

Unfair Trading Practices in the Business-to-Business Food Supply Chain

KEY FINDINGS

- **Unfair trade practices** imposed by the stronger party to a contract can have a profound **impact on the functioning of the market**, increasing costs and reducing revenues of the parties that experience them.
- Unfair trade practices can appear on **any side of the B2B transaction**, in **any sector** of the market. Recently unfair trading practices have been of particular interest to the EU in relation to food supply chains.
- Any consideration concerning **possible future action** in the area of unfair trading practices must consider a number of issues such as: **whether or not** legislative action is needed, and if so, **what scope and form** should it take. However, **the key element** of any action is to ensure its subsequent **effective enforcement**.

1. WHAT ARE UNFAIR TRADING PRACTICES?

Unfair trade practices are practices that grossly deviate from good commercial conduct and are contrary to good faith and fair dealing.¹ **Unfair trading practices** are typically imposed in a situation of imbalance by a stronger party on a weaker one, and can exist from any side of the B2B relationship.

2. EXAMPLES OF UNFAIR TRADING PRACTICES

Unfair trading practices can occur at any stage of the contractual relationship: during negotiations, when the contract is performed, or can be imposed in the post-contractual phase.

As emphasised by the European Commission,² during the performance of the contract, **unfair trading practices** may consist of two types of behaviour. On the one hand, one party may simply execute unfair terms contained in the contract, and on the other the stronger party might abuse its position, even if the terms of a contract appear to be acceptable for both parties (normally contracts do not cover all aspects of the parties' behaviour under the contract, or are so complex that the parties do not fully understand what the terms imply in practice). Moreover, parties might not have the same level of information about the transaction, which may lead to unfair conduct by a stronger party towards a weaker counterpart (in particular when the weaker party is an SME).

Examples of unfair trade practices brought forward include:

- contract-related changes: lack of written contracts, retroactive contract changes, unspecified, ambiguous or incomplete contract terms;

- unfair use of information: a failure to provide sufficient information about contract terms, a trading partner's use of confidential information;
- price-related measures: forced discounts, resale at loss, price control, low sales;
- advance/late payment, retrospective price adjustments, retrospective financing of promotions, or other practices that effectively lead to a retrospective adjustment of previously agreed supply arrangements;
- restricted market access/territorial supply constraints: selective distribution, geographical segmentation;
- misuse of private labels;
- purchase-related obligations: excessively high volume requirements, unjustified listing fees, exclusive supply obligations;
- additional payment requirements: listing fees, slotting allowances, joint marketing contributions;
- transfer of commercial risk: a trading partner's excessive and unpredictable transfer of costs or risks to its counterparty, placing the responsibility for the stolen goods entirely on the suppliers, obligation to compensate for losses incurred by the trading partners or long payment delays;
- unfair termination or disruption of a commercial relationship.

3. DISCUSSION ON UNFAIR TRADING PRACTICES IN THE B2B SUPPLY CHAINS (FOOD AND NON-FOOD) IN THE EU

The business-to-business supply chain is an important element of the European economy. Retail services represent 4.3% of the EU's GDP, 18.7 million (or 8.3%) of the EU's employees and 17% of the EU's SMEs.³ Supply chains guarantee the distribution to consumers of goods and services stemming from other economic sectors, such as agriculture, manufacturing, logistics and IT services. The food supply chains ensure the delivery of food and drink products to the general public for personal or household consumption. According to Eurostat HBS data, expenditure on food accounts for around 14% of the average EU household budget. Cross-border trade between EU Member States accounts for about 20% of total food and beverage production in the EU, and at least 70% of the total exports of agri / food products of EU Member States are destined to other EU Member States.⁴

In the last few decades, developments such as the increased concentration and vertical integration of market participants across the EU have led to structural changes in the organisation of supply chains. These developments have contributed to a situation of significantly different levels of bargaining power and economic imbalances in individual trade relations between the actors in the chain, and abuses of such differences may sometimes lead to unfair trading practices.

At an EU level, [unfair trading practices](#) were first discussed in the context of the food sector in 2009 when consumer prices rose against the background of agricultural price spikes. The lack of market transparency, inequalities in bargaining power and anti-competitive practices were reported to have led to market distortions with potentially negative effects on the competitiveness of the food supply chain as a whole. The Commission considered that consumers were not offered sufficiently fair deals in terms of product range and prices, and that intermediaries/food processing industrials/retailers had squeezed the margins of agricultural producers.⁵

In January 2013, the Commission published a Green Paper on unfair trading practices in the business-to-business food and non-food supply chain in Europe⁶ to gather stakeholder views on the occurrence of [unfair trading practices](#) in the food and non-food supply chain. The EC

Communication Tackling unfair trading practices in the business-to-business food supply chain,⁷ which followed the Green Paper of 2013 in July 2014, again restricted the scope of the Commission's interest to the food chain supply. The Commission concluded that while UTPs can, in principle, be present in any sector, the stakeholder feedback to the Green Paper of 2013 suggested that they are particularly problematic in the food supply chain. As declared in the Communication of 2014, the Commission does not foresee regulatory action at an EU level, and does not prescribe a single solution to address the issue of [unfair trading practices](#). The Commission encourages stakeholders and Member States to tackle UTPs in an appropriate and proportionate manner, taking into account national circumstances and best practice. In addition, the Commission encourages operators in the European food supply chain to participate in voluntary schemes aimed at promoting best practices and reducing [unfair trading practices](#) (in particular the Supply Chain Initiative). The Commission emphasises the importance of effective redress and is committed to continuing to work in close cooperation with the Member States and relevant stakeholders.

The European Parliament has also been present in the discussion on [unfair trading practices](#). In the Resolution of 2009 "Fair revenues for farmers: A better functioning food supply chain in Europe",⁸ the Parliament recognised the contractual imbalances and the enormous differences in numbers and economic power between farmers and retailers affecting the competitiveness of the food supply chain. The Parliament encouraged the Commission and Member States to adopt ad hoc measures in specific sectors (price transparency, competition, abuse of buyer power and contracting etc.). In 2010, EP Resolution "A more efficient and fairer retail market"⁹ stressed the importance of the retail sector as a driver for growth, competitiveness and jobs in Europe, and the need to remove all the obstacles that are hindering this sector from achieving its full potential. The Parliament recognised, among other things, the need to address contractual and commercial practices in business-to-business relations, where large actors are often perceived to impose unfair terms on weaker suppliers and retailers. EP Resolution "On imbalances in the food supply chain"¹⁰ tackled the problem of the progressive loss of bargaining power for agricultural producers, and in particular the critical aspect concerning their income. The Parliament insisted on the need to guarantee a fair, decent wage for farmers. Resolution "On imbalances in the food supply chain" of 2012¹¹ highlighted the European dimension of the imbalances in the food supply chain, which can lead to unfair practices. This resolution identified a list of specific [unfair trading practices](#) and called for specific regulation, supervision and sanctions. In 2013, EP Resolution "European Retail Action Plan for the benefit of all actors"¹² welcomed the establishment of a European Retail Action Plan by the Commission, and reaffirmed the economic importance of the retail sector. At the same time, the Parliament encouraged the Commission and the Member States to give the highest political prominence to the retail sector as a pillar of the single market. As for [unfair trading practices](#), the Parliament recognised their existence also in the non-food supply chain and underlined the difficulty that weaker market players (in particular farmers) experience when complaining about [unfair trading practices](#).

4. WHAT ARE THE CONSEQUENCES OF UNFAIR TRADING PRACTICES? (INTERNAL MARKET, CONSUMERS' WELFARE)

According to the Commission's findings,¹³ the key factor in the development of [unfair trading practices](#) is the inability to switch to another business partner and to terminate the existing relationship (due to high switching costs or the lack of such a possibility). The weaker party often fears that the commercial relationship could be terminated in the event of a complaint on its part. This 'fear factor' makes such complaints significantly less likely to occur: 87% of suppliers take no action beyond a discussion with their customer, 65% take no action due to fear of retaliation, and 50% doubt the effectiveness of public remedies.

As identified by the Commission,¹⁴ the harmful effects of [unfair trading practices](#) may take various forms:

- 1) **unfair trading practices** may affect the SME's capacity to survive in the market and undertake new financial investments in products and technology.
- 2) **unfair trading practices** can result in undue costs or lower-than-expected revenues for the trading partner in the weaker bargaining position.
- 3) Unpredictable changes of contract terms may lead to overproduction and result in unnecessary food waste.
- 4) The diverse regulatory environment that addresses UTPs at a national level implies that SMEs — with their limited legal resources — are confronted with a complex situation regarding **unfair trading practices** and the possible remedies.
- 5) **unfair trading practices** may dissuade some companies, in particular SMEs, from entering new geographic markets or even from cross-border trade.
- 6) **unfair trading practices** might have an impact on the welfare of consumers when it comes to pricing and the availability of products.

That being said, the overall effect of **unfair trading practices** on the market is difficult to fully assess in quantitative terms, yet the negative direct effect on those parties affected by such practices is beyond doubt. According to the data gathered by the Commission, 83% of the respondents asserting that they were subject to **unfair trading practices** said that these practices increased their costs, and 77% stated that these practices reduced their revenues.

5. EUROPEAN LEGISLATIVE INSTRUMENTS APPLICABLE TO UNFAIR TRADING PRACTICES

The EU law does not contain an instrument that would directly target **unfair trading practices**. The current regulatory framework at an EU level contains rules aimed at addressing unfair practices, but only in B2C relations (Directive on unfair contract terms in consumer contracts, Directive on unfair commercial practices). As stressed by the Commission, to some extent competition law, the proposed Directive on trade secrets and other cross-sectorial legislation can be useful in addressing **unfair trading practices** in certain situations. The Commission highlights that a proposal for a Regulation on a Common European Sales Law prohibits certain unfair terms in business-to-business contracts, which may provide a useful clarity in sustainable long-term relationships. However, the application of the CESL, once agreed by the co-legislators, would depend on a bilateral agreement between the trading parties concerned.

6. FUTURE ACTION CONCERNING UNFAIR TRADING PRACTICES AT AN EU LEVEL – ISSUES THAT SHOULD BE ADDRESSED

Legislative action – no legislative action

The first question that requires attention is whether a specific legislative action is required in order to limit **unfair trading practices** from the market, or even to eliminate them. The European Commission suggests that the most effective way of addressing UTPs is to combine voluntary measures (like the Supply Chain Initiative) and measures (also legislative) at a national level. At the moment there are no legislative instruments in EU law that would allow **unfair trading practices** to be addressed directly. This provokes the question whether, and to what extent, non-legislative measures can be effective in the area. The answer depends on who gives it: the representatives of retailers argue in favour of the effectiveness of the present, soft solutions, whereas the representatives of the suppliers are calling for hard law. The supporters of legislative measures claim that only hard law is sufficiently effective and persuasive to address such a complex phenomenon as **unfair trading practices**. The opponents argue that such an intervention would harm the freedom

of contract principle, and that since non-legislative measures have been introduced only recently, it is too early to claim that they are ineffective.

Legislative action – what form, which area?

If legislative action would be considered, there are two questions that require further attention: in which area of law should the measure be formulated, and what form should the intervention take.

It is evident that competition law in its present form does not properly address **unfair trading practices**, since the vast majority of market players (including those that use **unfair trading practices**) do not hold a dominant position triggering the application of EU competition law. At the same time, ensuring proper market functioning, where market power is evenly distributed among market players can be very useful tool in the long-term perspective. It can, on the one hand, reduce the possibility of **unfair trading practices** appearing on the market, and on the other reduce the fear factor impact when it comes to the reactions to UTPs by those businesses that are subjected to them.

When it comes to private law regulation, one could consider extending (with appropriate adaptations) the scope of application of the existing EU directives aimed at combating certain market phenomena, such as the Unfair Commercial Practices Directive or the Late Payment Directive. This type of regulation would ensure that the interested parties have the potential tools at their disposal to combat **unfair trading practices**. Such a legislative intervention could take a place at an EU or national level. The key aspect would be to provide a possibility to challenge the unfair trade practices in court. The mere existence of such an option would also have a preventive character. The ultimate success of the measure will depend, however, on whether the potential addressees will be willing to make use of the provided solutions (see also the point Private and public enforcement below).

Scope of the action (food – non-food supplies chains)

The Commission is in favour of limiting the scope of future actions to food supply chains. The arguments that support such an approach relate to the fact that the vast majority of responses in the public consultation held by the Commission came from the food industry. Moreover, the goods distributed in the food supply chain tend to be more perishable as compared with other types of goods distributed via supply chains. Accepting such an approach will also emphasise the special position of the agri-industry.

Arguments against the sector specific approach refer to the fact that there is no sufficient justification for distinguishing food and non-food supply sectors. According to this view, most of the problems that require attention have a general character and should be dealt with using general tools. Creating sectorial legislation might also have the negative effects of partitioning the market and preventing the creation of a coherent, harmonised regulation.

Public and private enforcement

The critical element of any future system addressing **unfair trading practices** is to ensure that the system is effective. This means that it must be accompanied by an effective enforcement mechanism, adjusted to the type of the chosen measure.

The greatest challenge for achieving the effectiveness of a system aimed at combating unfair trade practices is overcoming the problems that stem from the “fear factor”(i.e. when the weaker party fears that the commercial relationship could be terminated in the event of a complaint on its part). The fear factor is the reason why parties that are subjected to **unfair trading practices** are not willing to take action against their contractual partners who use these practices. The fear factor is an inherent element of unfair commercial practices, but also, to a certain extent, it is an inherent element of a contractual relation. As such, the fear factor cannot be effectively eliminated. Therefore, when assessing whether a given trade practice is unfair, the fear factor should be taken into account. That being said, it

must be remembered that for some parties it might be profitable/beneficial to remain in a business relationship even though its contractual partner uses [unfair trading practices](#).

The enforcement mechanism should therefore not be based solely on the concept of private enforcement, because the fear factor may indeed prevent parties who would be willing to combat [unfair trading practices](#) from doing so themselves. Therefore, the enforcement system should be based (at least partly) on the public enforcement mechanism. There are several building blocks to such a mechanism that can positively impact its effectiveness, i.e. limit the impact of the fear factor by making sure that the parties do not have to challenge UTPs openly by themselves. First, it would be the possibility of undertaking actions ex officio by a designated public office. Second – granting the possibility of filing anonymous complaints by the market players subjected to [unfair trading practices](#). The third element would be granting associations of businesses the right to collect and organise complaints from the market players that claim to be subjected to [unfair trading practices](#) (including anonymous complaints). Such an association could undertake action against [unfair trading practices](#) in its own name, after verifying that a certain practice is indeed harmful and frequent.

Documents related to unfair trading practices

1. The EP Resolution, *"Fair revenues for farmers: A better functioning food supply chain in Europe"*, (2009/2237(INI))
2. EP Resolution, *"A more efficient and fairer retail market"* (2010/2109(INI))
3. EP Resolution, *"On imbalances in the food supply chain"*, (2011/2904(RSP))
4. EP Resolution, *"On the imbalances in the food supply chain"* (2012/0012 (P7_TA))
5. EP Resolution, *"European Retail Action Plan for the benefit of all actors"* (2013/2093(INI))
6. EC Communication, *"A better functioning food supply chain in Europe"*, Brussels, 28.10.2009, COM(2009) 591
7. EC Communication *"Setting up a European retail action plan"*, COM(2013) 36 final
8. EC Green Paper, *"On Unfair Trading Practices in the business-to-business food and non-food supply chain in Europe"*, COM(2013) 37 final
9. EC Communication, *"Tackling unfair trading practices in the business-to-business food supply chain"*, Strasbourg, 15.7.2014 COM(2014) 472 final
10. EC Final Report, *"The economic impact of modern retail on choice and innovation in the EU food sector"*, September 2014
11. EC Final Report, DG Internal Market, *"Study on the legal framework covering business-to-business unfair trading practices in the retail supply chain"*, DG MARKT/2012/049/E, February 2014

- 1 EC Communication Tackling unfair trading practices in the business-to-business food supply chain, Strasbourg, 15.7.2014 COM(2014) 472 final, p. 2.
- 2 EC Green Paper On Unfair Trading Practices in the business-to-business food and non-food supply chain in Europe, COM(2013) 37 final, p. 6.
- 3 Eurostat 2010.
- 4 Report of the High Level Forum for a Better Functioning of the Food Supply Chain, December 2012.
- 5 EC Communication A better functioning food supply chain in Europe, Brussels, 28.10.2009, COM(2009) 591, p. 2.
- 6 EC Green Paper On Unfair Trading Practices in the business-to-business food and non-food supply chain in Europe, COM(2013) 37 final.
- 7 EC Communication Tackling unfair trading practices in the business-to-business food supply chain, Strasbourg, 15.7.2014 COM(2014) 472 final.
- 8 2009/2237(INI).
- 9 2010/2109(INI).
- 10 2011/2904(RSP).
- 11 2012/0012 (P7_TA).
- 12 2013/2093(INI).
- 13 EC Green Paper On Unfair Trading Practices in the business-to-business food and non-food supply chain in Europe, COM(2013) 37 final, p. 7.
- 14 EC Green Paper On Unfair Trading Practices in the business-to-business food and non-food supply chain in Europe, COM(2013) 37 final, p. 7.

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Manuscript completed in July 2015

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IMCO-2014-15

PE 563.430



CATALOGUE: QA-04-15-513-EN-C (paper)

CATALOGUE: QA-04-15-513-EN-N (pdf)

ISBN: 978-92-823-7634-8 (paper)

ISBN: 978-92-823-7635-5 (pdf)

doi:10.2861/81602 (paper)

doi:10.2861/530936 (pdf)