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# MODERN FOOD RETAIL AND UNFAIR TRADING PRACTICES

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## ABSTRACT

The abuse of bargaining power by retailers is reflected in unfair trading practices (UTPs) and there has been a growing interest among EU MSs to address them using regulatory approach and self-regulatory initiatives among market participants. The experiences of ex-YU and neighboring EU MSs are of interest for Serbia. Serbian food suppliers are not protected from UTPs apart from general competition and contract rules and payment terms regulation. Therefore, after a brief review of the global food retail trends and the role of power in the supply chain management in the introduction, the discussion focuses on UTPs and regulatory mechanisms to address them at the EU level, in selected EU MSs and in Serbia. Regarding existing EU and MS practices, it is recommended that Serbia introduce specific UTP regulation in the food supply chain and authorize the Commission for Protection of Competition for the enforcement.

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## Introduction

Modern food retailers have become more consolidated and concentrated and dominate food sales in developed countries. Highly competitive environment forces these companies to be more efficient and to expand their presence abroad, so their sourcing and outsourcing strategies become an important determinant of the integration of the world economy (Stamm, 2004).

According to Deloitte's Global Powers of Retailing Report, in FY2015 there are 133 FMCG (fast-moving consumer goods) retailers among world's Top 250 retail companies, accounting two-thirds of their total retail revenue (Deloitte, 2017). These

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retailers operate on average in 5.9 countries and earn 21.5% of retail revenue abroad. Six of the global Top 10 retailers in 2015 were FMCG companies with hypermarket/supercenter/superstore and discount store operational formats (Wal-Mart, Kroger, Schwarz, Carrefour, Aldi and Tesco) and their share in FMCG Top 250 retail revenue accounted for 21.7%. The Carrefour operates in 35 countries, Wal-Mart in 30, Schwarz in 26, Aldi in 17, etc.

In the late 1990s a wave of mergers and acquisitions in the supermarket sector was registered (Brown, Sander, 2007). This process continues throughout the 2000s and in 2016 was marked by the merger of the Koninklijke Ahold N.V. (the Netherlands) and Delhaize group SA (Belgium) to form Ahold Delhaize, one of the world's largest food retailers (Deloitte, 2017).

The share of the five largest operators (C5) on the total edible grocery markets in all large EU MSs, except Italy, lies in range of 40% to 60% (Chauve et al., 2014). According to the latest sector inquiry into the food, beverages and tobacco retail market in the Republic of Serbia, prepared by the Commission for Protection of Competition, the share of the five largest retailers in the total retail revenue in 2016 was 46.82%, with the dominant role of the two leading retailers - Delhaize Serbia (20.60%) and Mercator (15.98%). It is expected that the German Lidl soon after entering the market (2018, October) will have 5-7% market share and a third position, with good prospects for further growth (CPC, 2018).

Starting from the standpoints that supply chains compete, not companies (Christopher, 2005; Li et al., 2006) and that an effective supplier partnership can be a critical component of a leading edge supply chain (Noble, 1997), large grocery retailers take over the leading role in supply chain management - undertake new procurement systems and private quality and food safety standards (Reardon et al., 2004), adopt efficient consumer response practices (Van der Vorst, 2000) and develop private labels with higher profit rates as a result of economies of scale, developing the production itself and creating responsive customer-driven supply chains (Wortmann, 2010; Kotler, Keller, 2012).

Power represents one of the major elements of the supply chain management (Belaya, Hanf, 2016). Different sources of power (coercive, reward, legitimate, expert, referent, informational) have contrasting effects upon inter-firm relationships and chain performance (Maloni, Benton, 2000; Liu et al., 2010; Belaya, Hanf, 2016). Buyer power is globally defined as the ability of a buyer to influence the terms and conditions on which it purchases goods. A retailer has buyer (bargaining)<sup>4</sup> power if in relation to at least one supplier it can credibly threaten to impose a long-term opportunity cost (harm or withheld benefit) which, were the threat carried out, would be significantly disproportionate to any resulting long-term opportunity cost to itself (OECD, 1998).

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4 Buyer power and bargaining power are not substitutable concepts under European competition law. Unlike buyer power that can affect the whole market, bargaining power affects only a bilateral relationship of the parties concerned (Chauve et al., 2014).

According to Hernández-Espallardo and Arcas-Lario (2003), in the context of asymmetrical channel partnerships dominated by a downstream leader, authoritative mechanisms of coordination lead to improvements in market orientation of the upstream followers. Cox (2001) finds that buyer power, based on buyer dominance or buyer-supplier interdependence typical for food retailing, distinguishes itself as an effective tool in proactive supply development.

Supplier satisfaction, defined as the feeling of equity with the supply chain relationship no matter what power imbalance exists, is a potential source of supply chain competitive advantage and therefore it should have an important role in supply chain integration strategies (Benton, Maloni, 2005). However, necessity of maintaining a preferred supplier status, particularly in cases of inelastic supply, assets specificity and high switching costs, moderate supplier countervailing actions and creates opportunities for buyer power abuse (Renda et al., 2014; Fałkowski, 2017).

### **Materials and methods**

The review of the global food retail trends was carried out using Deloitte's Global Powers of Retailing Report. Several scientific papers and projects' reports and surveys examining the role of power in the supply chain management and the effects and costs of unfair trading practices in food retail is consulted and quoted. The analysis of unfair trading practices and regulatory mechanisms to address them at the EU level and in selected EU MS and in Serbia are mainly based on official documents and reports of relevant national and EU institutions and on national and EU legislation. During the discussion and formulation of conclusions and recommendations, the analytical-synthetic method was used.

### **Results and Discussion**

#### ***Unfair trading practices in the food retailer – supplier relationships***

The abuse of bargaining power by retailers<sup>5</sup> is reflected in unfair trading practices (UTPs). The UTPs are defined as practices that grossly deviate from good commercial conduct, are contrary to good faith and fair dealing and are unilaterally imposed by one trading partner on another (EC, 2014).

The key categories of UTPs can be described as follows: 1) unduly or unfairly shift of costs or entrepreneurial risks to the other party, 2) asking the other party for advantages or benefits of any kind without performing a service related to the advantage or benefit asked, 3) making unilateral and/or retroactive changes to a contract, unless the contract specifically allows for it under fair conditions and 4) unfair termination of a contractual relationship or unjustified threat of termination of a contractual relationship (EC, 2016).

In the case of British food retail, the most frequently recorded breaches of the Groceries Supply Code of Practices (GSCOP) include delayed payments, demands for lump sums for product stocking and demands for payment for better positioning on shelves

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5 UTPs can occur along the supply chain, but here the focus is on retailers' UTPs against suppliers.  
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(McClellan, 2016). Suppliers have been forced to pay for better shelf positioning or “seen money simply disappear from their trading accounts” (Moulds, 2015).

The following UTPs are on the List of bad practices in the food supply chain of the Ombudsman for relations in the food supply chain in Slovenia: payment delays, contractual restrictions on charging interest on late payments, franchising at noncompetitive prices, limitation of the right of suppliers to change prices upwards, return of purchased and received goods, transferring marketing activities to suppliers, unfair contractual penalty for non-delivery of goods and delay in delivery even due to force majeure, unwritten buyer’s requirement for lowering the purchase prices, transferring transport and storage costs to suppliers, slotting fees, introductory allowances, shrinkage fee and extra rebates, buyer’s recommendation to the supplier to sign a contract with a money transfer company, not agreed prepayment and cash discount billing and additional billing for the sale of receivables (Podgoršek, 2015).

Among the UTPs recorded in the Croatian retail sector are: restricted access to the market, advance payment for accessing negotiation, listing fee, slotting allowances, forced involvement in promotions, payment delays, unilateral and retroactive changes to contract terms, buyer’s requirement to the supplier to purchase packing materials from the specified operators, payment for not reaching certain sale levels, unilateral withdrawal of the product from the shelf, unconditioned return of unsold merchandise, etc. (Kelava, 2017).

The most common UTPs registered in the Hungarian distribution of agricultural and food products in 2010-2015 by The National Food Chain Safety Office were: use of fixed bonus, late payments, higher discount rates and long-term supplier’s consent, passing on the costs of actions benefiting the trader to the supplier, prohibited use of background conditions and unfair practices concerning business rules (Velő, Bors, 2015).

Several Romanian retail chains were registered in using framework contracts on which they would not intervene in case of objections, requiring an annual change of the contractual terms often increasing suppliers’ charges, delaying payments, delisting in an unreasonable way, blocking orders procedure or a supplier deliveries without refund of the entry or listing fees, imposing unconditional return of unsold merchandise, etc. (RCC, 2013).

There are many forms of “unfair coercive” conduct without economically objective justification in Bulgarian FMCG sector, in particular unjustified refusal to supply or purchase goods or services, subjecting a contractual partner to unjustified or discriminatory obligations or trading conditions and unjustified severance of established business relations (Petrov, 2015).

Agriculture in Serbia has been the biggest creditor of retail chains for years. Small and medium-sized enterprises are particularly affected by the high listing fees. Large FMCG manufacturers are also faced with payment delays and a range of discounts and charges – special promotion discount, warehousing inventory discount, shrinkage fee, listing fee, fee for stock to fill the shelves of new stores, etc. Among the special commercial

terms contracted as an expression of the buyer power are marketing costs, approval of a permanent loan to the buyer and cash discounts for prepayment. In addition to extra rebate for sale above a certain level, suppliers are demand to pay a year-end rebate (Dražković, Domazet, 2008).

In the CIAA & AIM EU-wide survey (2011) among intermediate FMCG processors, 96.4% of the respondents said they had been subject to at least one form of UTPs in 2009. The reported cost of these UTPs represents 0.5% of the turnover of companies surveyed (CIAA-AIM, 2011). According to a 2013 Dedicated Research for COPA-Cogeca, 94% of farmers and 95% of agri-food cooperatives report having been exposed to at least one UTP. The estimated damage from UTPs amounted to EUR 10.9 billion per year (EC, 2018a).

The lack of market transparency caused by UTPs leads to increased risk and uncertainty and squeezed margins with potentially negative effects on supplier investment and innovation capacities. Consumers may face loss of choice in short term, higher long-run prices and fewer new products, with potential knock-on effects on range and quality (Consumers International, 2012). However, it should be emphasised that the understanding of the impacts of UTPs (as well as of the effects of legal responses to UTPs) is still very limited and ambiguous (Fałkowski, 2017).

### ***UTP regulatory and enforcement frameworks***

The most significant UTPs related to contract breaches are covered with national contract law. Some EU MSs, like Germany, extended the application of Unfair Terms Directive (Council Directive 93/13/EEC on unfair terms in consumer contracts) towards B2B contracts (Renda et al., 2014; Glöckner, 2017). Excessive payment periods and late payment are tackled by the Directive 2011/7/EU on combating late payment in commercial transactions.

European competition law does not address the abuse of bargaining power in the zone below market dominance but Member States may, under Regulation (EC) No 1/2003 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, implement national legislation that prohibits or imposes sanctions on UTP acts, be they unilateral or contractual. Therefore, some EU MSs address the abuse of economic dependence or superior bargaining power within the extension of competition law (Renda et al., 2014; Glöckner, 2017; Cafaggi, Iamiceli, 2018).

The Directive 2005/29/EC concerning unfair commercial practices in B2C relationships (Unfair Commercial Practices Directive - UCPD) enables the extension to B2B relationships at national and EU level.

National private regulatory schemes often reflect the European private regulatory instruments, such as the European principles of good practice in vertical relationships in the food supply chain (2011), implemented and enforced by the Supply Chain Initiative (SCI), agreed in 2013 by 11 EU-level organisations, including Copa-Cogeca, and its national platforms (The SCI, 2018).

According to data from the Commission's 2018 Impact Assessment, 20 EU MSs have specific legislation on UTPs, four MSs have legislation of a limited scope (based on a consumer-type approach), and four MSs have no UTP legislation. Legislative instruments specifically applicable to the food supply chain were adopted in 12 EU MSs whereas in 8 MSs the UTP legislation is applicable to all sectors (though sometimes including specific provisions on food and groceries trade practices, e.g. in France, Latvia and Portugal) (*Table 1.*):

**Table 1.** EU MSs by UTP legislation

	Total	EU MSs
NO LEGISLATION ON UTPs	4	Estonia, Luxembourg, Malta, The Netherlands
LIMITED SCOPE LEGISLATION (mainly consumer-type UTP approach)	4	Belgium, Denmark, Finland, Sweden
SPECIFIC LEGISLATION ON UTP:		
CROSS-SECTOR, applicable: – along the supply chain	7	Austria, Cyprus, France, Germany, Greece, Latvia, Portugal
– towards retailers only	1	Lithuania
IN THE AGRI-FOOD SECTOR, applicable: – along the supply chain	8	Bulgaria, Croatia, Italy, Poland, Romania, Slovakia, Slovenia, Spain
– towards retailers only	4	Czech Republic, Hungary, Ireland, United Kingdom
TOTAL	28	

*Source:* Cafaggi, Iamiceli, 2018.

Considering the enforcement, many EU MSs, in addition to judicial enforcement and private dispute resolution mechanisms, designated an administrative enforcement authority with investigatory powers - ex officio or on the basis of parties' complaints<sup>6</sup> and sanctioning powers, including fines and, to a limited extent, injunctions (Cafaggi, Iamiceli, 2018).

The UK is among the leaders in the enforcement of rules against UTPs between retailers and their direct food suppliers. The Groceries Code Adjudicator, established by the Groceries Code Adjudicator Act (2013), enforces the Groceries Supply Code of Practice (GSCOP) set out in Schedule 1 to the Groceries (Supply Chain Practices) Market Investigation Order 2009, which regulates practices between designated UK retailers, with annual turnovers of more than £ 1 billion and their direct suppliers. The Adjudicator is able to investigate ex officio on the basis of parties' complaints, arbitrate disputes, make recommendations and fine designated retailers for breaching the GSCOP. The UK System has been mutually recognized with the EU SCI in June 2013 (The SCI, 2018). The Unfair Contract Terms Act (No. C. 50/1977) regulates unfair contract terms in B2C & B2B relations and is enforced by the courts.

6 Many administrative enforcers allow anonymous complaints but preserve the discretionary power to start investigations.

The ex-YU and EU MSs - the neighbors of Serbia were also regulated UTPs in food supply chain by a specific agri-food legislation, in addition to the existing provisions of general legislation and its extensions.

The Slovenian Agriculture Act (No. 45/08, 57/12, 90/12 – ZdZPVHVVR, 26/14, 32/15, 27/17, 22/18) defines UTPs as practices by which one party with its significant market power reflected in the volume or value of sales, contrary to good business practices exploits the other party, lists some of them and specifies that the contract is legally void in the part containing such provisions. The Agriculture Act introduces the institute of the Ombudsman for relations in the food supply chain. The Ombudsman is in charge for notification of UTPs to the Competition Protection Agency. The Agency is responsible for the supervision and imposition of fines in the minor offence procedure. Some UTPs are covered by unfair competition provisions of amended Prevention of Restriction of Competition Act (No. 76/15) and enforced by the court.

The Croatian Law on the prohibition of unfair trading practices in the B2B food supply chain (No. 117/2017) prohibits purchasers and/or processors or traders to abuse significant bargaining power, reflected in the total annual turnover, in relations to their suppliers. The Law lists UTPs and authorises the Competition Protection Agency to initiate the procedure ex officio and at the request of the party, detect breaches, assess voluntary commitments and issue injunctions and fines. The Law on Financing and Pre-bankruptcy Settlement (No. 108/12, 144/12, 81/13, 112/13, 71/15, 78/15) contains a blacklist of unfair contractual terms and is enforced by the court.

The Hungarian Act No. XCV of 2009 on the Prohibition of Unfair Distributional Practices Applied Towards Suppliers with regard to Agricultural and Food Products prohibits unfair distribution practices of traders, regardless of their market power, against suppliers of agricultural and food products and lists the practices considered to be unfair. Traders whose annual net revenues exceeded 20 billion HUF are obliged to prepare and publish their business rules and submit them to the National Food Chain Safety Office. The National Food Chain Safety Office has competence to collect confidential complaints, launch ex officio investigations, decides on commitments and impose sanctions.

In Romania, The Law 321/2009 on marketing of food products amended and supplemented by the Law 150/2016 incorporates the Code of conduct for the trade of agro-food products (2008) and mostly refers to the prohibition on traders to request invoicing/re-invoicing and charge suppliers for taxes and services, delisting and terms of payment. The National Consumer Protection Authority and the Ministry of Finance launch ex officio investigations and impose fines. The abuse of economic dependence is addressed by the Competition Law 21/1996 and enforced by the Competition Council.

The Law on Amendment and Supplementation of the Bulgarian Law on Food (No. 56/2015) prohibits a range of UTPs and establishes the Reconciliation Commission with the aim to settle out-of-court disputes between food producers and traders. The Law on Amendment and Supplementation of the Law on Protection of Competition (No. 56/2015)

prohibits the abuse of superior bargaining position (determined by the market structure and B2B relationship specificities) along the supply chains and provides a non-exhaustive lists of abusive practices. The Commission on Protection of Competition is entrusted to launch proceedings initiated by the affected parties as well as ex officio proceedings, following the procedure for unfair competition cases and issue injunctions and fines.

The Serbian Law on Protection of Competition (OG RS, No. 51/09, 95/13) does not go beyond the scope of EU competition law. The Law on Obligations (OG SFRY, No. 29/78, 39/85, 45/89, 57/89; OG FRY, No. 31/93; OG S&M, No.1/03) provides a general reference to the principles of good faith and fair dealing and rules for the obligatory relations, including general conditions of standard clause contracts. Late payments are tackled by the Law on deadlines for settlement of financial liabilities in commercial transactions (OG RS, No. 119/12, 68/15, 113/17).

The divergence of EU MS regulatory approaches to UTPs may lead to differences in the conditions of competition. The fear factor discourages the weaker party from taking legal action through courts. The enforcement and confidentiality issues are the main concerns related to the effectiveness of self-regulatory platforms in tackling UTPs. There is also very little coordination among MS enforcement authorities, due to the absence of formal coordination structures at EU level (EC, 2018a). These are the reasons why the UTP regulatory and enforcement frameworks is constantly changing, improving and harmonizing at the national and EU level.

### ***Future directions in UTP regulation***

Regulation of transboundary phenomena, overcoming divergence in UTP rules between the MSs, transaction cost savings and economies of scale in administration are listed as the main benefits of EU-wide UTP legislation. On the other hand, there are harmonisation and switching costs of such specific legislation that will be considerable, as well as the issues of over-regulation and further fragmentation and incoherency of the EU aquis (Swinnen, Vandeveld, 2017; Hilty et al., 2013).

According to Glöckner (2017), the application of contract law supplemented by an extension of Unfair Terms Directive to B2B contracts may afford appropriate protection against most types of post-contractual UTPs in supply chain. Competition law should be extended with regard to exclusionary practices of undertakings with less than absolute dominance. Unfair competition law can be used to address exploitative abuses in vertical relationships not covered by the contract or contractual declaration of intent (except in the situations of market dominance). Directive on unfair trading practices, drafted in general and large in parallel with the UCPD, should encompass both upstream and downstream commercial practices and include the prohibition of misleading advertising directed at nonconsumers.

Swinnen and Vandeveld (2017) suggest establishing a centralised adjudicator at EU level for aggregating confidential complaints from across the EU and referring them to national enforcement authority for proceedings and sanctions.



In 2017, after almost a decade of consideration of these issues, the Commission launched an inception impact assessment, which offers a set of policy options for UTP regulation in the food supply chain:

- 1) the status quo,
- 2) EU-wide non-legislative guidelines and recommendations,
- 3) EU framework legislation relating to only a few specific manifestly UTPs prohibited and stakeholders concerned, to complement national legislation and the SCI, in line with the approach outlined in the AMTF's report (2016),
- 4) minimum EU framework legislation relating to common general criteria at the chain level for MSs to determine UTPs, help stakeholders draw up a code of conduct and make the compliance with this code mandatory.

Legislation could further contain binding minimum criteria for national enforcement (EC, 2017).

After wide stakeholder consultations consolidated in the impact assessment report (EC, 2018a), the Commission launched a proposal for the Directive on unfair trading practices in B2B relationships in the food supply chain (EC, 2018b), with a restricted approach, complementary to stricter national UTP rules and voluntary codes, to tackle only a few particularly damaging UTPs in order to introduce a minimum common protection standard relating to UTPs for small and medium-sized farmers and SME suppliers in the food supply chain as regards their sales to non-SME buyers.

The UTPs that would be prohibited are: late payments for perishable food products, last minute cancellations of orders of perishable food products, unilateral and retroactive changes to the terms of the supply agreement and forcing the supplier to pay for wasted products. The UTPs that would be prohibited unless agreed in clear and unambiguous terms at the conclusion of the supply agreement are: a buyer returning unsold food products to a supplier, a buyer charging a supplier payment for the stocking, displaying or listing food products, a supplier paying for the promotion of food products sold by the buyer and a supplier paying for the marketing of food products by the buyer.

Member States are required to designate a public authority in charge for the enforcement while the Commission will set up a coordination mechanism between the enforcement authorities for the exchange of best practices. Suppliers established outside the Union should be able to rely on the EU minimum standard when they sell food products to buyers established in the Union to avoid unintended distorting effects. The Directive is expected to enter into force in 2020 (EC, 2018b).

Although faced with UTPs in relationships with large retail chains, Serbian farmers and food manufacturers are reluctant to address the court and discuss the violation of their rights within the chain because of the fear factor. Having in mind the above-considered EU MS practices and the Commission's proposal for UTP regulation, it may be recommended that Serbia introduce a specific UTP regulation in the food supply chain, harmonized with the EU UTP rules and authorize the Commission for Protection of Competition for its enforcement.

## Conclusions

Modern food retailers have become more consolidated and concentrated and dominate food sales in developed countries. The abuse of bargaining power by retailers is reflected in unfair trading practices. Although the understanding of UTPs impacts on suppliers, consumers and social welfare is still limited and ambiguous, there has been a growing interest of most EU MSs to address them at national and EU level using regulatory approach and voluntary, self-regulatory initiatives among market participants. Serbian farmers and food manufacturers are faced with a range of UTPs in their relationships with large retail chains but are unwilling to address the court because of the fear factor. Having this in mind as well as existing EU MS practices and the Commission's proposal for UTP regulation, Serbia should introduce specific UTP regulation in the food supply chain, harmonized with the EU UTP rules and authorize the Commission for Protection of Competition to monitor, collect confidential complaints, launch ex officio investigations and impose fines.

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## Conflict of interests

The authors declare no conflict of interest.

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