. Some mention that there seems to have been a presumption that PLs are overall good for consumer welfare and this presumption has acted as an “estoppel” to legal action against PLs.\textsuperscript{24} Others conclude that due to enforcement gaps in EU competition rules, there is not much scope for such action.\textsuperscript{25} This paper intends to investigate this assertions. It will first focus on showing that PL offerings by big supermarkets may result in a lessening of consumer welfare and thus produce anticompetitive effects. Then, it will examine the possibilities of capturing these effects in the framework of EU competition rules. It will highlight recent legislative changes and will consider their implications for the control of the anticompetitive effects of PLs. Finally, conclusions about the ability of competition rules as they stand to protect consumers from the welfare-reducing effects of PLs (where such effects exist) will be drawn.

4 Why a Consumer Welfare Focus?

Consumer welfare has become trendy in EU competition policy in recent years. Although there had been mention and certainly interest in establishing consumer welfare as one of the goals of EU competition policy before, consumer welfare as a legitimate, if not the ultimate goal of EU competition policy was proclaimed in former Commissioner Neelie Kroes’ speech at the Fordham Corporate Law Institute in 2005.\textsuperscript{26} There has been some skepticism regarding consumer welfare as a result of the judgment by the ECJ in Glaxosmithkline\textsuperscript{27} of 6 October 2009. In this judgment, the ECJ rejected the need to prove consumer harm as a pre-condition to finding restriction of competition by effect and affirmed that the

\textsuperscript{24} Andres Font Galarza, “Private Labels and Article 82 EC” in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009), p.129

\textsuperscript{25} This is the view expressed by Ariel Ezrachi in “Unchallenged Market Power? The Tale of Supermarkets, Private Labels and Competition Law” (2010) 33(2) World Competition; \url{http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1524718} accessed 13 June 2010

\textsuperscript{26} Neelie Kroes, “Preliminary Thoughts on Policy Review of Article 82” (Speech 05/537, delivered at the Fordham Corporate Law Institute in New York, 23rd September 2005). Kroes stated: “I like aggressive competition – including by dominant companies - and I don’t care if it may hurt competitors – as long as it ultimately benefits consumers. That is because the main and ultimate objective of Article 82 is to protect consumers [...]”

\textsuperscript{27} Joint cases C-501/06 P, C-513/06 P, C-515/06 P et C-519/06 P GlaxoSmithKline Services Unlimited, formerly Glaxo Wellcome plc v Commission of the European Communities (Glaxosmithkline)
goal of competition policy is protecting competition as such. However, judging by recent legislation and Commission publications, consumer welfare still has a role to play. The recently adopted Block Exemption Regulation on Vertical Restraints and the guidelines accompanying it confirm the importance, if not the primacy of the consumer welfare objective. Last but not least, the current Treaty on the European Union (TEU) mentions as a goal of the Union “a highly competitive social market economy” in Art. 3(3) and at the same time loosens the link between the internal market objective and competition policy.

Another reason to focus on consumer welfare is novelty. Consumer welfare is normally not the focal point of research on PLs. Competition law scholars have emphasized the harm inflicted on branded firms or own label suppliers; market investigations and reports seem to focus on addressing the specific complaints received, mainly from brand suppliers and from independent retailers. Economics research does touch upon consumer welfare, but there is a problem of the differing definitions of consumer welfare in economics and competition law. It is possible that analysis of the harm to branded producers may capture many of the welfare-reducing effects that could arise in the case of PLs (such as eroding incentives for innovation and improving or maintaining quality), it does not necessarily exhaust the subject of consumer detriment.

28 GlaxoSmithKline (above). The ECJ noted at paras. 59-60: “En effet, d’une part, il ne ressort aucunement de l’article 81, paragraphe 1, CE que seuls les accords privant les consommateurs de certains avantages pourraient avoir un objet anticoncurrentiel. D’autre part, l’article 81 CE vise, à l’instar des autres règles de concurrence énoncées dans le traité, à protéger non pas uniquement les intérêts des concurrents ou des consommateurs, mais la structure du marché et, ce faisant, la concurrence en tant que telle. Dès lors, la constatation de l’existence de l’objet anticoncurrentiel d’un accord ne saurait être subordonnée à ce que les consommateurs finals soient privés des avantages d’une concurrence efficace en termes d’approvisionnement ou de prix. Il s’ensuit que l’existence d’un objet anticoncurrentiel ne saurait être subordonnée à la preuve que l’accord comporte des inconvénients pour les consommateurs finals”

29 It is stated that: “This Regulation should not exempt vertical agreements containing restrictions which are likely to restrict competition and harm consumers or which are not indispensable to the attainment of the efficiency-enhancing effects” in Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices (Vertical Block Exemption Regulation) [2010] L 102/1 [10].

30 It is stated that “The objective of Article 101 is to ensure that undertakings do not use agreements – in this context, vertical agreements – to restrict competition on the market to the detriment of consumers” in European Commission Guidelines on Vertical Restraints (Guidelines on Vertical Restraints) [2010] OJ C 130/1 [7].

31 Previously, Art. 4 EC suggested that competition policy and internal market are closely linked. Now the goal of competition policy is at least visually separated from the market integration imperative. The link itself between the two is preserved in Protocol (No 27) On the Internal Market and Competition which states that “the internal market as set out in Article 3 of the Treaty on European Union includes a system ensuring that competition is not distorted”, though the roles seemed to be switched: the internal market ensures that there is competition, or competition policy ensures there is a functioning internal market?

32 This is the case, for example, with the UK CC Report on own label goods in Appendix 9.10. The UK CC mostly responds to the concerns raised by the British Brands Group (BBG) or by independent retailers.

33 In economics, consumer welfare is mostly considered to be consumer surplus - the difference between the consumer’s marginal willingness to pay (the Demand curve) and the final price he has to pay on the market for the good or service.

34 In EU Competition law, consumer welfare is mostly defined as lower prices, more choice and high quality.
5 Structure of this Paper

This paper will start out by reviewing the economics literature and other sources and placing the insights from these into a consumer welfare framework (Chapter 2). After identifying the anticompetitive effects\(^{35}\), the spotlight will be on competition law and how, and to what extent EU competition rules as they stand at the time of writing, may capture these effects. Chapter 3 will glance over some bottlenecks which may explain the paucity of case-law involving PLs. Chapters 4, 5, and 6 will assess the effects of PLs in light of, respectively, Article 101 TFEU and Commission Regulation (EU) 330/2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices (The Block Exemption Regulation)\(^{36}\), Article 102 TFEU, and Council Regulation (EC) No. 139/2004 on the control of concentrations between undertakings (the EC Merger Regulation)\(^{37}\). In these three chapters, reference will be made to the most recent guidelines and draft guidelines published by the Commission. Although a purely consumer welfare approach is not entirely possible\(^{38}\), each chapter will draw some conclusions about consumer welfare. Finally, conclusions will be drawn as to the applicability of EU competition rules to the effects of PLs and the implications for EU consumers.

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\(^{35}\) Although the focus is on the anti-competitive effects, the pro-competitive effects are also considered.

\(^{36}\) Commission Regulation (EU) 330/2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices (The Block Exemption Regulation) [2010] L 102/1


\(^{38}\) For example in some instances the incentives of brand suppliers to develop new products may be eroded. The concerns of the brand producer in this case are also concerns of the final consumer, who may wish to have more choice or better quality products.
Chapter 2: The Effects of PL Introduction on Price, Quality and Choice on the Grocery Market

1 Consumer welfare in EU Competition Law

There is hardly a sophisticated and coherent framework of consumer welfare in EU competition law. The Commission started inserting references to consumer welfare in policy documents not too long ago, and the definition given over and over is: low prices, higher quality, and more choice. It is not entirely clear how consumer welfare is assessed and whether price effects weigh more than effects on quality and innovation. There is some reason to think that price decreases or increases may be more important than the other “parameters of competition” from the Commission’s perspective: several policy documents use “increase in prices” as shorthand for increase in prices and quality degradation and less choice. Practitioner Phil Evans also suggests that the focus has been on price in established practices of assessing consumer welfare or detriment, and opines that “a more nuanced consumer detriment would use price as the primus inter pares of factors, but would also consider rewards for innovation, transparent market operation, and fairness”. The definition of consumer welfare, and respectively, harm, leaves something to be desired. This chapter, however, will stick to the definition as given by the Commission, and will look into the ways in which the introduction of PLs might affect the final prices that consumers pay for their groceries, and the choice and quality of the products available to consumers on the retail market as a whole.

39 European Commission Guidance on the Commission’s enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings* (Guidance paper on Article 82) [2009] OJ C 45/7 [19]; The discussion paper on Art. 82 also gives as example of consumer welfare “benefits to consumers, such as low prices, high quality products, a wide selection of goods and services, and innovation.” European Commission, “DG Competition discussion paper on the application of Article 82 of the Treaty to exclusionary abuses” (2005) <http://ec.europa.eu/competition/antitrust/art82/discpaper2005.pdf> accessed 6 June 2010 [4]; The new Guidelines on Vertical Restraints [2010] OJ C 130/1 state at [97]: “For vertical agreements to be restrictive of competition by effect they must affect actual or potential competition to such an extent that on the relevant market negative effects on prices, output, innovation, or the variety or quality of goods and services can be expected with a reasonable degree of probability. The likely negative effects on competition must be appreciable”. A number of press releases also use this definition of consumer welfare. See for instance Europa Press Release “Antitrust: consumer welfare at heart of Commission fight against abuses by dominant undertakings”, IP/08/1877 of 3 December 2008 <http://europa.eu/rapid/pressReleasesAction.do?reference=IP/08/1877&format=HTML&aged=0&language=EN&guiLanguage=en>; accessed 14 June 2010. Last but not least, former Commissioner Neelie Kroes’ speech (above) at Fordham in 2005 also talks about consumer welfare in these terms.

40 See for instance the Guidance paper on Article 82 [2009] OJ C 45/7 at [11]: “In this Communication, the expression ‘increase prices’ includes the power to maintain prices above the competitive level and is used as shorthand for the various ways in which the parameters of competition — such as prices, output, innovation, the variety or quality of goods or services — can be influenced to the advantage of the dominant undertaking and to the detriment of consumers”. The same shorthand is used in the European Commission Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings (Merger Guidelines) [2004] OJ C 31/03 at [8]

41 Phil Evans, “Assessing consumer detriment” (2007) ECLR 28(1), p. 34

42 Another point which is unclear is how to strike the balance between consumer harm suffered by some consumers against the welfare of other consumers but this point will not be addressed in this paper.
Vigorous competition in the grocery sector can benefit consumers directly in a number of ways. Competition between supermarkets could lead to nicer stores in convenient locations, offering a wide range of products at competitive prices; stores investing in improvements that lead to shorter checkout times, more payment options, fresher and better displayed products, and nice and helpful personnel. Competition between product suppliers could lead to cheaper products, higher quality, more innovation and thus more choice, products designed to meet a variety of consumer needs.

The introduction of PLs alters competition in the grocery sector, both among products (inter-brand) and among retailers, in several fundamental ways. With respect to the retailers, it increases their bargaining power vis-à-vis suppliers of brands. It also positions the retailer as a competitor of his suppliers while he is still in charge of setting the retail prices for both PLs and national brands (NBs) and while fully aware of the prices, promotion plans and other confidential information related to the brand. With respect to competition, PL introduction may soften intra-retailer competition as PL programs contribute to differentiation between competing retail stores and boost store loyalty. Finally, the information supplied by producers to retailers in the course of negotiating product launches, promotions and purchases, may result in collusive outcomes.

2 Interbrand Price Competition in the Context of PLs

Theoretically, the introduction of PLs can lead to lower product prices in several ways: PLs put competitive pressure on branded goods; they increase the bargaining power of the retailer vis-à-vis the suppliers of branded products, they are cheaper to produce so they sell for less.

PLs are sometimes described as “the revolutionary” - the underdog that challenges the lazy incumbent brand(s) on quality, offers a lower price, and ends up stealing its customers. Indeed, PLs have stolen substantial market share from brands, though the degree varies per category. They are also credited with the decrease in price in various categories of goods. For example, in a 2004 article, Richard Steiner cites evidence from one of the most prominent marketing scholars of the past century, Neil Borden, who conducted research on PLs in the 1940s in the US. In Borden’s framework, also supported by his price surveys, PLs reduced the prices of NBs by directly competing with them and by serving as a threat used by

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43 Usually, PLs are cheaper to bring to the market as they save on the advertising, marketing and, in the case of me-too products, Research and Development expenses that account for about 30-40% of the cost of a brand – see table 2.1 on p.27 in D Bell, “The Business Model for Manufacturers’ Brands” in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009).

As Bell explains, PLs do not need the advertising as they benefit from the reputation of a well-known retailer.

retailers to obtain lower prices from NB suppliers. Additionally, Steiner cites evidence from the 1960s, 1970s and 1980s of how PL introduction resulted in price reductions of leading national brands such as dishwashing detergents, aluminum foil wrap, ready-to-eat cereals, diapers, and detergent. On certain occasions, this has led to a strengthening of the brand as it repositioned itself or increased its perceived and or actual quality. In these cases, PLs have lost market share to NBs.

2.1 Theoretically speaking: PLs may stimulate interbrand price competition

PLs can, theoretically, lead to lower prices for NBs. The model of Bontems et al. (1999) shows that when PLs are of a comparable quality, their introduction could lead to a decrease in the price of an NB. In this situation, PLs are an effective competitive constraint on NBs and can thus lead the brand to reconsider its efficiency, innovativeness and its mark-up in order to meet the competition. When they are not of a quality comparable to that of NBs, PLs can still lead to a decrease in the price of an NB by increasing the bargaining power of a retailer. This situation is considered at length in the model by Mills (1995).

In Mills’ model, depending on the quality of a store brand (low, above a certain threshold, or above a specific quality threshold), the retailer chooses to introduce the PL, use it as a threat or not introduce it at all. When the PL is of a relatively high quality, its introduction or the threat to introduce it leads to a reduction in the prices that NB suppliers ask for; when the PL is of a very low quality, the threat of its introduction does not have an effect on the NB price. However, even in the latter case, the PL may still increase the retailer’s power because he might decide to improve the quality in the future. Thus, because the power to increase quality is a decision taken by the retailer, and not the PL manufacturer, the introduction of the PL in any case (whether of high or low quality) strengthens the position of the retailer in wholesale

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47 Fabian Bergès-Sennou, Philippe Bontems and Vincent. Réquillart. “Economics of Private Labels: A Survey of Literature” (2004) 2 Journal of Agricultural & Food Industrial Organization, p.9. The model allows the marginal production costs to vary with the increase in quality of the PL. Bontems et al. conclude that where the PL has higher production costs for the same quality as the brand. This scenario seems less likely to occur, because PLs in general have lower production costs than brands (because they save on advertising and R&D costs for one thing). Bontems et al. the introduction of a PL may lead to a short-term NB price decrease which could be followed by an NB price increase as the PL becomes too costly to produce. Where the PL does not face higher production costs, the price of the NB always decreases in proportion to the quality increase of the PL. The implication of this research is that the PL is a real threat to the NB when it is above a certain quality threshold.
48 Mills (1995) as seen in Fabian Bergès-Sennou, Philippe Bontems and Vincent. Réquillart. “Economics of Private Labels: A Survey of Literature” (2004) 2 Journal of Agricultural & Food Industrial Organization, p. 8. This model focuses on the situation in which PLs and NBs face identical production variable costs but have different fixed costs, the latter being the costs for advertising essential to branded products, but not for store brands.
49 In Mills’ model there are three scenarios in two of which the price of the NB decreases as a result of the increased bargaining power of the retailer.
51 Ibid., p. 11
price negotiations with the NB manufacturer. This conclusion is also supported in Bontems et al. In conclusion, both models (by Bontems et al. and by Mills) confirm that PLs could benefit consumers by leading to lower prices for NBs, though this result depends on whether and to what extent the retailer chooses to pass on the savings to the final consumer.

PLs may reduce prices in yet another way – by introducing value or budget options for a variety of products. Such PLs are not really in competition with NBs as they are of very low quality. Indeed, store brands have been applauded for their innovativeness in terms of price – by introducing “basic”, “value” or “budget” varieties of products. Because the low quality product is targeted at people who would normally not be buying the NB anyway, the price of the NB would likely stay the same or could increase to reaffirm the difference in quality.

Finally, again from a theoretical perspective, PLs could lead to lower consumer prices by eliminating the double marginalization problem. This model as well as the other models presented above rests on the assumption of a 2-player scenario, in which a retailer-monopolist and a brand-manufacturer-monopolist interact. This, however, is rarely the case in the real world. The retail markets in European Union countries are generally dominated by several big players and have oligopoly characteristics. Thus, while theoretically, PLs are likely to increase consumer welfare by lowering grocery prices, the characteristics of the downstream competition would have to be considered. But before that, it is worth looking into the opposite claims – that PLs may lead to higher grocery prices in the future both for own labels and for brands.

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52 Ibid., p.9. The logic of the model is as follows: as the quality of a PL improves, it also becomes more costly to produce; thus, while the price of the competing NB might decrease at first, the increasing costs of the higher quality product will make it uncompetitive. Then, the NB, which is more efficient will become a monopolist again – see p. 9


54 This might be the strategic response of a brand producer. As people assume that there is a relationship between price and quality, the NB might be tempted to rely on the PL setting the low price benchmark.

55 Some economic research points out to the potential of PLs to increase total and consumer welfare, by eliminating the inefficiencies associated with double-marginalization. When the retailer decides to stock PLs, he essentially integrates the downstream and the upstream level, thus reducing the inefficiencies that would arise when a monopolist-supplier and a monopolist-retailer both set a monopoly price for the product. For a general model of double marginalization, see Massimo Motta, Competition Policy: Theory and Practice (CUP, New York 2004), pp. 307-313. Also, Caprice discusses the elimination of double-marginalization in Fabian Bergès-Sennou, Philippe Bontems and Vincent Réquillart. “Economics of Private Labels: A Survey of Literature” (2004) 2 Journal of Agricultural & Food Industrial Organization., p.9

56 Ibid., p.7

57 D Bell, “The Business Model for Manufacturers' Brands” in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009), p. 31 table 2.4
2.2 In practice: PLs may soften interbrand competition

It has been suggested that competition between brands may also be weakened when a PL is introduced.\(^{58}\) For instance, the introduction of a PL might result in a situation in which the retailer sets an artificially high price for NBs in order to make the own brand seem cheaper (as opposed to lowering the price of the PL). Bronfrer and Chintagunta, in analyzing 5 stores and 104 categories over 104 weeks, suggest that the retailer might increase the price of an NB to induce the customers to try the own brand.\(^{59}\) Bronfrer and Chintagunta advance this argument in trying to explain their observation that the entry of a store brand tended to raise the prices of NBs in 50% of the cases. The retailer certainly has the incentive to do so because the Retail Gross Margins are often higher for PLs than they are for NBs\(^ {60}\), a finding also evidenced by the UK CC investigation\(^{61}\).

The introduction of a PL might prompt the retailer to orchestrate the prices in the store to his own advantage, in a way he may not have been able to do with separate brands. For instance, one of the concerns in retail competition is “umbrella pricing”. Umbrella pricing, as defined by the UK CC, refers to a situation in which the price of the NB “effectively sets an upper limit for the pricing structure of the entire product group”\(^{62}\). This might lead to a situation in which the cost of the private label is falling but its retail price stays the same, i.e. there is no pass-on to consumers of the efficiency gains.\(^{63}\) The UK CC was concerned that the prices of the own brands do not seem to be based on the marginal costs of the product, but rather were pegged to the price of the leading national brand.

This phenomenon is easily observable. In supermarkets, the price of the PL is almost always a certain percentage less than the price of the NB. This appears to be the case regardless of the product type or category. However, it seems unlikely that the PLs across very different categories would always be cheaper for the retailer to produce, and even when cheaper that they would always be within a certain percentage cheaper to produce than brands. This intuitive finding has been tested empirically and is supported by the model of Lynch which predicts with remarkable accuracy the prices of PLs. Lynch derived a simple formula

\(^{58}\) See, for instance Rainer Olbrich, Gundula Grewe, and Ruth Orenstrat, “Private Labels, Product Variety, and Price Competition – Lessons from the German Grocery Sector” in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009), at pp.247-257


\(^{61}\) The British retailers reported to the UK CC that absolute margins for PLs could be less, but still yielded a higher percentage margin than NBs. However, the budget PL lines often resulted in negative margins. Chapter on Pricing 2000 Report on the Supply of Groceries from Multiple Stores in the UK, p.139


\(^{63}\) Ibid., p.139
which predicts the PL price when the retail price of the national brands and the factory selling prices of both PLs and NBs are plugged in.\textsuperscript{64} Lynch’s formula was developed on the basis of data from the Chicago area grocery retail chain Dominick’s but was also shown to hold for the prices in the sample of own-label grocery products presented in the 2000 \textit{Report on the Supply of Groceries from Multiple Stores in the UK}.\textsuperscript{65}

The UK CC was unable to prove that umbrella pricing was occurring in the UK but it did acknowledge that the amount pass-through of direct cost savings from PLs to consumers in terms of lower price seemed to depend on the retailer and his competitive strategy.\textsuperscript{66} But while the UK CC was unable to \textit{prove} that the British chains were engaged in “umbrella pricing”, the doubts remain that they might in the future. Richard Steiner, for example warns that while the UK grocery sector seems to be competitive at present, as PLs continue to grow and the concentration in the industry increases, it will be increasingly difficult for consumers to make informed decisions about the relative prices between brands and PLs.\textsuperscript{67}

As for competition among the own brands of different retailers, it is not certain that PLs face competitive pressures from other PLs. Because they are distributed in different stores, PLs are more difficult to compare. According to Neil Borden, because consumers could not easily compare PLs across stores, retailers could charge a bit more for them than they would under normal competition circumstances but they exercised self-control so as not to appear more expensive than their competitors.\textsuperscript{68} This is also confirmed in the UK CC’s 2000 Report on Pricing.\textsuperscript{69}

The major competitive constraint on the retailer’s pricing freedom is exerted by strong competition from other retailers and the threat that potential competitors might enter the industry if there are excessive profits to be made. Thus, while PLs might help the retailer obtain better prices from his suppliers, these will only be passed on to the final consumer in the face of strong retailer competition. In the absence of such competition, PLs only contribute to the retailer’s own profit margins and further increase his buyer power.

\textsuperscript{64} Lynch’s model is discussed in R Steiner, “Market Power in Consumer Goods Industries” in Ariel Ezrachi and Ulf Bernitz (eds), \textit{Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition} (OUP, Oxford 2009), pp. 90-93

\textsuperscript{65} Discussed in R Steiner, “Market Power in Consumer Goods Industries” in Ariel Ezrachi and Ulf Bernitz (eds), \textit{Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition} (OUP, Oxford 2009), p. 92; See also Chapter 8 of the \textit{Report on the Supply of Groceries from Multiple Stores in the UK}, pp. 178-180

\textsuperscript{66} UK CC Grocery Report 2000 Chapter 7 (above), p.139. The UK CC analysis of supplier and retailer margins on own labels on a sample of five PLs showed that three retailers (Asda, Sainsbury, Tesco) passed ~2/3 or their direct cost savings; one retailer (Morrison) passed nearly all of these; while another one (Safeway) passed through only 1/3. It seems to depend on the competitive strategy of the retailer to determine how much to pass through to consumers.


\textsuperscript{69} UK CC Grocery Report 2000 Chapter 7 (above)
3 Reasons to worry about retailer competition in a concentrated grocery retail sector?

Retail markets are mostly local, defined by the UK CC in terms of the driving time (15 minutes) from one store to another. Stores have grown in size over the years, and new entry is not easy, mostly due to urban planning and zoning regulations, a point also raised in the UK CC investigations, as well as in merger cases. The UK CC found, for example, that urban planning in certain areas led to the result that certain stores have local dominance or even quasi-monopoly. The UK CC recommended that in deciding whether to grant land development permit for the opening of certain chain stores within 15 minutes of another store of the same chain should be carefully examined from a competition law perspective.

There has not only been a change in landscape in the last century, but also in lifestyle. In the past, when there were small neighborhood shops selling roughly the same goods or only brands, price comparisons were easier and “cheaper” (in terms of search costs) for the consumer. However, modern people are busy. As shops have grown in size, so have the distances between them and the checkout times. It is no longer as easy to be brand loyal where some of the preferred brands are stocked by one supermarket and others – by another. Pieter Kuipers talks about the different types of shopping trips that consumers might make and suggests that depending on how much choice a consumer wants, she might make several trips to several large stores each week, but, as he says “there is a limit, and [consumers] will not switch stores only for a couple of products, nor will they travel a long way to get the groceries they want.” It seems logical that people nowadays, busy as they are, are more sensitive to these switching costs. Kuipers notes that “the costs (including time spent) for the consumer to switch between stores is higher than choosing between different products in store.”

Another factor is that it is no longer reasonable to expect that retailers will compete on all products in their stores due to the large number of product offerings. Especially with less known brands or those with low customer loyalty, the retailer will unlikely be penalized by customers walking out of his store if he fails to

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70 In Kesko/Tuko, for instance, the Commission considered that it may take a retailer 5 years to obtain a permit to open a store and that Kesko owned too many spaces. Kesko/Tuko (Case IV/M.784) Commission Decision 97/277/EC [1997] OJ L 110/53
72 Ibid., p.7
73 For instance, he identifies “bulk-shopping trips” or indulgence shopping trips, or quick trips to buy something immediately needed in P Kuipers, “Retailer and Private Labels: Asymmetry of Information, In-store Competition and Control of Shelf Space” in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009) at pp. 205-206
75 Ibid., p. 206
provide these items at a competitive price. It certainly would be in the interest of customers if competition is taking place on as many product offerings as possible. However, supermarkets seem to be more concerned with the image that consumers have of them – for example as being an expensive supermarket, or a cheap supermarket.

This concern with image may lead to less genuine competition. For example, the UK Competition Commission survey in 1999 identified as a problem the fact that the big supermarkets focused their competition “on a relatively small proportion of their product lines” to create the image of being a store offering “lower value”, while at the same time “restrict[ing] active competition on the majority of product lines”(emphasis added). For this practice to be sustainable, the UK CC notes, the condition is that consumers should not be able to remember the prices of a lot of products as offered in the different stores and they should not notice that price competition is limited to certain “core” products or lines of products but the UK CC was unable to prove whether this was possible.

The concern with “store image” rather than intense competition on as many items as possible is evident in a different geographical market. In the Netherlands, supermarket prices are monitored by the Dutch Consumers’ Association which regularly issues reports on the price levels in the different retailers based on the price of a pre-determined shopping basket consisting of 120 different products. Because the composition of the basket never varies, Dutch supermarkets have effectively limited their competition to the products therein.

Comparing between brands in the same store may be difficult due to the difference in the package size and quality. Comparing PLs is even more difficult because own brands of different stores are not available for side-by-side comparison in the same store. As Richard Steiner has also pointed out, “interbrand competition among stores can never rise to [the intensity of intrabrand competition on famous brands] because many consumers will assume that there is a positive price/quality relationship and will not desert

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76 Robert Steiner, “The Nature and Benefits of National Brand/Private Label Competition”(2004) 24 Review of Industrial Organization, p. 120-121. According to Steiner, there are brands, referred to as “blind items” by retailers, where they allow themselves to charge purely unrestrained, monopolistic prices. This is so because of certain items, i.e. fringe brands, consumers are not expected to remember and be able to compare the price of that same item at a rival retailer.


78 The British retailers maintained that consumers should not be assumed to be unable to compare across many different products offered by different stores. However, the doubt remains that not many people are really able to compare the prices of many different products across stores.


Retailer A if his price on Brand X is higher than Retailer B’s on rival Brand Y”\(^{82}\). In his opinion interbrand competition within stores is much stronger than intrabrand competition, because customers can directly compare the items on the shelves, whereas comparing the different prices among stores would entail high search costs.\(^{83}\)

In light of the above discussion, retailer competition in the grocery sector these days may not be at its most vigorous. Such a conclusion puts doubt on the assumption in economic research that savings on NBs as a result of the PL-bolstered bargaining position of retailers will necessarily be passed on to the consumer and that competition among PLs will keep own brand prices in check. Thus, while PLs may increase interbrand competition in certain circumstances, the benefits (or a fair share of the benefits) from that competition may fail to reach the final consumer. In the case of weakened intrabrand competition, the PLs may simply serve the store’s own interest to the detriment of consumers.

### 3 Store Differentiation, store loyalty and intra-retailer competition

Economist Neil Borden argued that PLs were originally introduced as a means for the retailer to “be free from the direct price comparisons upon merchandise that consumers know to be identical”\(^{84}\). Borden’s explanations is as follows: brands spend a lot of money on advertising to make sure that their brand is desired by consumers. This increases their bargaining power and allows them to obtain better prices on their products from the retailers. The fact that they are selling identical goods, however, makes the competition between retailers fiercer. Both of these factors drive down the retail gross margins of retailers.\(^{85}\) Originally, retailers introduced PLs to differentiate themselves from rival retailers and to increase their bargaining power with brand manufacturers. Of course, it is undisputable that PLs are also a significant source of profit for supermarkets. However, it does not seem to be the primary reason why PLs are introduced. Borden’s logic is supported by empirical research.\(^{86}\) Bergès-Sennou et al., for example, cite a 1996 survey of French retailers which breaks down the reasons why French supermarkets develop PLs: to improve their competitive position against other retailers (34%)\(^{87}\), to better compete with the brands (58%)\(^{88}\). Semeijn et al. show that PLs add to the image of a supermarket and allow for better differentiation between supermarkets in the eyes of customers.

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82 Robert Steiner, “The Nature and Benefits of National Brand/Private Label Competition”\(^{2}\) Review of Industrial Organization, p. 120-121
83 Ibid., p. 121
85 Ibid., p.108-109s
87 To increase customer loyalty (16%), to improve positioning (18%)
It is tricky to compare store differentiation with brand differentiation. The latter is known to weaken price competition. Customers perceive the products as having distinct characteristics, whereas when products appear to be identical the customer will decide based on the price. Without PLs, the main way for stores to differentiate themselves would be the type and quality of services offered, the location of the store, the display, and the prices. With PLs, a store’s differentiation is boosted significantly because store brands can only be found in the respective chain. If a consumer really likes certain PLs in a specific store, she will more likely choose to do her shopping there.

In addition to contributing to store differentiation, PLs build store loyalty. It has been shown that PL programs may enhance the supermarket's image and customer loyalty. Ailawadi et al. cite a significant body of research confirming that store brand use is correlated with high store loyalty. They measure behavioral loyalty to a store by estimating the share of the wallet, the share of the items purchased and share of shopping trips that a certain retailer can claim. The research of Ailawadi et al. shows that increased PL use affects these measures significantly. While Ailawadi et al. distinguish that for very heavy PL-users, store loyalty is not important, they do confirm that PLs are an important positioning tool for retailers.

### 4 Implications for Choice and Quality

Even if PL introduction may drive down the prices of certain categories of products, their introduction may fail to boost other aspects of consumer welfare. Long-term quality and innovation may actually be impacted negatively as a result of the overwhelming success of PLs. Although it is often mentioned that PLs invigorate competition as they are essentially new products, a fact that may have been overlooked is that PLs usually substitute another product, for instance a less known or a regional brand. Empirical research by R. Olbrich for instance shows that there has been a decline in the number of listed national brands for the period 2000-2005 in Germany but that the decline was not compensated for by the addition of private labels. Olbrich
concludes that overall, there “has been a dramatic reduction of the variety of different products in the product group, to the detriment of the national brands”\textsuperscript{95}. Yet a private label is not like any other brand. PL’s defining characteristic is that their features are determined by the retailers and not by the production facility that actually makes them.\textsuperscript{96} And while it has been noted that PL quality has improved over time\textsuperscript{97}, and that innovation through PLs does happen\textsuperscript{98}, it is worth remembering that there are thousands of PLs in very different product categories. Richard Steiner notes that expensive R&D personnel are not easily affordable even for the largest retailers, not to mention for the PL producers who operate on very thin margins.\textsuperscript{99} The reason according to Steiner is, on the one hand, that PLs need to be priced competitively, so the revenue would not be sufficient to finance R&D; also, he notes that there are PLs in almost 300 categories of products.\textsuperscript{100}

Apart from the issue of paying for R&D while keeping prices competitively low, it would be difficult for a retailer to develop the specialist knowledge needed to excel in the making of all products.\textsuperscript{101} Finally, quality and innovation are not just a matter of the capacity but also a matter of strategic choice. Berges-Sennou note that “the strategic choice of product quality by a retailer and a producer is not identical”, the retailer being inclined to introduce a less differentiated product than one of his supplier would have.\textsuperscript{102} The choice of differentiated products for consumers will thus be reduced where a supermarket only sells one brand and a copycat PL.

True, innovation incentives have not entirely dried up as a result of PL introduction. The UK CC shows evidence from Mintel, a leading market research firm, showing that innovation is still vigorous in the UK and also that market shares have not been completely stolen by PLs, but rather tend to go back and forth between brands and PLs.\textsuperscript{103} This has been confirmed by other studies.\textsuperscript{104} Indeed, R. Steiner has noted that

\begin{itemize}
  \item \textsuperscript{95} Rainer Olbrich, Gundula Grewe, and Ruth Orenstrat, “Private Labels, Product Variety, and Price Competition – Lessons from the German Grocery Sector” in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009), p.249
  \item \textsuperscript{96} Fabian Bergès-Sennou, Philippe Bontems and Vincent. Réquillart (2004) on p.11; R Steiner (2004) on p.117 also notes that usually retailers do not “integrate backwards”; rather, they contracts for PLs with PL producers.
  \item \textsuperscript{97} R Steiner (2004) p.117
  \item \textsuperscript{98} P Dobson and R Chakraborty “Private Labels and Branded Goods: Consumers’ ‘Horrors’ and ‘Heroes’” in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009) pp.107 -124; also UK CC “Appendix 9.10: Own-label Goods” in Groceries Market Investigation (Final Report) (2008) at [38]. Also at [45], the UK CC notes that own labels could be credit with some innovations such as introducing “developing category ranges of basics, healthy, kids, organic and premium own-label products”.
  \item \textsuperscript{99} R Steiner (2004), p. 118
  \item \textsuperscript{100} Ibid., p. 118
  \item \textsuperscript{101} This view is confirmed in an article by Tim Condon “Brand new: Wal-Mart’s Foray into Private Labels” New York University Sternbusiness Winter 2002, 42. Condon stated that “[Wal-Mart] does not have the culture or the research and development facilities to become a true innovator across thousands of categories” cited in Doris Hildebrand, “Thirty years prohibition of resale price maintenance – Germany on the verge of change” (2005) 26 (4) ECLR, 235
  \item \textsuperscript{102} Fabian Bergès-Sennou, Philippe Bontems and Vincent. Réquillart (2004),p.19
  \item \textsuperscript{103} UK CC referring to Mintel’s Own Label Food and Drink report from October 2006 in Appendix 9.10: Own-label Goods” in Groceries Market Investigation (Final Report) (2008) [43] and footnote 27 thereto.
\end{itemize}
imitation from PLs has induced many producers, for instance Procter and Gamble, to innovate and become more sophisticated\textsuperscript{105}. Steiner calls innovation “one of the strongest competitive weapons against private labels in the manufacturer’s arsenal” and notes that rapid innovation by a brand may make a PL seem outdated and thus cause it to lose market share to the NB.\textsuperscript{106}

Yet PLs have not always lagged behind for too long. Brand manufacturers in the UK complained in the course of the latest investigation that with respect to new product launches retailers “could demand access to brand manufacturer’s marketing plans and new product plans (six months or more before launch)” which they could then strategically exploit to develop their own PL copy and promote it very soon after or even at the time that the brand’s new product is launched, thus giving them a first-mover advantage even with respect to imitation, as non-retailer affiliated imitators do not have access to such information.\textsuperscript{107}

Although the UK CC investigation revealed that “some suppliers are becoming more careful about releasing commercially-sensitive information about new products to retailers [and that] [t]hese suppliers have identified an advantage in limiting the sensitive information that is provided to retailers”\textsuperscript{108}, the doubt remains as to the implications for innovation incentives in the grocery industry where information is misused.

It is precisely because of the preciousness of incentives to innovation that intellectual property rights are strictly guarded. For the same reason, preserving brand competition is also important. The latter has been recognized in several merger assessments of the European Commission. In \textit{Kimberly-Clark/Scott} the Commission found that it was “branded, and not private-label, products promote innovation and product quality improvement”.\textsuperscript{109} It went on to state:

“Product innovation is a key competitive tool in consumer product markets. It is well established in almost all consumer product markets that product innovation is pioneered by branded producers and that private-label products follow. In general, private-label products are rarely innovative products that generate new users and new occasions of consumption. Instead they tend to be price followers and product imitators.”\textsuperscript{110}

\textsuperscript{104} Ibid., Figure 5.2 Private label category shares in UK grocery retailing for 1997 and 2007; the table compares the market shares of the different categories of PLs a decade apart. (see Annex) The table shows that there have been both increases and decreases in market share over time. (source of data is from Nielsen Homescan, a type of research service provided by AC Nielsen, a global marketing research firm)

\textsuperscript{105} R Steiner [2004], p.118

\textsuperscript{106} Ibid., p. 118

\textsuperscript{107} Appendix 9.10: Own-label Goods” in \textit{Groceries Market Investigation} (Final Report) (2008), [40] footnote 23

\textsuperscript{108} Ibid., [40]

\textsuperscript{109} \textit{Kimberly-Clark/Scott} (Case IV/M.623) Commission Decision of 16 January, [161]

\textsuperscript{110} Ibid.,[162]
In the Kimberly-Clark/Scott case, the Commission also recognized the need to preserve competition among brands in light of their important function as innovators and quality benchmark setters. While agreeing that the own label paper products in the UK and Ireland had “the most well-developed, highest quality and aggressively marketed store brand segments in all of Europe [...] and] the most sophisticated and competitive retail grocery chains in Europe”, the Commission also said that this does not “remove the need for effective brand competition”.

In conclusion, while retailers do innovate, their innovation is not on the same scale and scope as that which can be achieved by companies which are specifically in the business of developing new products. Brands still have a role to play and the incentives to participate in the innovation race need to be preserved. PLs may keep the brand honest, but mostly they keep it honest about production costs.

5 Procompetitive Effects of PLs

Dobson and Chakraborty suggest that PLs might have an important role to play when the brands have become a “horror”. They explain that the introduction of a PL may alleviate consumer welfare detriment inflicted by brands in the following “horror” scenarios: where a brand is dominant and behaves aggressively or in a predatory manner, or deliberately raising the costs for other brands; where it leverages its position in different categories by using its market dominance in another market to kick other brands out of the market through tying and refusing to supply; where a brand has various lines of products and it forces them on its customers to foreclose its rivals.

In such situations, own brands backed by a powerful retailer can come in and save the day. They can challenge the brand on price and innovation by introducing a product with equivalent or better quality than the brand. As they are developed by retailers who have good knowledge of consumer habits and needs, PLs may surprise us with original product ideas or with value alternative of very pricey products. PLs in the UK have innovated by introducing healthy options, kids options, organic, and ethnic meal options as well as ready to eat chilled meals.

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111 Ibid., [48]
112 Ibid., [50]
113 Ibid., [51]
115 Ibid., p 106
116 Ibid., p. 107
117 Ibid., 115-116
118 Ibid., p. 115
119 Ibid., p. 116
6 Collusive Outcomes as a result of PL introduction?

As discussed above, retailers have a privileged position as a customer that allows them access to their competitors’ new product plans and promotions. This, among other things, allows them to develop their own copycat PLs very quickly after the launch of a new product of the brand. Peter Kuipers, Deputy General Counsel of Unilever for Europe, notes that retailers receive access to confidential information including new product developments, promotion plans and prices of its suppliers and this is legitimate because as a customer it needs this information to plan for product introductions and promotions. He notes that avoiding to tell this information may simply not be possible for the brand because “you simply have to tell your customer about [new product developments] in order to plan things.”

However, often the retailer uses the information it legitimately obtained as a customer, to develop its competing private labels or to decide on the prices and promotions for its own label. While the practice of imitating might be attacked under Intellectual Property or consumer protection laws, the exchange of information between a customer who is also a competitor, and the ability of such a double-hatted agent to fix both prices in the end, deserve attention from competition authorities.

In the Kesko/Tuko decision, the Commission noted:

“ [...] recent developments in retailing will enhance the buying power of the merged entity. In particular, private label development is a key element in the power wielded by retailers vis-à-vis branded daily consumer-goods producers. It enables retailers, who are inevitably privy to commercially sensitive details regarding the branded goods producers’ product launches and promotional strategies, to act as competitors as well as key customers of the producers. This privileged position increases the leverage enjoyed by retailers over branded-goods producers. Both Kesko and Tuko already market successful private label products.”

122 Alastair Gorrie, “Retail Competition: The Use of Ex-ante and Ex-post Remedies” in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009), p. 314
124 Ibid., p.194
125 Ibid., p.194
The finding of information exchange was further confirmed in the merger decision in Procter and Gamble/Gillette.\textsuperscript{127}

The fact that retailers may use their suppliers’ information to launch competing products is important in terms of pricing decisions, and also with respect to the quality decisions made by a retailer. It is yet another reason not to view PLs as just any other brand. If PL suppliers were instead developing brands of their own, they would be developing these in the absence of knowledge of the quality and specific characteristics or selling points of their rivals. They would have to strive to develop the best possible quality for the price they are attempting to match or beat and they would have the incentive to be the best. This incentive is seriously compromised if information about competitor’s plans is available, as it might be most rational to only strive to achieve a certain quality for a certain price, i.e. to become a price/quality follower.

If collusive outcomes (as if retailer and supplier had colluded, although on the supplier’s side the collusion might be termed involuntary) in terms of quality may be difficult to prove, collusive outcomes in terms of prices are certainly possible. Theoretical models from economics confirm the potential for collusion, or at least for a “peaceful and profitable co-existence” of advertised national brands and private labels.\textsuperscript{128} Kim and Parker expressed suspicions that the retailers might be setting monopolistic prices for both brands and private labels, while at the same time using “promotion rivalry and large-scale advertising campaigns [to] give the additional\textsuperscript{129} appearance of competitive strategy (e.g., to the public)”\textsuperscript{130}. The anonymous interviews conducted by N. Kim and P. Parker with supermarket managers confirmed that coordination was indeed taking place.

\textsuperscript{127} Procter & Gamble/Gillette (Case COMP/M.3732) Commission Decision of 15 July 2005; at [124] the Commission stated: “Since the retailers know the prices of the goods offered by the parties, they have the advantage to be in a position to fix the prices for their own private labels in reaction to the producers of branded products. In contrast, these producers are not able to readjust their prices to the retailers' private label prices. Therefore, the retailer has the capacity to counteract efficiently against the leading brands of the parties with its own private labels, whilst the parties have an asymmetry of information vis-à-vis prices for private labels”

\textsuperscript{128} Namwoon Kim and Philip M. Parker, “Collusive Conduct in private label markets”, (1999)\textit{16} International Journal of Research in Marketing, p. 143

\textsuperscript{129} Kim and Parker explain a strategy engaged by retailers and brands in order to segment the market: the NBs use a two-tier branding strategy – developing two brands – one cheap brand to compete with PLs, and another – to appeal to those willing to pay the price premium for a NB; kim and parker note “the co-existence and apparent stability of these segments may allow all players to price discriminate within an unofficial cartel”. – p.154. This model is also explained in Levy on p. 8 my copy where he notes that the strategic conduct that the Commission took into account in its examination of the KCS proposed merger, is well known in economics and marketing – it is referred to as the ‘two-tier marketing’ where two brands are developed – a premium-priced brand and a lower-priced ‘figting brand’ which channels the competition with the private label, thus allowing the manufacturer to avoid price wars with the PL”.

\textsuperscript{130} Namwoon Kim and Philip M. Parker, “Collusive Conduct in private label markets”, (1999)\textit{16} International Journal of Research in Marketing, pp. 154
7 Conclusions

This chapter has shown that anticompetitive effects from the introduction of own brands are possible and can translate into lessening of consumer welfare. PLs strengthen the bargaining power of retailers towards their suppliers, thus eroding suppliers’ margins, but the cost savings from the fiercer bargaining are not necessarily passed on. The ability of the retailer to determine the prices for both NBs and PLs could lead to supracompetitive prices or collusive outcomes in terms of both price and quality. When they profit from the misuse of supplier’s information by retailers, PLs may erode the incentives of brands to innovate and invest in quality development. The argument was also made that private labels may soften competition between retailers by contributing to the differentiation of stores from one another.
Chapter 3: Anticompetitive Effects Resulting from Private Label Offering – A Role for EU Competition Law?

“To state what is obvious but fundamental, competition law enforcement should condemn and remedy and possibly punish breaches of the law, either existing ones or newly-recognized ones. It is not intended in the first place to change how the marketplace functions, although this will normally be a consequence of its invocation.”

Ian Forrester (2007)

1 A Role for EU Competition Law

It is clear that competition rules should not be bent to capture structural effects where these are the result of legitimate practices. Legal certainty would be jeopardized if competition rules were used to punish retailers for developing private labels programs if it was not forbidden to carry PLs in the first place. If the reason for the anticompetitive effects of legal conduct is that competition between retailers is weak in general, though even more so because of growth in private label use, there is little applicability to competition law rules ex post. Alternatively, there might be a role for regulators and legislators. However, where there exist identifiable anticompetitive practices, competition law can help.

For instance, the higher prices for PLs and NBs resulting from PL introduction may prompt an examination as excessive pricing while in a possession of an essential facility (a network of shelves). Such an examination would fall under Art. 102. If the higher prices can be traced to the retailer’s use of information about competitor’s prices or future plans regarding promotions and product developments, Art. 101 rules on collusion may be applicable. Where consumers face less choice in grocery stores because PL introduction has led to the de-listing of differentiated products and crowding out of brands by PLs in general, both Art. 101 and 102 may apply depending on the case.

There have been complaints about retailer practices, though they have not necessarily been phrased this way. Complaints have focused on the position of brands, and the way they are treated by powerful retailers in general or specifically in the context of own PLs. Complaints, however, have failed to translate in actual cases. The scarcity of case-law is surprising especially given the vociferousness of brand producers with respect to, for instance discriminating in favor of own label products to the detriment of branded goods.

On a separate note, private label cases would be expected to arise if not under competition rules, at least under Intellectual Property laws, as the majority of PLs blatantly copy the design and/or trademarks of major brands. But despite the complaints on numerous grounds, actual litigation levels are low. On the European level, the only decisions where issues related to private labels are addressed seem to have been merger decisions.

2 A Difficult Relationship

One often advanced reason for the absence of case-law is the fear on the part of the suppliers to bring action against an important customer. For example, in the course of the market investigation in the UK, suppliers were invited to give information about their relationships with large retailers to the UK Competition Commission. Although some suppliers jumped at the opportunity to provide feedback, the response rate was not high. The UK CC noted the strong concern of suppliers, among them even large suppliers were not willing to bring an action against an important customer. The UK CC also noted the strong concern of suppliers, among them even large suppliers were not willing to bring an action against an important customer.

Footnotes:

132 For example, the CIAA has expressed concern over retailers’ anti-competitive practices and has added to the list of abusive practices identified by the Commission the following: “chronically late payments, long payment periods for suppliers, ‘forced’ discounts [from food suppliers] to meet buyers’ targets, ‘forced’ contributions to finance mergers and acquisitions”. See: Jess Halliday, "Calls for supplier relations watchdog; retailers disagree", 6 Aug 2009. Available at: http://www.foodanddrinkeurope.com/Retail/Calls-for-supplier-relations-watchdog-retailers-disagree; accessed on 4 Nov 2009; as well as Sarah Hills, “New Code Proposed for Retailer-Supplier Deals”, 5 Mar 2009. Available at: http://www.foodproductiondaily.com/Supply-Chain/New-code-proposed-for-retailer-supplier-deals; accessed on 4 Nov 2009; Other practices include also retailers taking advantage of price knowledge asymmetries (See Arnold & Porter LLP publication, “Private Label Brands, “Must-Have” Brands, and Their Impact on Retailer Buyer Power”, FMCG Issues, February 2009, p. 4). Another concern has been the practice of imposing unfair and/or unexpected costs on suppliers, listing fees and promotion contributions, as well as requiring the supplier to bear the costs of inaccurate forecasts or customer complaints. See excerpt from interview with Peter Freeman, Competition Commission Chairman and Chairman of the Groceries Inquiry in Daniel Palmer, “UK supermarkets face new code of conduct designed to protect suppliers” Australian Food News website (27 February 2009)< http://www.ausfoodnews.com.au/2009/02/27/uk-supermarkets-face-new-code-of-conduct-designed-to-protect-suppliers.html > accessed 15 June 2010

133 As the retailer also competes upstream, it has incentives to place its own products on more visible shelves, and to run better promotions for its own products. All of these practices need not be directly related to the retailer having its own brand – the retailer may engage in some of them anyway in order to increase its bargaining power vis-à-vis the food supplier, and thus to be able to obtain better purchasing terms.

multinationals, about confidentiality.\textsuperscript{135} Even though their anonymity was guaranteed by the UK CC, many suppliers still chose not to submit evidence or respond to the questionnaires sent to them.\textsuperscript{136} One supplier put it this way “it would be commercial suicide for any supplier to give a true and honest account of all aspects of relationships with retailers”.\textsuperscript{137}

This is not surprising given the crucial importance of retailers for all suppliers, from the smallest to the largest. The imbalance of power was noted by the EU Commission in \textit{Procter & Gamble/Gillette}, where it was implied a retailer is more important to the supplier than the supplier is to the retailer – in the proposed merger under review, the combined sales of P&G and Gillette were found to be no more than 2\% of the sales of the retailers, whereas for them certain retailers accounted for 10\% and more of all the sales in a country.\textsuperscript{138} The Commission found that even after the merger, these two powerful international suppliers who own must-stock” brands would still be constrained by the power of retailers and would not be able to behave independently.

It was found that the proposed concentration would be constrained by the “multiple sourcing strategy” which retailers embrace. This is a sourcing strategy relying on multiple suppliers with the objective to avoid dependence on a single supplier and which would allow for cheap and efficient substitution of the supplier with other suppliers.\textsuperscript{139} The Commission’s surveys revealed that retailers would “never renounce to a multiple sourcing strategy and to the ownership of own private label products that compete with branded ones”, all in order to reinforce their bargaining position.\textsuperscript{140} Also in \textit{Rewe/Meinl}, the Commission recognized that switching between sales channels is very difficult for producers, if not impossible in the short term.\textsuperscript{141} In conclusion, losing the business of a major retailer could be detrimental for a supplier because it might lose economies of scale and lose competitive

\textsuperscript{136} Ibid,[11.23] on p. 234
\textsuperscript{137} Ibid. 2000 [11.27] on p. 235
\textsuperscript{138} \textit{Procter & Gamble/Gillette} (Case COMP/M.3732) Commission Decision of 15 July 2005 [125]. The UK CC grocery market investigation of 1999 for instance reported that a supermarket could have anywhere from 1600 to 2000+ individual suppliers. See UK CC Chapter 11 in \textit{Supermarkets: A report on the supply of groceries from multiple stores in the United Kingdom} (2000) table 11.1 on p.231
\textsuperscript{139} \textit{Procter & Gamble/Gillette} [126]
\textsuperscript{140} \textit{Procter & Gamble/Gillette} [126]
\textsuperscript{141} \textit{Rewe/Meinl} (Case IV/M.1221) Commission Decision 1999/674/EC [1999] L 274/1 at [80] and also at [102]: “It must be borne in mind here firstly that, when they lose a major customer, producers do not have much in the way of alternatives. In the food-retailing trade - especially if the firm concerned is already on the list of the leading competitor Spar - only small competitors are left, and they are hardly in a position to take up a large share of turnover. Switching to other sales channels is difficult, costly and, in the short term at least, generally impossible.”
advantages vis-à-vis other competing suppliers.\textsuperscript{142} Suppliers would not only lose short term profits if they behaved independently, but they might also lose the loyalty of final consumers who, in the absence of their preferred brand might decide to try a competitor’s product.

3 Unwritten Contracts

Another reason for the lack of cases involving private labels might be the nature of doing business in the sector. The close study of the industry carried out by the UK Competition revealed that the majority of contracts between suppliers and producers are unwritten. Indeed, the UK Commission noted that “full written agreements between the main parties [supermarkets] and their suppliers are unusual[!]”\textsuperscript{143} Both suppliers and retailers confirmed that the majority of their disputes were resolved through (mostly oral) negotiation and “it was extremely rare for legal departments to become involved”\textsuperscript{144}. Suppliers submitted to the competition authority that they would actually prefer to have written contracts.\textsuperscript{145} In the absence of written contracts, potential abuse or unfair, restrictive terms would be much more difficult to prove in court. Given the fact that it is still difficult for consumers to bring class action suits under EU competition rules, it might fall on the EU Commission or the national competition authorities (NCAs) to use competition rules to deter or punish anticompetitive actions.

4 Uncertainty about bringing a successful challenge

Another reason for the reluctance to sue might be the fact that legal action is costly. Suppliers operating on thin margins may be particularly hesitant to take action if it is unclear how EU competition rules as they stand might be applied to the practices of supermarkets. EU Competition rules, which generally form the backbone of Member States’ own competition rules, provide for agreements or concerted practices which are anticompetitive by object or effect (Art. 101 TFEU) and for unilateral practices leading to exploitation of consumers or foreclosure of competitors through exclusion (Art. 102 TFEU) yet it has been suggested that these rules may be difficult to apply to powerful retailers, for instance because most retailers would fall below the market share thresholds associated with a finding of

\textsuperscript{142} Alastair Gorrie, “Competition Between Branded and Private Label Goods. Do Competition Concerns Arise When A Customer is Also a Competitor?” (2006) 27 (5) ECLR , 225-226
\textsuperscript{145} UK Competition Commission, UK Grocery Report 2000 Chapter 11 [11.56] on p. 240
dominance.\textsuperscript{146} The next sections will closely look at the ways in which EU competition rules may catch the practices identified in the beginning of the chapter, and thus alleviate the consumer-welfare reducing effects arising from private label introduction. As the Commission has recently adopted several policy documents, reference will be made to the newest documents available.

Chapter 4: Private Label-Related Concerns in the Framework of Art. 101 TFEU

There have been suggestions that Art. 101 TFEU may be instrumental in curtailing some of the anticompetitive effects related to private labels discussed in the previous chapters (higher prices; in the long run less choice and lower quality). One of the possibilities is to control for the distortion of genuine competition on price, as well as quality and innovation, by restricting the exchange of information between retailers and suppliers. In seeking to preserve product choice for consumers both in the short and long-run, an examination of de-listing practices by a PL-carrying retailer may be examined under the rules on vertical restraints. The discussion will be in light of the recently adopted guidelines on vertical restraints.

1 The Exchange of Commercially Sensitive Information between Competitors and Art. 101 TFEU

1.1 Exchange of information in EU competition Law

The underlying principle of Art. 101(1) is that “each economic operator must determine independently the policy, which he intends to adopt on the market” (emphasis added). The Horizontal Guidelines of 2004 identify as collusive the conduct adopted by at least one undertaking or a contractual obligation such that “the uncertainty as to [parties’] conduct on the market is eliminated or at least substantially reduced.” This principle applies to cartels as much as to vertical restraints.

When competitors exchange information, they are essentially reducing their uncertainty as to each other’s conduct on the market and the result is a suboptimal outcome with respect to price, output and product characteristics. Not surprisingly, the Commission has kept an eye on information sharing for a long time – information sharing has been formally acknowledged as a form of co-operation falling under article 101(1) since 1968 when the Commission first provided guidance on the assessment of information exchange in the 1968 Commission Notice on Cooperation Agreements. In this document for example, the

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147 Alastair Gorrie, “Competition Between Branded and Private Label Goods. Do Competition Concerns Arise When A Customer is Also a Competitor?” (2006) 27 (5) ECLR, 224-227
148 Ibid., pp. 224-227
149 European Commission Guidelines on the application of Article 81(3) of the Treaty (Horizontal Guidelines) [2004] OJ C 101/08 [14]
150 Ibid.,[15]
151 In the case of PLs, for example, where a retailer requests that an own-label supplier sell own-labels only to him (i.e. contracts for exclusive supply with the own label producer), he is certain that a rival retailer will not be able to obtain the same product from that particular supplier. While the rival retailer may still find a supplier to produce the good in question, he has less choice to the type of supplier, i.e. he is foreclosed as to the full competition on the upstream market and the competing retailer knows that.
Commission excluded from exemption information exchange in an oligopolistic market for homogenous products where the exchange would serve as a ‘device for facilitating either the coordination of [the companies’] commercial behavior or the adoption of a common industry response to market indicators’ 153.

Later on, in its Report on Competition Policy 1977 (Volume VII), the Commission stated that it would regard as anticompetitive practices by object or effect the following type of organized exchange of information from individual undertakings: “figures or quantities produced and sold, prices and terms for discounts, higher and lower rates, credit notes, and general terms of sale, delivery and payment” 154. The most onerous type of exchange of information was considered that which related to prices, output, product introductions, and especially so when the information specifies these parameters in the future. 155. The reason is that this type of information can lead to a collusive outcome and “may allow competitors to arrive at a common higher price level without incurring the risk of losing market share or triggering a price war during the period of adjustment to new prices.” 156.

The 1968 notice has been replaced by subsequent notices; currently in force are the 2001 the Guidelines on the applicability of Article 81 of the EC Treaty to horizontal cooperation Agreements of 2001 157, which, interestingly, are silent on the issue of information exchange 158. These guidelines however are about to expire, and there is a draft of the new guidelines available. 159. The novelty of the Draft guidelines is that they include a chapter specifically dedicated to the assessment of information exchange between undertakings. 160. This chapter is also the most extensive guidance on the approach that the Commission or another competition authority in the EU would take in assessing the anti-competitive effects related to an information exchange. The Commission explains the inclusion of this chapter with the “strong demand from stakeholders and national competition authorities for extensive guidance on the assessment of information exchange” 161 as well as the need to strengthen legal certainty.

156 Draft horizontal co-operation Guidelines[67]
157 Guidelines on the applicability of Article 81 of the EC Treaty to horizontal cooperation Agreements (2001/C 3/02) [6-7]
159 The Commission is carrying out public consultation on its Draft Guidelines on the applicability of Article 101 of the Treaty on the Functioning of the European Union to horizontal co-operation agreements until 25th June 2010.
As was discussed in chapter two, information exchange is taking place between retailers carrying PLs and their suppliers. Part of it is simply in the course of business as the retailer is a customer of the supplier and as such knows the price at which the suppliers’ goods are sold – after all, it is the one negotiating the prices, volumes, and discounts. Additionally, the retailers have some knowledge of the cost structure of the brand as in the course of negotiation they know what discount they may and may not be able to secure; also, retailers are notified of new product developments, and receive information about the characteristics of the product. At the same time, the retailers make decisions as to the prices and volumes of their own labels, which compete on the same shelves with the brands. Alastair Gorrie notes such an exchange of information would not be exonerated if it were to occur among retailers themselves or amongst suppliers. He suggests that Art. 101 may be used to condemn the information exchanges as if it were between competitors.\footnote{Alastair Gorrie, “Retail Competition: The Use of Ex-ante and Ex-post Remedies” in Ariel Ezrachi and Ulf Bernitz (eds), \textit{Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition} (OUP, Oxford 2009), p.313-315} Yet, a question that he does not consider is whether a retailer would actually be considered a competitor of a brand supplier.

### 1.2 A Retailer carrying PLs: a competitor?

In EU competition law the following definition of actual or potential competitors is in use:

Two companies are treated as actual competitors if they are active on the same relevant market. A company is treated as a potential competitor of another company if, absent the agreement, in case of a small but permanent increase in relative prices it is likely that this first company, within a short period of time, would undertake the necessary additional investments or other necessary switching costs to enter the relevant market on which the other company is active.\footnote{Draft Guidelines on horizontal co-operation agreements [10] but such is also the definition in other policy documents, for instance the \textit{de minimis notice}.}

It appears that if the retailer is marketing his own label products which fall into the same product and geographical market as those for which he is contracting with the supplier, then he could be considered an actual competitor. Alternatively, if a retailer does not carry the PL version of the product(s) in question but could reasonably be expected to introduce a PL if profitable, he might be considered a potential competitor. Indeed this is how most PLs appeared - they followed the introduction of a successful brand or copied such a brand. The Commission itself seems to be of the view that PL-carrying retailers are competing with suppliers of branded goods. In the \textit{Kesko/Tuko} decision, it stated:
[PL development] enables retailers, who are inevitably privy to commercially sensitive details regarding the branded goods producers' product launches and promotional strategies, to act as competitors as well as key customers of the producers.\(^{164}\)

Yet, by reference to a different policy document, the matter is not as straightforward. The new Vertical Restraint Guidelines provide that “a distributor who provides specifications to a manufacturer to produce particular goods under the distributor’s brand name is not to be considered a manufacturer of such own-brand goods”.\(^{165}\) (emphasis added).

The above caveat, sneaked in the subsection in the Vertical Restraint Guidelines dealing with vertical agreements between competitors\(^{166}\), seems to imply that where the retailer owns the production facility for private labels, the retailer could be considered a competitor but where the retailer carries a PL that it contracts for separately, it is not to be considered a competitor to a supplier who only acts as a supplier. This discussion is particularly important because vertical agreements between competitors are excluded from the benefit of a block exemption and are to be assessed under the guidelines on horizontal co-operation agreements.\(^{167}\) The newest draft of these guidelines\(^{168}\) contains no rules for this situation.

It is interesting to note that the mirror situation to a retailer venturing upstream by developing a PL program, the case of a downstream-integrated supplier (i.e. dual distribution)\(^ {169}\) is covered by the block exemption regulation (and is excluded from the scope of the guidelines on horizontal co-operation agreements)\(^ {170}\). However, it remains uncertain whether the retailer would be considered a competitor.

### 1.3 Who owns the own brand?

There is some logic to not considering a retailer offering PLs as a competitor of his suppliers. If a retailer simply contracts with a manufacturer for the production of the own label, that does not make the own label different from ordering any other product. The only difference would be that it is marketed under the retailer’s brand, but apart from that it is just like any other item that the retailer purchases from suppliers.

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164 Kesko/Tuko [152]
165 European Commission “Guidelines on Vertical Restraints” (Guidelines on Vertical Restraints) [2010] OJ C 130/1 [27]
166 Ibid., [27-28]
167 Ibid. [27]
169 Article 2(4)a of the Block Exemption Regulation defines dual distribution agreements, as non-reciprocal agreements between competing undertakings where “the supplier is a manufacturer and a distributor of goods, while the buyer is a distributor and not a competing undertaking at the manufacturing level”. Article 2(4)b essentially repeats the statement for services.
170 European Commission “Guidelines on Vertical Restraints” (Guidelines on Vertical Restraints) [2010] OJ C 130/1 [28]
and sells to make a profit and only insofar as it makes a profit. However, there is more to the discussion than first meets the eye.

A retailer’s own label is not the same as any other brand.\(^{171}\) While he may not own the facility manufacturing the product, the retailer still owns “the brand” and it is the retailer who provides the “specifications”. PLs develop in the context of the retailer’s knowledge of confidential information about other brands. Even where the retailer entrusts the actual research and development for the own label product to the manufacturer, the fact remains that private label brands are being ordered by an informed retailer. The knowledge of brand firms’ plans enables the own-label supplier to produce, and the retailer to sell, with less uncertainty. It could also be argued that the retailer acts as a transmitter of information between horizontal competitors (the branded supplier and the PL supplier) with the exception that the information exchange, as already mentioned, is asymmetric – it goes from the brand to the own-label supplier, to the benefit mainly of the retailer.

Conversely, an independent supplier has to develop his products without the backing of a retailer and in the absence of privileged knowledge. Such a supplier would have to take the key decisions (and risks!) regarding the level of quality of the product, the price to be charged, the capacity for production - all on its own. The result may be more or less successful than leading brands, but the producer cannot know and thus strives to achieve the best result. Arguments about fairness set aside, uncertainty is a key ingredient to competition on prices, as well as to competition in innovation and competition on quality.

The issue could be approached differently – in a lot of cases, brands also are not active at the manufacturing level themselves. Brand producers often contract for the manufacturing of their products.\(^{172}\) Although they are called suppliers, the firms actually focus on product development, i.e. market research, developing new product concepts, marketing and brand image. Such suppliers are also merely providing specifications to a separate manufacturer, but the core of their business is brand development. In today’s world of sub-division of labor and outsourced production, should they not be considered to be competitors of the retailer?

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\(^{171}\) This point was also raised by the British Brands Group (BBG) in the 2006 grocery market investigation in the UK. The BBG advocated for a distinction between private labels sold by retailers and tertiary products sold by an independent convenience store because the latter would have to compete for shelf-space and consumer recognition on par with branded products and in the absence of the information that a retailer gets from its trading partners and uses in the development of its own labels. The Competition Commission, however, set the claim aside as irrelevant because it concluded that an own-label and a tertiary brand basically perform the same function from the consumer’s point of view. See UK Competition Commission, “Appendix 9.10: Own-label Goods” in Groceries Market Investigation (Final Report) (2008), footnote 4. Also, see discussion in Chapter 2 of this paper.

\(^{172}\) See for example the following interview with a manager of Anthony Alan Foods Ltd., owner of the Weight Watchers brand, in which he talks about outsourcing the production of the goods marketed under the brand. The interview appears on a UK government sponsored website providing guidance to companies and entrepreneurs: [http://www.businesslink.gov.uk/bdotg/action/detail?type=CASE%20STUDIES&itemid=1076888409](http://www.businesslink.gov.uk/bdotg/action/detail?type=CASE%20STUDIES&itemid=1076888409); accessed on 9 June 2010
Such a reading should not be inconsistent with the statement in the Vertical Restraint guidelines, because the Guidelines do not explicitly state that a retailer is not to be considered a competitor of the brand supplier. All they say is that the retailer is not to be considered the manufacturer of the products where he provides specifications. If the core of the business is brand development – both for the retailer’s PL development division and the supplier’s business - there just might be a possibility for their relationship to be classified as between actual or potential competitors. This would allow for exchanges of information to be examined as between competitors but would preclude the application of the rules on vertical restraints (including the exemption) to agreements between retailers with PL programs and branded suppliers.

1.4 Scope of Application of Art. 101 to Information exchange

The absence of guidance on how retailers with PLs might be assessed in the Draft horizontal co-operation guidelines seems almost intentional. These guidelines do mention PLs but they do so in the discussion of joint purchasing where an example is given of a buying alliance of retailers who carry PLs. There is certainly no mention of PLs in the chapter on exchange of information. A careful reading of the guidelines also does not show how exchange of information could possibly be discussed in the framework of horizontal co-operation agreements, as the information that the retailer receives is not subject to a specific co-operation agreement.

If not as a horizontal co-operation, information exchange could be examined under Art. 101 as a collusive practice, even where the information is not submitted voluntarily and even when collusion was not intended by one of the parties. With respect to exchange of information between competitors, the ECJ has held that it could be interpreted as collusion, because an undertaking who is a competitor cannot take advantage of this information in its business practice. In other cases, the Court mentioned the possibility that an exchange of information that might be used to establish a cartel could be examined as a concerted practice. With respect to cartels, they are defined as:

“Agreements and/or concerted practices between two or more competitors aimed at coordinating their competitive behavior on the market and/or influencing the relevant parameters of competition through practices such as the fixing of purchase or selling prices or other trading conditions, the allocation of production or sales quotas, the sharing of markets including bid-rigging, restrictions of imports or exports and/or anti-competitive actions against other competitors.”

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173 See example3 in the Draft Guidelines on horizontal co-operation agreements [2010][218]
176 European Commission Notice on Immunity from fines and reduction of fines in cartel cases [2006] C298/11 [1]
In the absence of more specific guidance with respect to what the nature of the relationship between a supplier and a retailer offering PLs may be, it would come to a surprise if retailers were to be punished for their long-standing practice of offering competing PLs.

The argument could also be made that since the exchange of information is essential, it represent an ancillary restraint. An ancillary restraint is defined as a restraint which is needed for the implementation of an agreement that does not have as its object or effect the restriction of competition. This would be the situation where suppliers and buyers need to communicate, and that is in the ordinary course of business, in order for the transaction to take place. The test applied to ancillary restraints requires proof that the restraint is subordinate to the main transaction, that it is inseparable and indispensable for the transaction to take place, that it is objectively necessary for the main transaction, and that it is proportionate. The exchange of information between suppliers and retailers in the context of negotiating purchases and promotions may meet these criteria especially where the only information shared is that which is strictly necessary for the completion of a purchase. However, the fulfillment of the last condition, of proportionality, may be problematic for a retailer. Discussing future product introductions or product promotions might be necessary for the retailer to fulfill its function as a retailer; but if following the discussion, a retailer’s buying manager picks up the phone and shares the information with the retailer’s PL development department, this is hardly necessary for the fulfillment of the retailer’s obligations with the supplier.

The retailer can preserve his or her role as a seller and keep his private labels. One way of doing so would be the erection of “Chinese walls” within the enterprise – i.e. the buyers of the retailer communicating with the brands should not talk to the private labels development program. This model has been used successfully in the context of telecoms where incumbent network-owners also operating downstream charge fees for use of the network both from their own downstream division and with a competing service supplier. In the network industries, the situation is not exactly the same because the price at which the service is supplied to a competing service provider is often set by national regulators. However, if a retailer follows such principles, genuine competition between brands and PLs would be restored to the benefit of consumers.

1.5 The implications for consumer welfare

Chapter two presented evidence from theoretical and empirical research pointing to the potential for retailers with PLs to collude with their suppliers to set prices that benefit both parties; as well as to determine prices and product characteristics on the basis of the information they have of suppliers’ plans.

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177 Horizontal Guidelines [2004] [28-29]
178 Horizontal Guidelines [2004] [29]
179 Managers appointed to negotiate the purchases with retailers
Such practices reduce consumer welfare not only by leading to supracompétitive prices but also by lowering the incentives to strive for better quality and more innovation. In the absence of an effective remedy or deterrence, these outcomes may be sustained. The rules under Art. 101 and the case law related to information sharing between competitors may be applied to these practices, but this depending on whether retailers will be considered competitors of their suppliers in the first place. Such an interpretation necessitates an approach strongly grounded in the reality of the interactions in the food supply chain, rather than a formalistic assessment of what constitutes a competitor.

2 PLs and the rules on vertical Restraints

2.1 The Customer/Competitor Dichotomy Again

Agreements between competing undertakings, even if they are of a vertical nature need to be assessed under the Horizontal co-operation guidelines.\textsuperscript{180} The stance of the Commission on this matter is difficult to discern, because the Vertical Restraint Guidelines contain specific references as to how PL behavior is to be assessed for example in the case of de-listing and cumulative foreclosure. They also introduce a market share threshold for buyers, as if to make sure that agreements between powerful retailers and suppliers which would have been exempt under the previous regulation due to low retailer market shares, would not escape scrutiny any more.

At the same time, the Commission’s language in merger cases\textsuperscript{181} and in its 2008 Communication on Food Prices in Europe (below) hints that retailers with PLs are to be considered competitors of brands. No less than in the context of a discussion on vertical restraints, the Commission states the following about PLs:

“Similarly [to single branding obligations and certain tying practices], the increased use of private label products by retailers may lead to foreclosure of existing and potential competing suppliers. This could reduce the number of product items on the shelves, thereby limiting consumer choice”\textsuperscript{182}(emphasis added).

In light of the new guidelines and the above discussion on customer-competitor, it is all the more puzzling whether and under which rules the consumer-welfare reducing practices related to PLs will be discussed.

\textsuperscript{180} Guidelines on Vertical Restraints [2010] OJ C 130/1 [27]. The wording is somewhat misleading, yet a reading of the Draft Horizontal co-operation guidelines [12] confirms that this is the case.


\textsuperscript{182} European Commission Communication on Food Prices, p. 10
2.2 De-listing, foreclosure, and lessening of consumer choice

The above quote may be confusing with respect to the interpretation of what constitutes a competitor, but it certainly recognizes the foreclosure effect of retailers’ delisting practices, i.e. the decision of a retailer to cease to stock a certain product, and the impact on consumer welfare as a result. This problem and the conflict of interest of retailers carrying PLs along with branded products, has been addressed explicitly in the new Vertical Restraint Guidelines:

“While in most cases the distributor may not have an interest in limiting its choice of products, when the distributor also sells competing products under its own brand (private labels), the distributor may also have incentives to exclude certain suppliers, in particular intermediate range products. The assessment of this upstream foreclosure effect is made by analogy to the assessment of single branding obligations [...] by addressing issues like the market coverage of these agreements, the market position of competing suppliers and the possible cumulative use of such agreements.”

It is interesting that although choosing to interrupt an agreement (which is essentially what delisting is) can hardly be thought of as an agreement, de-listing was effectively sneaked in the Guidelines on Vertical Restraints. It is also interesting that the Commission provides for an assessment of the cumulative foreclosure effects.

2.3 Cumulative Foreclosure

In the situation where one retailer chooses to de-list many products, cumulative foreclosure may be evoked and Art. 101 may apply. The Delimitis judgment recognized the possibility of finding cumulative foreclosure in the case of many similar agreements with suppliers, but set the condition that “the agreement in issue must make a significant contribution to the sealing-off effect brought about by the totality of those agreements in their economic and legal context”. This, on the other hand was found to depend on “the position of the contracting parties in the relevant market and on the duration of the agreement”.

With respect to what is a significant contribution to foreclosure, De minimis notice provides some guidance. The notice states that for cumulative foreclosure to be considered likely it is necessary that 30% or more of the relevant market “[be] covered by parallel (networks of) agreements having similar effects”.

However, in light of the requirement for a consideration of buyer market shares on the purchasing market (see below), it is unclear whether the purchasing or the distribution market would be considered. It has been noted that retailers rarely have market shares above 30% on the retail market. The uncertainty as to the market shares on which market are to be considered, it is also unclear whether multiple de-listing decisions taken by one retailer would be examined in the framework of cumulative foreclosure under Art. 101.

Cumulative foreclosure may also arise where a number of retailers, independently, choose to de-list a brand or brands and replace it with an own label. Such independent decisions, though they may result in cumulative foreclosure cannot be caught by Art. 101 but they may be caught by Art. 102 if the retailer is found to be dominant or if several retailers are found to be collectively dominant. This issue will be examined in the next chapter. It is still important that part of the assessment of an individual retailer’s decision to de-list in order to replace with an own brand will include a consideration of cumulative foreclosure.

2.4 A Note on Resale Price Maintenance (RPM)

It has been suggested that strict rules regarding resale price maintenance may no longer be in the best interest of the competitive process. Specifically with respect to buyer power and the threat of PLs, some scholars have noted that resale price maintenance may be the only weapon that a brand may use to protect itself from the perverse incentives of a retailer-competitor who fixes the prices of the supplier’s goods. Recently, the rules with respect to RPM were relaxed in the US as a result of the Supreme Court judgment in *Leegin Creative Leather Products, Inc. v. PSKS, Inc. (2007)*, in which the Court held that minimum resale price maintenance would no longer be regarded as a *per se* violation of competition rules, but will be assessed on a case-by-case basis (i.e. will be subject to a rule of reason approach).

RPM remains a hardcore restriction under the new guidelines, with the exception of maximum resale price or a recommended resale price. The latter are covered by the Block Exemption as any other agreement, when both parties to the agreement fall below the market threshold of 30%; respectively, they are assessed as any other vertical restraint, if this condition is not met. The caveat is that in the assessment of such an agreement, the market position of the supplier remains the more important factor for fear that this maximum or recommended resale price might become a focal point for all resellers.

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188 See the market shares (for the distribution market) for the British retailers and for Tables 2 and 3 showing the market shares of the five largest retailers in given European countries in the Annex.
190 ibid., Ibid.
193 Guidelines on Vertical Restraints [2010] OJ C 130/1 [228]
It is interesting to note that with respect to RPM, the Guidelines seem to recognize the conflict of interest between buyers and suppliers which might motivate the distributor to tweak the price difference between the private label and the brand to his own advantage.\textsuperscript{194} The Guidelines note that the maximum resale price “may also help to ensure that the brand in question competes more forcefully with other brands, including own label products, distributed by the same distributor”.\textsuperscript{195}

2.5 The Buyer Market Share Threshold Under the New Vertical Block Exemption Regulation

The major novelty of the Vertical Block Exemption Regulation (VBER)\textsuperscript{196} and the Vertical Guidelines that came into force on 1 June 2010 is the introduction of a market share thresholds for buyers. As per Article 3(1) of the VBER for a vertical agreement to be exempt, both buyer and supplier need to have less than 30% market share on the relevant market, the relevant market being respectively for the supplier, the market on which he sells, and for the buyer – the market on which the buyer purchases the goods or services. Thus, for a buyer-supplier agreement to be automatically exempt under Art. 101, the market share of the buyer on the purchasing market, and the market share of the supplier, should individually not exceed 30%. One implication of these stricter rules is that many agreements between buyers and suppliers that would have fallen short of an examination under the former regulation because the retailer’s market share was less than 30%, would now be the subject of an individual assessment.

This assessment will be made with regard to the actual or likely effects on any actual or potential competition, and whether these effects are or are likely to be appreciable.\textsuperscript{197} Appreciable effects are considered likely when at least one of the undertakings has market power and when the agreement creates, maintains, strengthens or allows the exploitation of such market power.\textsuperscript{198} Under these rules, it would be possible for delisting decisions by a powerful retailer against a smaller brand to be caught by Art. 101(1) and then examined under Art.101 (3). The test under Art.101 (3), which requires pass-on of efficiencies to consumers, would unlikely allow the exemption of retailer decisions to delist a competitive, differentiated product.

\textsuperscript{194} Given the higher margins that the PL represents for the retailer, the retailer’s advantage in maximizing the more profitable (to him) good may work against the brand image or the branded product’s interest.
\textsuperscript{195} Guidelines on Vertical Restraints [2010] OJ C 130/1 [229]
\textsuperscript{196} Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices
\textsuperscript{197} Guidelines on Vertical Restraints [2010] OJ C 130/1 [97]
\textsuperscript{198} Guidelines on Vertical Restraints [2010] OJ C 130/1 [97]
2.6 Calculation of Market Shares on the Purchasing Market

While some might find the inclusion of a buyer market threshold exciting, for others this requirement might be a huge headache. A purchasing or a procurement market, unlike a selling market, is certainly not a familiar concept. Presently the Vertical Restraint Guidelines is the only document containing some advice on how the purchasing market shares are to be calculated. The Notice on the definition of the relevant market\(^\text{199}\) and the \textit{De minimis} notice are largely silent on the issue of buyer shares. The Vertical Guidelines document itself does not offer very detailed guidance on the calculation of the market shares on the procurement market. It notes that “the product market depends in the first place on substitutability from the buyer’s perspective”\(^\text{200}\), that the wholesale market is to be considered in general wider than the distribution market\(^\text{201}\) and that the calculation of the market shares should be based on value figures, rough estimation of value figures if the latter are not available or on volume figures.\(^\text{202}\)

With this type of guidance, it seems very difficult to assess with certainty what the market share of the buyer would be. It might be difficult for a supplier seeking to contest a delisting decision, to gauge with precision the market share of his trading partner, especially since substitutability is to be assessed from the buyer’s perspective (see above). But it might be just as complicated for the retailer to calculate its market share because supermarkets purchase thousands of products and their purchases are placed frequently, for some products every week, for others – every month. The Guidelines do provide that “where suppliers generally sell a portfolio of products, the entire portfolio may determine the product market when the portfolios and not the individual products are regarded as substitutes by the buyers”, yet that does not solve the problem for the supermarket to calculate its market share separately for eggs, apples, pasta sauce and baby food.

One might think of looking for guidance in calculating market shares on the purchasing market in case-law, though it is unlikely that much case law dealing with this problem is available. For instance, although the Commission considered the procurement market in the \textit{Kesko/Tuko} decision in 1996, it did not specifically calculate Kesko or Tuko’s shares on that market.\(^\text{203}\) Such an analysis, however, was carried out in the \textit{Rewe/Meinl} merger decision three years later. In \textit{Rewe/Meinl}, the Commission noted that while usually market shares would be determined by reference to the consumer and her preferences, the procurement market shares are to be determined by reference to the suppliers and their ability to “substitute” between

\(^{199}\) European Commission Notice on the definition of relevant market for the purposes of Community competition law [1997] OJ C 372/5
\(^{200}\) Guidelines on Vertical Restraints [2010] [89]
\(^{201}\) Guidelines on Vertical Restraints [2010] [89]
\(^{202}\) Guidelines on Vertical Restraints [2010] [93]
\(^{203}\) See the \textit{Kesko/Tuko} decision especially paras[146-153]
sales channels as well as to change their output.\textsuperscript{204} Also, because of the differences between the different products and suppliers, the retailers’ power would have to be estimated separately on the different procurement markets for each distinct category of goods sold.\textsuperscript{205} This decision shows how difficult it may be for an individual retailer to calculate its buyer market share as required by the new Block Exemption Regulation. In \textit{Rewe/Meinl}, the Commission calculated Rewe/Billa and Meinl’s buyer shares in no less than 16 product categories!

\textbf{2.7 Implications of the New Vertical Block Exemption}

The new Vertical Block Exemption and the accompanying guidelines reflect a concern on the part of the Commission with the exercise of buyer power and with the phenomenon of PLs. By referring specifically to private labels, although not in great detail, in several points in the guidelines, the Commission is giving the private label practices a name, and thus some status in competition law. Also, by providing for assessment of delisting decisions, the vertical restraints rules may provide opportunities to discipline retailers who consciously limit the choice for consumers by delisting innovative or differentiated branded products. Finally, by allowing producers to impose a maximum resale price, the Block Exemption Regulation would restrict the opportunity for a retailer to set an artificially higher price for a branded good, in order to make the PL seem relatively cheaper.

However, it is unclear whether the Vertical Block Exemption Regulation is even applicable to retailers carrying PLs, because of the absence of a clear statement as to whether such a retailer is to be considered a competitor to his suppliers, or not. Another major pitfall is that the Vertical Restrain Guidelines fail to provide specific instructions for the calculation of a buyer’s market shares on the purchasing market. These omissions on the part of the Commission will unlikely be helpful to suppliers seeking redress for being delisted for no good reason or for NCAs seeking to protect consumers’ choice. On the contrary, they might contribute to an understanding among suppliers and NCAs, that competition rules are largely inapplicable to practices by large retailers carrying PLs.

\textsuperscript{204} \textit{Rewe/Meinl} (Case IV/M.1221) [76]

\textsuperscript{205} \textit{Rewe/Meinl} (Case IV/M.1221) [75-77]; Although the definition of the categories is somewhat intuitive, it may still not be immediately obvious to a retailer that beer is a market distinct from wine and spirits and soft drinks.
Chapter 5: Private Label-Related Concerns in the Framework of Art. 102 TFEU

“But I would be interested in your views on the other case, buyer power. Imagine a monopsonistic market, and imagine that there are high barriers to entry which exclude alternative purchasers who could drive the price up if they had access to the market. In this situation our monopsonist exploits suppliers and forces their prices down to a level which you would consider abusive. Is that a case for Article 82? From a legal point of view, I would say yes. I cannot find a reason to treat a monopsonist better than a monopolist. But a prohibition of this abuse of a monopsonistic position cannot be explained by reference to consumer welfare. Why? Because here the harm is done to producers, not to consumers.”

Daniel Zimmer, a panel on price regulation and Art.82 (currently 102 TFEU) 2007

1 Types of abuse under Art.102 TFEU

Zimmer may be right in that the harm inflicted by a monopsonist may be more palpable for a supplier. Yet, albeit indirectly, consumers are also affected by actions that harm suppliers, especially where the harm accumulates over time and impacts an industry (the food production industry, for instance) as a whole. If the cumulative foreclosure effects of independent decisions to delist taken by multiple retailers is not caught by Art. 101, these decisions may be assessed as the unilateral action of one or more dominant undertakings under Art. 102 TFEU. This article might also capture the pricing practices of retailers, taking place in the context of PLs, where these practices result in excessively high prices for PLs and NBs.

Two categories of abuses are distinguished under Art. 102: exclusionary abuses and exploitative abuses. Exploitative abuses are those which are “directly exploitative of consumers, for example charging excessively high prices” 207. Exclusionary abuses focus on anti-competitive foreclosure, the ability of a dominant undertaking to exclude its competitors from the market which would in turn subsequently enable it to “increase prices” 208 to the detriment of consumers. 209

The conduct of private label carrying retailers has both exploitative and exclusionary characteristics. For example, when a retailer benefits from the insufficient downstream competition and sets the prices for

207 European Commission “Guidance on the Commission’s enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings” (Guidance paper on Article 82) [2009] OJ C 45/7, para [7]
208 In the context of the Guidance paper on Article 82 “increase in prices” is used as shorthand for higher prices as well as degradation of quality or limitation of consumer choice. Guidance paper on Article 82) [2009] OJ C 45/7, para [11]
209 ibid. [19]
national brands and private labels at supracompetitive levels, his conduct could be considered exploitative of final consumers. When he forces a supplier to sell at a huge discount, thus significantly depressing the supplier’s margins, his conduct is exploitative of his trading partner, in which case the consumers may suffer harm indirectly, for instance as a lessening of choice if the supplier exits the market. Exclusionary conduct, on the other hand, might occur when a buyer selling PLs decides to de-list a competing brand. This is essentially the same issue discussed in the previous chapter under Vertical Restraints. Article 102 may also be applied to this type of conduct, when the retailer holds a dominant position or when several large retailers together hold a dominant position.

The distinction between exploitative abuses and exclusionary abuses is important. The former seem to have been pushed to the bottom of the enforcement priorities agenda of the Commission following the publication of the Discussion paper on Art.82 in 2005 and the adoption of the Guidance paper on the enforcement priorities in applying Art. 82210 (currently Art. 102) in 2009.

1.1 Exploitative Abuses

Exploitative practices may be defined as those which directly harm consumers, one example being charging excessively high prices for the PL or the NB.211 Exploitation cases are not with high priority on the Commission’s agenda these days as is evident from the Guidance paper on the enforcement priorities in applying Article 102. In this paper, which is the first document providing guidelines on the Commission’s approach to Art. 102 cases212, the Commission recognizes the gravity of exploitative abuses, but it states that it will focus on exclusionary, rather than exploitative conduct.213 While this does not necessarily mean that the Commission will reject every complaint outside the scope of the guidelines, it makes it clear that it will privilege the examination of conduct of the exclusionary type.214 Similarly, in its 2005 Discussion paper on the application of Art. 82 (currently Art. 102), the Commission limited its discussion to exclusionary conduct.215 The Commission did note in a press release that “other forms of abuse, such as discriminatory and

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210 Ibid.
211 Ibid.
212 See the Commission website section on Art.82 review <http://ec.europa.eu/competition/antitrust/art82/index.html> accessed on 7 June 2010
213 Guidance paper on Article 82 [2009] OJ C 45/7 [6-7]
214 Ibid., [3]
exploitative conduct, will be the subject of further work by the Commission in 2006\textsuperscript{216}, no further guidance has been provided in the past five years.

1.1.1 High Selling Prices

One reason for not privileging exploitative abuses is that abusive exploitation is difficult to prove. From an economist’s perspective, determining what the prices would have been under “normal competitive conditions” is a difficult task. For a lawyer, it is an uncertain bet in court because it is still not clear what the European Courts consider as excessive pricing.\textsuperscript{217} From a legitimacy perspective, there are also doubts as to how fair prosecuting these abuses is and to what extent it amounts to price regulation\textsuperscript{218}; along the same lines, it seems unfair to punish a successful firm, whose behavior complies with competition laws, for reaping the benefits of its success and efficiency.\textsuperscript{219} Controlling that prices are close to marginal costs is very difficult to enforce in practice and there are very few cases on this specific abuse.\textsuperscript{220}

True, in its prosecution of excessive pricing cases, the Commission has paid attention not only to prices but also to non-cost factors, for instance if the dominant undertaking had control over a specific right or facility that were not easily substitutable, as in the cases, for example in the cases General Motors Continental\textsuperscript{221} and Scandlines Sverige AB v Port of Helsingborg\textsuperscript{222}. In the latter case, for instance, the Commission took account of the good location of the port.\textsuperscript{223} Along the same lines, it could find that the insufficient competition among retailers on NB prices, and the exclusivity of the PL offerings, place the retailer in a position to independently determine prices. However, even in these decisions, the Commission was not able to meet the standard of proof required by the Court of Justice.

1.1.2 Low Buying Prices

Sometimes, as part of their competition with other retailers, supermarkets were found to engage in below-cost selling to the detriment of small retailers, but also to their suppliers. Below-cost selling in the context of

\textsuperscript{216} Europa Press Release, “Competition: Commission publishes discussion paper on abuse of dominance” IP/05/1626 of 19 December 2005
\textsuperscript{217} Ibid., [4.365] on p.398
\textsuperscript{218} Ibid., pp.397-398
\textsuperscript{220} Case 26/75 General Motors Continental [1975] ECR 1367:[1976] 1 CMLR 95
\textsuperscript{221} Case Comp/36.568 Scandlines Sverige AB v Port of Helsingborg
\textsuperscript{222} Jonathan Faull and Ali Nikpay (eds), \textit{The EC Law of Competition} (2\textsuperscript{nd} edn, OUP, New York, 2007) [4.376] on p.400
\textsuperscript{223} Jonathan Faull and Ali Nikpay (eds), \textit{The EC Law of Competition} (2\textsuperscript{nd} edn, OUP, New York, 2007) [4.373] on p.400
supermarket price wars, as well as promotions, has been found to put a lot of strain on suppliers because these have had to reduce their price in order to offset the losses of retailers and at the same time they would have to increase their output because a lot of consumers switched to the cheap products. The implications of this conduct for consumer welfare are evident when they force suppliers to exit the market. For example, as a result of the ever decreasing buying prices in the course of the “baked bean wars” between supermarkets in the mid-1990s in the UK, multinational food producer Nestle exited the market for canned baked beans. Another example came up in the UK Competition Commission, in which it was found that “the suppliers of retailers’ own-label bread, lettuce, apples, eggs, lamb and chicken were found, by and large, to be selling these products at a net loss.” Exploitative practices which put in question the viability of the producer and its ability to maintain the high quality of the product could thus also be harmful to consumers.

Article 102 refers to “imposing unfair purchase or selling prices or other unfair trading conditions” which includes the “extraction of unfairly low prices by dominant buyers”. However, while charging too much has been difficult to prove, paying too little has been equally challenging. A case involving dominant buyers paying too little is CICCE, where film distributors complained about the low fees they received for the airing of their films by broadcasters. The case was rejected both by the Commission and the Court on the grounds that there was insufficient evidence that the “fees bore no reasonable relation to the economic value of the films”, hence again the question of what is a “just” price was raised.

In conclusion, despite the Commission’s concern specifically with the ability of large retail chains to obtain very low prices from their suppliers, no concrete proceedings have been undertaken so far. Consistent with the 2009 Guidance paper on Art. 82, pricing below-marginal cost becomes an enforcement priority only if used to successfully foreclose actual or potential horizontal competitors, i.e. when it serves exclusionary rather than exploitative purposes. Thus, it is unlikely that below-cost selling as such will be condemned.

1.2 Exclusionary Abuses

1.2.1 De-listing

It has been suggested that “the same rules which allow us to condemn a dominant seller who terminates a contract thus refusing to supply on some “arbitrary and not objectively justified grounds, should allow us to

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224 UK Competition Commission, UK Grocery Report 2000 Chapter 11, see paras.11.88-11.93 on pp.245-246
225 Ibid, para. 11.99 on p. 247
226 Ibid., para. 11.100 on p. 247
227 UK Competition Commission, UK Grocery Report 2000 Chapter 11, para. 11.161 (e) on p. 259
229 Case 298/83 CICCE [1985] ECR 1105
consider the conduct of a supermarket which on the same arbitrary and unjustifiable grounds, refuses to
stock a brand to clear off space for its own brand. Delisting the products of a competing brand to clear
up shelf space for own label products could be examined, ironically, in the framework of “Refusal to Supply”.
The analogy between a network and the totality of shelves in a certain distribution market has been
advanced elsewhere. This analogy captures the reality that suppliers face: for a given product on a given
market there is a limited number of shelves where that product may reach the customers that it is
intended for. Replicating this network or substituting with another distribution format is not easy. One
very obvious reason is that there are only that many convenient pieces of land within an urban zone, where a
supermarket can be built.

Suppliers of national brands (or of brands hoping to become national), on the other hand, need to
reach as many consumers as possible. They invest a lot in advertising on a national scale and their strength is
derived from the number of consumers who are loyal to their brand. As the Commission noted in
P&G/Gillette, even suppliers with must-stock items may be delisted by the retailer. If the brand is not on
the shelf, the consumer might choose another brand, and there is always the risk that a company would lose
the loyalty of an actual or potential consumer. In conclusion, competition for these shelves as well as for
particular shelves (eye-level shelves, freezers, end-of-aisle shelves), is intense and all the more so in the
context of PLs.

Applying the concept of a network to grocery store shelves would allow us to see why a retailer with
as little as 10% market share in the downstream (selling) market, can exert significant pressure on a supplier
with 50% or more market share. This point is also supported by the finding of the UK CC that a retailer with

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232 Andres Font Galarza, “Private Labels and Article 82 EC” in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009), p. 135
233 See for instance Alastair Gorrie, “Retail Competition: The Use of Ex-ante and Ex-post Remedies” in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009), p. 298
234 For example John Ratliff notes that “there is a physical constraint”, in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009), p. 295-596
236 ibid., [116-118]
237 Procter & Gamble/Gillette (Case COMP/M.3732) [127]
238 John Ratliff, “Retail Consolidation: The Implications of Mergers and Buying Alliances” in in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009), p. 295-596
239 In Rewe/Meinl, the Commission conducted surveys with suppliers and determined that on average where 22% or more of the turnover of a supplier was achieved within a single trade channel, the replacement of this channel would involve substantial financial losses for the supplier [101]. Another interview in the course of the merger investigation showed that even retailers accounting for as little as 5-10% of the supplier’s turnover, are difficult to replace [97] and this was reflected in the Commission’s conclusions [96-116]
market share as low as 8% may be able to engage in practices with serious anticompetitive effects.\(^240\) (See Table 3 “Who owns the shelves in the UK?” in Annex.)\(^241\)

The Commission considers refusal to supply based on whether the input is “objectively necessary” for the product to be able to compete effectively on a downstream market; whether could lead to the elimination of effective competition downstream, and whether the refusal could result in consumer harm.\(^242\) The Commission identifies as consumer harm instances where innovative goods and services are foreclosed from the market, such goods defined as those which do not “essentially duplicate the goods and services already offered by the dominant undertaking on the downstream market”.\(^243\) It is very likely that a brand producer with a differentiated product when delisted and replaced with PL-imitator would satisfy these conditions. There is no indication, however, whether the network industry analogy would be considered legitimate by the courts.

### 2 The Rules on Dominance

#### 2.1 Dominance Thresholds

The High Level Group established by the Commission recognized in its report of 2009 that the European Commission and some NCAs have investigated cases related to the concentration in the agro-food industry and especially the relationship between suppliers and retailers.\(^244\) However, while the authorities recognized the tensions, they noted that abuse of dominance has been difficult to prove in individual cases and for the moment they will just continue to monitor the industry.\(^245\) Yet so far there has been no case under Art. 102 TFEU related specifically to PLs or to abuse of dominant position against supermarkets.\(^246\)

The problem in applying Art. 102 to the potential abuses by retailers are the market share thresholds, established in EU competition law. Dominance is defined in the Commission’s guidance by reference to ECJ decisions as “a position of economic strength enjoyed by an undertaking, which enables it to

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\(^240\) UK Competition Commission, “Chapter 1: Summary and Conclusions” in *Supermarkets: A report on the supply of groceries from multiple stores in the United Kingdom* (2000) [1.10-1.12]

\(^241\) The table was created on the basis of data from Europanel which reports the following market shares for the UK: Tesco – 30.4 % (represented as 30.5), Asda – 17.5%, Sainsbury’s – 16.1% (represented as 16), Morrisons – 11.8 (represented as 12), Aldi, Lidl, Netto (combined) – 5.9% (represented as 6), Miscellaneous other stores 18.3% (represented as 18)

\(^242\) Guidance paper on Article 82 [2009] OJ C 45/7, [81]

\(^243\) Guidance paper on Article 82 [2009] OJ C 45/7 [87]


\(^245\) ibid., pp.47-48

\(^246\) This is also confirmed in Ariel Ezrachi, “Unchallenged Market Power? The Tale of Supermarkets, Private Labels and Competition Law” [2010] *World Competition* 33(2), p.12 and also in Alastair Gorrie, “Retail Competition: The Use of Ex-ante and Ex-post Remedies” in Ariel Ezrachi and Ulf Bernitz (eds), *Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition* (OUP, Oxford 2009), p. 318 where the author states: “so far as the author is aware, there have been no Article 82 EC cases brought against supermarkets”
prevent effective competition being maintained on a relevant market, by affording it the power to behave to
an appreciable extent independently of its competitors, its customers and ultimately of consumers (3).” In
Akzo, a dominance of 50% market share was established. However, in United Brands the court found
that a 40-45% market share could also result in dominance especially given that the company United Brands
was very independent of its suppliers due to its integration and had a significant ability to control its
output.

As illustrated by Table 3 in the Annex, it would be difficult for British retailers to meet the market share thresholds. It also does not seem likely that many retailers in Europe would hold a market share of 40% or more on the downstream market. In light of this data, it might seem superfluous to examine the possibilities of applying Art. 102 to the behavior of supermarkets. This is nonetheless not a completely futile exercise. The Commission states in the guidelines that finding dominance below 40% market share in the relevant market is not likely, but it leaves open the possibility of “paying attention” with Art. 102 to “specific cases below that threshold where competitors are not in a position to constrain effectively the conduct of a dominant undertaking.” The Guidance paper also affirms the notion that assessing dominance is a complex formula which involves the evaluation of both quantitative (i.e. market shares and their stability over time) and qualitative factors such as the constraints imposed by suppliers, buyers, and actual and potential competitors.

2.2 Collective Dominance

Technically, it seems possible for exclusionary conduct on the part of a retailer-oligopolist to be attacked under Art. 102 in the case of collective dominance. For instance it might be possible for the concept of collective dominance to be applied to account for the cumulative foreclosure effect, resulting from the unilateral actions of rival retailers.

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248 Joanna Goyder and Albertina Albors-Llorens, Goyder’s Competition Law (5th edn, OUP, New York, 2009), pp.298 and C-62/86
250 Joanna Goyder and Albertina Albors-Llorens, Goyder’s Competition Law (5th edn, OUP, New York, 2009) pp.296-297,
in Britain in 2009, the four largest retailers had the following market shares: 11.8%, 16.1%, 17.5%, 30.4%, with only Tesco
being above the 30% threshold.
251 See Annex I, table 2, which shows that in most countries the situation is one of oligopoly rather than a duopoly or a single
dominant firm; see also Alastair Gorrie, “Competition Between Branded and Private Label Goods. Do Competition Concerns
Arise When A Customer is Also a Competitor?” [2006] European Competition Law Review 27 (5) on p. 225: Gorrie notes that in
terms of market shares, Kesko is the exception
252 Guidance paper on Article 82 [2009] OJ C 45/7 [14]
253 Guidance paper on Article 82 [2009] OJ C 45/7 [12-15] and in more detail [16-17-18]; See also Joanna Goyder and Albertina
Albors-Llorens, Goyder's Competition Law (5th edn, OUP, New York, 2009), pp.311-312
The possibility of applying the concept of collective dominance was first recognized by the ECJ in the *Flat Glass* case[^255] where the CFI held that collective dominance could occur where “two or more independent economic entities [...] united by such economic links that, by virtue of that fact, together they hold a dominant position vis-à-vis the other operators in the same market”[^256]. Subsequently, the requirement for the presence of “economic links” has been modified and it has become possible for the concept to be applied to oligopolies where no contractual or structural links connect the largest market players but where there are incentives for parallel behavior and likelihood for tacit collusion.[^257]

This approach has been used in the assessment of merger cases, which used to require an assessment of dominance. A look at the merger case law reveals that although the concept of collective dominance may be applied in the case of oligopolies where market participants have strong incentives to adopt parallel behavior, there are limitations to the concept. In the *Airtours/First Choice*[^258] merger proposal, the Commission argued that after the merger there would be a triopoly on the market and the firms would have strong incentives to decrease output.[^259] The Court of First Instance allowed the possibility for applying the concept of collective dominance to such a situation, but quashed the Commission’s decision on the ground of insufficient evidence that collusion would have been likely enough.

Following the disappointing experience with *Airtours/First choice*, there have hardly been any cases (antitrust or merger) involving collective dominance where no contractual or structural links are present.[^260] The problem, of course, is that delisting decisions resulting in cumulative foreclosure are taken independently by rival retailers in the absence of contractual or structural links between these retailers. Furthermore, the 2009 Guidance paper, while recognizing the possibility that Art. 102 be applied to abuse of dominant position where this position is held by more than one undertakings, excludes the of collective dominance abuses from its scope, and thus, implicitly from the Commission’s enforcement priorities in applying Art. 102.

### 2.3 Buyer Dominance

In the report “Buyer Power and Its Impact on Competition In the Food Retail Distribution Sector of the European Union”, prepared at the request of DG Competition, economist Paul Dobson states that “academic


[^260]: ibid., [4.124] on p.343
economists have devoted far less attention to retailing than to manufacturing. "\(^{261}\) Dobson also suggests that “an overall assessment of social welfare must be based on an assessment of producer, buyer and (final) seller concentration”\(^{262}\).

Dobson’s views are echoed by some competition law scholars and practitioners. Andres Galarza, for instance, notes that it is important to consider the application of Art. 102 in the context of retailers with market power that offer private labels, especially in light of a consumer welfare approach. \(^{263}\) Galarza, just as Zimmer quoted in the passage in the beginning of this chapter, sees no reason why the legal framework developed around the concept of abuse of dominance should not be applied to the “buying side”\(^{264}\). Alastair Gorrie also urges the Commission to “extend its examination of abuse of dominance to situations where abuse arises below the level of dominance, particularly in relation to retailer buyer power and the combination of their gatekeeper and competitor roles”\(^{265}\).

According to Faull and Nikpay, the “commission has [also] acknowledged the possibility of applying Article 82 to abuses of a buyer’s dominant position but there is little case law actually applying this concept”\(^{266}\). Indeed, nothing in the wording of Art. 102 would preclude it from applying to dominant buyers - dominant position encompasses the ability to behave independently of one’s suppliers as well as one’s buyers, competitors, and final consumers. However, a quick look through some major recent textbooks on EU Competition law reveals that there is still not much attention paid to buyer power. The discussions on buyer power are accorded anywhere from 0 to 1 page in books of 1000+ pages. Notwithstanding the Commission’s investigations in the so-called “demand cartelization”\(^{267}\), there has hardly been a case involving buyer power under Art. 102.

In terms of the case law, Faull and Nikpay point to the *Virgin/British Airways*\(^{268}\) case in which it was confirmed that abuse of dominance encompasses both dominance toward suppliers and toward customers. \(^{269}\) Faull and Nikpay consider that most cases of abuse of buyer dominance would arise where the


\(^{262}\) Ibid., p. 156

\(^{263}\) Andres Font Galarza, “Private Labels and Article 82 EC” in Ariel Ezrachi and Ulf Bernitz (eds), *Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition* (OUP, Oxford 2009), p.129

\(^{264}\) Ibid., 133

\(^{265}\) Alastair Gorrie, “Competition Between Branded and Private Label Goods. Do Competition Concerns Arise When A Customer is Also a Competitor?” (2006) 27 (5) ECLR, p 226


\(^{268}\) Case T-219/99 British Airways v Commission [2003]ECR II-5917; also the appeal Case c-95/04 British Airways v Commission

undertaking is a monopolist in another market, as is provided for instance in the Guidelines for the application of competition rules to the telecommunications sector. This was the case in one of the first cases involving abuse of buyer power - the 1989 case Filtrona/Tabacalera. Filtrona Espanola, a Spanish filter producer, complained that Tabacalera, the tobacco monopolist in Spain, had abused its dominant position as a purchaser of cigarette filters when it decided not to purchase from Filtrona any more. Tabacalera had decided to enter the upstream market and produce all the filters it needed itself. In this case, the European Commission rejected the complaint on the grounds that Filtrona was not to be considered dependent as it could export its filters or switch its production, and also because “a company’s production of its own requirements is not in itself an abnormal act of competition.” The Commission also considered the efficiencies that Tabacalera would achieve through its vertical integration, including economies of scale and a reduction of production costs. In these cases however, the dominant position of the buyer on the downstream market was not in question, although it is still a problem, even for large retailers. Yet, there might be reason to think that applying the concept of buyer dominance to cases in the future is likely. In light of the Commission’s introduction of a threshold for buyer market shares in the new Vertical Block Exemption Regulation, the Commission might consider taking into account the market shares of the buyer on the purchasing market(s).

But not unimportant is the fact that the Guidance paper on Art. 102 includes “countervailing buyer power” as one of the factors to be taken into account in finding dominance. This reduces the possibility of applying Art. 102 to cases where a “dominant supplier” might be coerced into anticompetitive behavior by a non-dominant retailer who, however, is a powerful buyer. A case that nicely illustrates this point came before the District Court of Den Bosch in 2004. It concerned a decision by deemed “dominant” supplier Peijnenburg to cease to supply Dutch grocery retailer Albert Heijn with a popular breakfast cake. Albert Heijn brought Peijnenburg to court for breach of contract without sufficient notice and also on the grounds that Peijnenburg had attempted to coerce it to breach competition rules by trying to impose a minimum resale price.

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270 Guidelines for the application of competition rules to the telecommunications sector [1991] OJ C233, paras 116-120
272 Filtrona/Tabacalera, Commission decision adopted on 26 April 1989 reported in European Commission. “XIXth Annual Report on Competition Policy” 1989, para [61] on p. 77; available through the DG Comp website
273 Ibid.
274 Ibid.
275 Ibid.
276 Ibid.
277 Ibid.
278 For instance countervailing buyer power appears in the Guidance paper on Article 82 [2009] OJ C 45/7 [18] and in the Merger Guidelines [2004] OJ C 31/03 [64-67]
279 Case N. 121916 KG ZA 05-39 [2004] District Court of Den Bosch, the Netherlands
cost, and trying to recuperate the losses by demanding larger and larger discounts to the point where the viability of the brand was at stake. The District Court of Den Bosch exonerated Peijnenburg’s refusal to supply on the grounds of fairness in Dutch commercial law, and it took account of the fact that the commercial viability of the brand was in danger. Subsequently, Albert Heijn decided to introduce its own label version of the product.280

This case nicely illustrates a point raised by John Ratliff that competition rules failing to take account of the real strength of buyers, may be working against efficient firms. He points out that the position of buyers may place suppliers meeting the dominance criteria (for instance those carrying must stock brands) in a tricky situation.281 John Ratliff refers to this as a “compliance headache” for the companies as “dominant companies are generally advised not to do precisely what the retailer may seek: non-cost justified rebates on total turnover, or at least across more than one product family.”282 Ratliff notes that a dominant supplier does not think of himself as “dominant” given the fact that the buyer controls a portion of the precious shelf network.283

3 A Note on Economic Dependency Laws

Instead of figuring out how to apply the national equivalents of Art. 102 to instances of abuse occurring below the dominance market share thresholds, some Member States have responded by amending their national competition laws to guard against “economic dependency” whether on the part of the buyer or on the part of the supplier. Such laws have been known to exist in several European countries: France, Germany, Spain, Portugal and Greece.284 The report on buyer power by Dobson Consulting notes that in Germany and Portugal the provisions of these laws had been strengthened recently, in Germany by adding a presumption of dependence and prohibiting loss-leading; in Portugal by prohibiting per se certain categories of “abusive bargaining practices”.285 Other countries have also followed suit. Italian competition laws were modified to provide that “any agreement to achieve abuse of economic dependence is null and void”286. Last year Latvia, also in response to the growing retailer power, changed its legislation so that abuse of dominance

280 Ibid, p. 108
281 John Ratliff, “Retail Consolidation: The Implications of Mergers and Buying Alliances” in in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009), pp. 289-290
282 Ibid., p. 290
283 John Ratliff, “Retail Consolidation: The Implications of Mergers and Buying Alliances” in in Ariel Ezrachi and Ulf Bernitz (eds), Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition (OUP, Oxford 2009), p. 290
284 Dobson Report, pp. 34-35. With respect to France and Germany, the report is referring, respectively, to Article 8(2) of the 1986 Ordonnance and to Section 22 and 26(3) of the German Competition Act in footnotes, 26 and 27 on p.34
285 See footnote 29 on p.35 of the Dobson Report
286 Section 11 of Law No. 57 of March 5th, 2001 as seen on the Italian Competition Authority’s website http://www.agcm.it/eng/index.htm
could capture abuse of dependence. It is unclear what the effectiveness of these laws has been in protecting consumer welfare. Yet, they do offer an alternative to competition rules on dominance.

4 Consumer Welfare, Private Labels and Art. 102 TFEU

This chapter outlined the difficulties of applying Art. 102 TFEU to welfare-reducing behavior of strong buyers. Given the difficult standard of proof, and the enforcement priorities of the Commission as defined in the Guidance paper, it is unlikely that the pricing behavior of retailers toward their final consumers or toward their suppliers will be examined. It might be possible for unilateral delisting practices to be captured by Art. 102 if the concept of a network is applied to shelf space. However, this is unlikely, given the relatively low market shares held by individual retailers. On the other hand, it also seems unlikely that the cumulative foreclosure effect of retailers’ delisting practices will be captured by the concept of collective dominance in the absence of any coordination or links between rival retailers.

In 2006 Faull and Nikpay note that the abuse of buyer dominance is especially relevant in the retailing industry and predict that given the increasing concentration of retailers in Europe, these provisions may be applied more frequently to this situation. The provision for the calculation of market shares on the relevant purchasing market for buyers in the Vertical Block Exemption Regulation is a first step in this direction. It is possible that there might be a spillover effect, and that as a result the assessment of buyer dominance under Art. 102 will also be based on the market shares on the purchasing market. Although the Commission has been moving to a more economic approach toward Art. 102, especially following former Competition Commissioner Kroes’ speech at Fordham in 2005, it seems to have chosen the scenic route in relation to assessment of buyer power under Art. 102.

It should be recognized that the Guidance paper does sneak in the equivalent of Art. 101(3) in the assessment of dominance under Art. 102, and with it – the requirement of “pass-on” to consumers if the conduct is to be exempt. However, just as under Art. 101(3), this assessment is possible only after the conduct has been found to be in breach of competition rules, which, as this paper so far has shown, is difficult to do in practice.

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289 The so called “efficiency defense” is provided only under Art. 101 in the TFEU and was never a part of Art. 102
Chapter 6: Private Label Assessment in the EU Merger Control Framework

1 Merger Control - Bridging the Gap?

One of the main reasons for the adoption of the Merger Control Regulation in 1989 was the perceived gap in the powers of the Commission to control for behavior which would not be caught by Art. 101 nor by 102, but which could have significant negative consequences for competition in the common market.\(^{290}\) A gap with respect to Art. 101 would occur where companies interested in a collusive outcome, would avoid the difficulty and uncertainty of a cartel or tacit collusion by merging.\(^{291}\) An enforcement gap with respect to Art. 102 would occur where a company achieves independence of its customers, competitors and final consumers by acquiring a dominant position.\(^{292}\)

Through the control of concentrations, the Commission has been able engage in substantial economic analysis of the future effects of merger, and to consider the structure of a market or of a supply chain in its entirety. Indeed, it has to provide substantial evidence – if not, the Court of First Instance will not shy about quashing its decisions. It is thus not surprising that PLs, where they have come up in a merger examination, have been paid attention.

Private labels have been discussed in merger decisions ever since the early 1990s and have been examined under the old Merger Regulation (EEC) No 4064/89. In the absence of case law under Arts. 101 and 102 of the Treaty, it could even be argued that the examination of the role of PLs in merger decisions paved the way for the subsequent investigations of PLs and the inclusion of PL-specific references. Even if they were not the reason for these changes, some of the merger decisions have provoked the interest in scholars in these issues, and have “brought to life” the theoretical discussion of PLs in previous chapters. But also, they illustrate how much broader the scope for assessment is under the Merger Regulation rather than under the Treaty articles, among other things, with respect to dominance criteria (including collective and buyer dominance) and buyer power.

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\(^{291}\) Ibid., pp.385-386
\(^{292}\) Ibid., pp.385-386
2 Dominance v ‘Significant Impediment to Effective Competition’

Originally, the application of the Merger Regulation required finding that the merging companies would become dominant on the relevant market and thus be able to significantly impede effective competition. Under the 2004 Merger Regulation, however, a finding of dominance was reduced to being indicative, though not mandatory for the Commission to show that effective competition would be impeded. After these changes, dominance is reduced to just one example of an impediment to effective competition.

This broader test enables the Commission to consider mergers of entities with much lower market shares than those in Art. 102 case-law; and even lower than the market share thresholds required to trigger an individual assessment of vertical restraints under Art.101. Under the Merger Guidelines, the Commission presumes that no investigation would be necessary for mergers between entities whose combined share does not exceed 25% in the common market or a substantial part of it, however the Regulation would be applicable to entities with combined market shares between 40% and 50%, and sometimes below 40%.

Even before the adoption of the 2004 Merger Regulation, the Commission had already reviewed mergers between retailers where dominance would have been shaky to prove. In the Rewe/Meinl decision, for instance, the parties had respectively [27-33]% and [5-10]% market share, thus accounting for, at most, 43% of the market. The combined share of Kesko and Tuko supermarkets in the retail market for groceries was found to be 55%. Such market shares would have been more difficult to qualify as dominant for the purposes of Art. 102, where the standard threshold is 50% and the lower limit is 45% market share. It has been pointed out that the clearing of a merger does not preclude the subsequent application of Art 102 should the undertaking start abusing its dominant position in the future. Yet, for situations in which the

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293 Art. 2 (3) reads: “A concentration which creates or strengthens a dominant position as a result of which effective competition would be significantly impeded in the common market or in a substantial part of it shall be declared incompatible with the common market” (emphasis added).
294 Art. 2(3) of the 2004 Regulation reads: “A concentration which would significantly impede effective competition in the common market or in a substantial part of it, in particular as a result of the creation or strengthening of a dominant position, shall be declared incompatible with the common market” (emphasis added)
296 European Commission Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings (Merger Guidelines) [2004] OJ C 31/03 [18]
297 Ibid., [17]
298 These are the market shares without taking into account discount stores. As Rewe/Billa operated some discount stores, if these would be taken into account the market share of Rewe/Billa would be in the band 33-38% and 5-10% for Meinl, thus accounting for at most 48% of the market – still below the traditional concept of dominance established in Akzo of 50% market share. –see Rewe [24]
merged entity falls short of dominance, the importance of merger control becomes even greater. The flexibility of the Merger rules with regard to dominance allows the Commission to fill that gap.

Under the Merger Regulation, it is also possible for the Commission to review a merger which would result in an oligopoly or a position of collective dominance. As was discussed in the previous chapter, the concept of collective dominance has hardly been used under Art.102 to capture the unilateral action of oligopolists or oligopsonists. However, the Merger Regulation specifically provides for the possibility of controlling for situations of collective dominance. The Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings (the Merger Guidelines) state that “the concept of dominance has also been applied in an oligopolistic setting to cases of collective dominance” and it is not necessary to prove likelihood of coordination between oligopolists for the Regulation to bite.

3 Buyer Power in Merger Decisions

The Merger Regulation and Guidelines explicitly allow for the possibility of examination buyer power on its own, not just as “countervailing buyer power”. In its brief discussion of buyer power, the Commission makes reference Rewe/Meinl and Kesko/Tuko, both mergers between supermarket chains. Indeed, buyer power in these decisions was assessed much before the adoption of the 2004 Regulation and Guidelines (respectively in 1996 and 1999). For example, in Kesko/Tuko, the Commission recognized that there is a separate market for the procurement of goods, and carried out a comprehensive analysis to determine the buyer power of the retailers, especially Kesko (though it did not come up with specific market shares on the procurement market). The Commission concluded that “the most important distribution channel for daily consumer goods is clearly through retail supermarkets” and that although there were other possibilities, they could not substitute the one-stop-shop experience provided by the supermarket.

In Kesko/Tuko, the Commission estimated that the majority of the suppliers of Kesko and Tuko depend on them for approximately 50 to 70% of their total sales in the country. Finally, the commission identified Kesko’s buyer power as the main reason why there is no actual or potential competition from foreign companies in the markets for retail distribution of goods and for cash and carry. The Commission’s

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303 The Merger Guidelines [2004] OJ C 31/03 state at [61]: “the Commission may also analyse to what extent a merged entity will increase its buyer power in upstream markets”.
304 See Kesko/Tuko [146-153]
305 Kesko/Tuko [146], also [33-35]
306 Kesko/Tuko [150]
307 Kesko/Tuko [154]
research showed that Kesko’s buying power “will constitute one of the most significant barriers to foreign entry since one of the key questions for any potential entrant will be to secure access to daily consumer goods at prices which allows such an entrant to effectively compete with Kesko”\(^\text{308}\).

Similarly, in the *Rewe/Meinl* merger decision, the Commission recognized the “decisive importance” of buyer power because it brings the buyer more favorable conditions which in turn fuel the company’s growth in the distribution market.\(^\text{309}\) Dominance as a buyer and as a retailer, the Commission notes, would enable a company to squeeze its competitors from the retail market, and thus from all the markets.\(^\text{310}\) The Commission also found that the procurement side is very concentrated, while the supply side is fragmented and varies in terms of the number and size of producers supplying (including a lot of small and medium-sized enterprises).\(^\text{311}\) It also recognized the fact that switching distribution channels for the suppliers is costly if not impossible, and that overall suppliers are much more dependent on retailers than the other way around.\(^\text{312}\) Finally, *Rewe/Meinl* is also interesting because, as was noted in Chapter 4, in it the Commission actually worked out the procurement market shares held by the merging retailers.

As for mergers between brands, the Regulation provides the examination to include an assessment of countervailing buyer power as a stage of the examination of constraints to the exercise of dominance (i.e. countervailing buyer power)\(^\text{313}\), much before the countervailing buyer power was introduced in the Guidance paper on Art. 82.

### 4 A Virtuous Circle

Furthermore, both in Kesko/Tuko and Rewe/Meinl, the Commission recognized that the procurement and retail markets, may be separate, but a strong position on one reinforces the retailer’s position on the other.\(^\text{314}\) In *Rewe/Meinl*, the Commission calls it an “interdependence between the distribution market and the procurement market” and also a “spiral” to reflect the reality of one advantage feeding into the other. The implications are, the Commission notes, that the dominant buyer can make or break a brand, i.e. because “the supplier has no chance of reaching the final consumer [if the dominant buyer refuses to purchase, it the retailer who] determines the success or otherwise of product innovations.”\(^\text{315}\).

The discussion of the dynamics of buyer power above is not directly related to the effects of PLs. Nevertheless, such a discussion is very important, because the anticompetitive effects of PLs play out in the

\(^{308}\) Kesko/Tuko [158] also 154-161  
\(^{309}\) Rewe/Meinl [54-55]  
\(^{310}\) Rewe/Meinl [55]  
\(^{311}\) Rewe/Meinl [78], [89]  
\(^{312}\) Rewe/Meinl [79-80]  
\(^{313}\) Merger Guidelines [2004] OJ C 31/03 [64-75]  
\(^{314}\) Kesko/Tuko [38], Rewe/Meinl [71-74]  
\(^{315}\) Rewe/Meinl [74]
context of buyer power, from which they feed and which they back into. The consideration of buyer power in merger decisions provides necessary guidance for its assessment under the Vertical Block Exemption and paves the way for its more serious consideration under Art. 102.

5 The Incentives to Collude or to Follow

The Merger Regulation recognizes the possibility that a concentration may have as its object or effect the creation of coordination (or the strengthening of existing coordination between the undertakings on the competitive market and provides for the application of Art. 101 (1), and the efficiency defense in Art.101(3) to such concentrations. But also, the Merger Regulation allows for review of mergers where the collusive outcomes would not be the result of coordination. As oligopolistic firms are considered interdependent, it is anticipated that other firms in the market while not coordinating with the merging entities, may jump at the opportunity to increase their own prices. thus following the price increase initiated by the merged entities. The implication for stores carrying PLs is that in the context of mergers between brands, stores’ incentives to act as a price or quality follower will be considered. Their own brands (or just in general) will be considered, whether as a non-coordinated or coordinated effect regardless of the actual shares of the own label product.

Retailers’ general incentives to resist price increases as customers been assessed for instance in the proposed merger between Procter & Gamble and Vereinigte Papierwerke Schickedanz AG (VP Schickedanz). In this decision, the Commission examined the actual incentives for retailers to use their countervailing buyer power to resist a price increase or to go along with the increase in the aftermath of the merger. The Commission concluded that the incentives were insufficient:

“Even if it were accepted that retailers did have some countervailing power to use against P&G, it is also important to examine what the motivation of the stores would be to do so. [...] Higher prices might thus simply mean higher margins for distributors. Furthermore, given the relative price insensitivity of consumers in this sector and their brand loyalty, and the effect of advertising, which is to reduce the price elasticity of

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316 Merger Regulation Article 2 (4) of the
317 Merger Guidelines [2004] OJ C 31/03 at [24-25] where it is stated that “Non-merging firms in the same market can also benefit from the reduction of competitive pressure that results from the merger, since the merging firms’ price increase may switch some demand to the rival firms, which, in turn, may find it profitable to increase their prices. The reduction in these competitive constraints could lead to significant price increases in the relevant market” (footnote omitted).
318 Merger Guidelines [2004] OJ C 31/03 footnote 29
319 ibid, [24-25]
the advertised good, the distributor will be able to pass on the increase to the customer without losing volume. There is thus little motivation for a retailer to resist a price increase by P& G"321 (emphasis added).

There has also been consideration of retailers’ incentives to follow a brand’s price increase by increasing the prices of their own labels. In the context of the merger proposed by Kimberly-Clark and Scott, the Commission, in noting that a lot of retailers expressed support for the merger between the two paper products companies, interpreted this support as “a certain parallelism in the interests of retailers and the merging parties”322. It further explained that:

“the price leadership enjoyed by [the brand] and the high price level made acceptable by the success of its advertising, has allowed retailers in the past to follow [the brand’s] price increases upwards for the sale of their own store brands”.323

The Commission explained that it was “the phenomenal commercial success” of the brand which allowed “tissue paper manufacturers and retail sellers in the UK and Ireland to charge consumers prices for toilet paper that are among the highest, if not the highest, in the world”324. The Commission concluded that there was no reason to think that retailers’ behavior would change after the merger.325 Commission recognized the far-reaching effects in the market price rises by the merging brands may prompt several retailers to independently yet simultaneously raise the prices for both the brand and the private label. Finally, the Commission noted that price increases in the past have successfully been transferred onto consumers “to the mutual benefit of retailer and supplier”326, and to the obvious detriment of the final customer.

6 The Importance of Innovation

An interesting approach with respect to PLs was taken in the Kimberly-Clark/Scott merger decision. Usually, the Commission would include PLs in its analysis of the relevant market. However, in this case the Commission’s analysis went beyond a traditional consideration of market shares to assess whether private labels could be considered an important enough competitive constraint on the merging brands.327

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321 Ibid. [170]
323 Kimberly-Clark/Scott [192]
324 Kimberly-Clark/Scott [191-192]
325 Kimberly-Clark/Scott [192]
326 Kimberly-Clark/Scott [194]
327 Nicholas Levy, p.8-9 my copy
The Commission in this case found that private label competition was mainly on price and that PLs would not be capable of sustaining the levels of innovation in the industry because they were imitators, not innovators. Thus, the proposed merger was evaluated in light of the finding that it is the brands in the particular industry that drove innovation. Nicholas Levy compares this approach in *Kimberly-Clark/Scott* with the approach in DuPont/ICI where the Commission’s analysis once again went beyond market shares to emphasize the role of the merging companies as leaders “in terms of quality of products and technological development”. Even for brand companies which had not innovated for a while, the Commission took note of the possibility of eliminating “competition in innovation” and noted that such an elimination would cause consumer harm.

Nicholas Levy mentions that a merger between two brands is likely to be more carefully examined than a possible merger between two PL producers with the same market shares. Stricter merger control of mergers between brands may be justified as it will help preserve competition in innovation and competition in quality as well as competition on price. This is especially relevant in the case of the growing popularity of PLs, most of which depend on brands for product innovation and quality product development.

### 7 Consumer Welfare

The problem with merger control, as has been pointed out, is that it is only applied to new cases and cannot be used to address existing situations. Yet, it seems that the comprehensive analyses carried out under the Merger Regulation have been instrumental to defining notions such as collective dominance and buyer power, and have given a lot of food for thought to scholars and practitioners. The pass-on to consumers is also a requirement for the exemption of a merger.

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328 *Kimberly-Clark/Scott* at [162], the Commission states: “Product innovation is a key competitive tool in consumer product markets. It is well established in almost all consumer product markets that product innovation is pioneered by branded producers and that private-label products follow. In general, private-label products are rarely innovative products that generate new users and new occasions of consumption. Instead they tend to be price followers and product imitators. Indeed, manufacturers of branded products develop innovative products in part to slow, halt or reverse private-label growth, as well as to take sales from other branded products.”

329 *DuPont/ICI* (Case No IV/M.984)


331 Ibid., 406-407

332 *Procter & Gamble/VP Schickedanz (II)* (Case IV/M.430)) as cited in Nicholas Levy, “*Kimberly-Clark/Scott and the power of brands*” (1996) 17(7) ECLR, p.407


335 As per Art. 2 (4) of the Merger Regulation provide for an assessment of consumer harm when examining efficiencies just as under Art. 101(3)
Chapter 7: Conclusions

This paper has started out with the presumption that private labels introduced by retailers are not harmful to consumer welfare and that there is no scope for the application of EU competition rules to such situations. It has come to show PLs may lead to a reduction in consumer welfare, and that there might just be possibility for capturing some of these effects under EU competition rules. It has relied on theoretical and empirical studies in economics as well as on data from market investigations and EU Commission merger decisions to show that the introduction of own brands by retailers may result in, among other things, supracompetitive prices for both national brands and private labels, a lessening of the choice of products in stores, and even to collusive outcomes (with respect to price and quality). This is, of course, not due to the presence of the PL per se, but rather to the fact that PLs skew the incentives of a retailer and cause him to behave anticompetitively. The consumer welfare focus was chosen to fill a gap in the literature, and also because of its importance as one of the recently embraced goals of competition policy.

This paper has also offered insights as to the lack of litigation under EU competition rules in the case of anticompetitive behavior by powerful retailers. It was suggested that fears of retaliation, and the uncertainty as to how EU competition law may be used against a non-dominant retailer might have precluded suppliers from taking legal action. The adoption of new policy documents by the Commission might help alleviate these concerns, and create opportunities for the examination of the anticompetitive conduct associated with PLs. In particular, the introduction of a requirement that the buyer market share on the purchasing market be less than 30% in order for a vertical restraint to be exempt, may allow for the delisting of differentiated products in favor of copycat PLs to be examined under Art. 101 TFEU. It might also prompt the consideration of buyer dominance and buyer shares on the purchasing market under Art. 102 TFEU. On a separate note, the inclusion of more specific rules on information exchange in the context of horizontal cooperation agreements may inspire investigations into the (mis)use of suppliers’ information in the development, pricing, and quality decisions taken by the retailer with respect to the PL.

Although these new rules seem to offer exciting possibilities for the application of competition rules, they leave much to be desired. For one thing, the uncertainty as to whether a retailer offering PLs may be considered a competitor of his suppliers or not, might preclude interested parties or national competition authorities from evoking Art. 101. Furthermore, the lack of clarity as to how buyer market shares are to be calculated, and as to how a relevant purchasing market should be defined, might also
lead to uncertainty about the possibility of attacking a vertical restraint, in particular delisting. With respect to Art. 102, the rules on dominance remain such, so that proving retailer dominance, whether on the purchasing or on the distribution market, remains difficult. As for collective dominance and cases of abusive exploitation: these remain outside the scope of the Commission’s enforcement priorities for Art. 102.

In comparison, the effects of private labels have been the subject of thorough analysis in EU merger decisions. Indeed, these decisions offer important insights as to the potential application of EU competition rules to the PL-related practices of retailers and to the possible interpretation of these rules, i.e. with respect to the question whether the retailer is a competitor of his suppliers by virtue of offering PLs, and as to what approach is to be taken in determining market shares on purchasing markets.

This paper reveals that the application of EU competition law to cases of powerful retailers is a bit of a creative exercise. It almost seems as if the rules “don’t fit” the case. It could be, as some scholars have noted that competition rules, in the EU and in the US, were developed with the presumption of strong suppliers, as opposed to strong buyers. Where the market structure changes fundamentally, it is reasonable that rules should change as well. The recent revisions of some of these rules show a commitment on the part of the Commission to keep in pace with these changes. However, it seems that it will take time and, certainly, case law before the full reach of these new rules is known, this leaving to be seen what their actual implications will be for, among other things, consumer welfare.

336 Doris Hildebrand notes in her discussion on resale price maintenance that “Whereas in 1973 it was important to protect retailers from the power of the brand manufacturing industry, in 2003 the situation is almost the other way around” in Doris Hildebrand, “Thirty years prohibition of resale price maintenance – Germany on the verge of change” (2005) 26 (4) European Competition Law Review, p.237; Peter de la Cruz notes that the analytical criteria for vertical restraints in the US were developed with this kind of framework in mind in Peter De la Cruz, “Vertical Restraints: US and EU policy toward manufacturer-retailer relationships ” (1997) 18(5) ECLR, p. 292
ANNEX
### Table 1: European Grocery Market Concentration for 2000

<table>
<thead>
<tr>
<th>Country</th>
<th>Market share of the five largest retailers</th>
<th>Herfindahl-Herschman Index</th>
</tr>
</thead>
<tbody>
<tr>
<td>Netherlands</td>
<td>95</td>
<td>2394</td>
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<td>Sweden</td>
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Data source: AC Nielsen.

Table is replicated from Table 2.5 in D Bell, “The Business Model for Manufacturers’ Brands” in Ariel Ezrachi and Ulf Bernitz (eds), *Private Labels, Brands and Competition Policy. The Changing Landscape of Retail Competition* (OUP, Oxford 2009), p. 32
Table 2 : The Market Structure of the Grocery Retail Market in the EU in 1996

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Table 3 Who owns the shelves in Britain?\textsuperscript{337}

<table>
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</table>

The table is based on the 2009 market shares of British grocers as reported by Europanel\textsuperscript{338}. Tesco – 30.4% (represented as 30.5), Asda – 17.5%, Sainsbury’s – 16.1% (represented as 16), Morrisons – 11.8% (represented as 12), Aldi, Lidl, Netto (combined) – 5.9% (represented as 6), Miscellaneous other stores – 18.3% (represented as 18).

\textsuperscript{337} Author’s own work.

\textsuperscript{338} Europanel “Consumer Index. Western Europe – Big 6” (edition covering 1\textsuperscript{st} quarter of 2009) (Report) 
<http://www.gfk.at/imperia/md/content/gfkaustria/data/newsletter/int/europanel-consumer_index-big_six_q12009_en.pdf> accessed 12 June 2010. Note: market shares are available only for the British grocery chains.
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