

Chapter Three

Ban on Selling Below “Net Invoice Price” – 1987 to 2005

3.1 Introduction

In this Chapter we concentrate on the definition of “cost” in the 1987 Order as, we believe, it is one of the most critical aspects of the ban that currently exists.

In the introduction to the previous Chapter we explained how the definition contained in the 1987 Order is based on the concept of “net invoice price”. We also looked in some detail at how that came about and why the definition does not represent the real cost of the goods concerned.

3.2 The 1987 Report of the Restrictive Practices Commission

In July, 1986, The Minister for Industry & Commerce requested the RPC to carry out a review of the operation of the 1981 Order “...in the light of developments since the Order was made and with particular reference to the issue of below cost selling...”¹

The resulting Report, which examined the practice of selling below cost in some detail, was submitted to the Minister on 9 January, 1987. The Commission decided “...after considering the intrinsic unfairness of the practice, and the effects which a prohibition on below cost selling might have, to recommend that selling below the net invoice price be prohibited by Order with no exceptions apart from products excluded from the scope of the Order.”²

This was the first time that the Commission had recommended a ban on below cost selling. We believe that the Commission’s deliberations on the issue in 1986/7 are of such fundamental importance even today that we have included the full text of Chapter 4 of their 1987 Report as Appendix Six to this Report.

It is clear that one of the key reasons for the recommendation was what was seen as the ineffectiveness of the ban on below cost advertising. The advertising ban had been introduced in the 1973 Order and strengthened in 1981. Now in 1987 the RPC said:

¹ RPC Report of Review of Restrictive Practices (Groceries) Order, 1981, Stationery Office, Dublin, 1987 (Pl. 4678).

² RPC 1987 Report, Para. 4.56, P.55 (See Appendix Six).

“The prohibition on advertising below cost, in particular, has not diminished the extent or reduced the effectiveness of below cost selling. We believe, therefore, that, in order to eliminate the practice of below cost selling, which the Commission has always regarded as unfair, we must now recommend the prohibition of the practice by Order.”³

Notwithstanding this conclusion, however, the Commission themselves said: *“It does appear that the ban on below cost advertising was largely effective up to June 1985...”* and they went on to acknowledge some of the reasons why it was no longer effective after this time. Principal among these seems to have been a High Court ruling in that year which identified a crucial flaw in the drafting of the prohibition.

According to the Court, in order for an offence to be committed it was not sufficient for the advertisement to list a price that was below cost, it would have to specifically say that it was below cost. Since it was unlikely that any advertiser would have made such a claim, it would have been clear from the ruling that the 1981 Order would have to be amended to facilitate a successful prosecution.

The files of the former Department of Industry and Commerce show that the Department had prepared an amending Order to take account of the High Court ruling but this Order had not been confirmed by an Act of the Oireachtas at the time the RPC completed their 1987 Report.

Notwithstanding the willingness of the Department and the Minister to tackle this deficiency in the ban on below cost advertising, the RPC recommended the introduction of a ban on below cost selling.

In fact, the 1987 Order, which implemented the recommendations in the 1987 Report and which remains in existence to this day, includes a prohibition on both below cost advertising and below cost selling. And it also includes the enabling provision first introduced in 1956 allowing suppliers to withhold supplies from a retailer who sells below the net invoice price.

3.3 Commission’s Conclusions & Recommendations on Use of “Net Invoice Price

While the RPC⁴ recommended the introduction of a ban on below cost selling, they did not do so unconditionally or without reservation, particularly in regard to the issue of net invoice price.

³ RPC 1987 Report, Para. 4.75, P.59 (See Appendix 6)

⁴ The members of the RPC at this time were Myles O’Reilly, Chairman, Patrick Lyons and Eamon Rohan.

In the context of the current debate on the future of the Order, the RPC's comments in 1987 concerning the issue of net invoice price are particularly relevant.

Indeed they are so germane to the issue at hand that we believe it is necessary to quote the RPC Report in some detail as follows:

“A further issue to be considered is the definition of cost. The [1981] Order at present defines it as net invoice price. We show elsewhere in this report that this may not be the real cost. If a prohibition on selling below cost is to be made, it would seem that, ideally, cost should be the real purchase price...”

“...It would seem then that, if a prohibition on below cost selling were to be recommended, it should have the following characteristics –

...(iii) Net invoice price should be, ideally, the real purchase price by the retailer...”⁵

*“We have already seen that the High Court in 1979, for the purposes of the prohibition on advertising below cost, established beyond doubt the meaning to be attached to net invoice price. However, the practice has developed, as we shall see later in this Report, of giving substantial discounts, rebates, allowances, long term allowances, fidelity bonuses and so on, in addition to the price list discounts. In general, while the invoice conforms to the price list it does not show all of the additional rebates. If this practice were to continue, a prohibition on selling below net invoice price would, as the 1980 Report feared would happen, be allowing the manufacturer to fix a price below which his products could not be sold but which was not the true cost. **This would be a form of resale price maintenance.** (Emphasis added.) It seems likely that competition will drive the invoice price down to the real price and if it does not do so, it would follow that the market is not as competitive as it appears. Acceptance of the definition of cost in the 1981 Order, because the High Court accepted it, and because it would likely to be the easiest way for the Examiner [of Restrictive Practices] to compare cost with the selling price, would seem to be the best approach if below cost selling were to be prohibited. This acceptance would not mean that there would be any valid reason, in our view, why all or almost all rebates, discounts, or allowances could not be shown on the invoice and this would seem to be one effect of a prohibition on below cost selling. In our view this would be beneficial.”⁶*

“A desirable effect (of a prohibition on below cost selling)...might be to encourage the inclusion of all discounts and allowances on invoices.”⁷

⁵ RPC 1987 Report, Para.4.31, P. 43/44.

⁶ RPC 1987 Report, Para.4.41, P.49.

⁷ RPC 1987 Report, Para.4.48, P.52.

“We recommend to suppliers and purchasers that all allowances, rebates, discounts and so on allowed to purchasers should be shown on the invoice and that, therefore, the invoice should show the true cost of the goods supplied. While we recommend this, and discuss it further in Chapter 5, we do not propose to make it mandatory by recommending an amendment to the Order.”⁸

“We have already recommended in Chapter 4 that below cost selling be prohibited on the basis that the prohibition would apply to selling below the net invoice price of the products. We would like to see the net invoice price representing the real cost of the products. This can be achieved by transferring all allowances, discounts or rebates to the invoice. We think this is good practice anyway and will simplify many operations for buyers and sellers. Because of the competition between multiples which appears to exist, we would expect that some multiples would want to sell some of their products at real cost or close to real cost. We hope that they will request that the net invoice price show the real cost to enable them to do so. We expect that these measures will, in time, increase transparency in the trade.”⁹

“The invoice does not, in many cases, reflect the real net price of the goods. In some cases, for example, suppliers pay ‘long term allowances’ which are not reflected in the invoice price. We accept that long term allowances might be useful to a supplier, if they are genuinely contingent on the achievement of certain sales targets by the retailer or wholesaler. However, we find this type of price reduction to be generally unsatisfactory for several reasons. As we are now proposing that retailers must not sell below the net invoice price we hope that competitive market forces will bring about a change and that the invoice will in future reflect the real net price of the goods.”¹⁰

3.4 The 1991 Review of the 1987 Order

The Order giving effect to the ban on selling below net invoice price, as recommended by the RPC, came into effect on 11 December, 1987.

On 2 December, 1988, almost a year to the day later, the Minister for Industry and Commerce requested the Fair Trade Commission¹¹ to carry out a review of the 1987 Order. This was in keeping with a recommendation to this effect contained in the Commission’s 1987 Report.

In fact, due to pressure of work, the review did not take place until 1991 and the subsequent Report of the FTC was not submitted to the Minister until 2 August 1991.

⁸ RPC 1987 Report, Para.4.62, P.56.

⁹ RPC 1987 Report, Para.5.27, P.74.

¹⁰ RPC 1987 Report, Para.9.10.

¹¹ The Restrictive Practices Commission was renamed the Fair Trade Commission by virtue of Section 5 of the Restrictive Practices (Amendment) Act of 1987.

3.5 The Majority View

The majority view¹² expressed by the FTC in its Report was that the ban on below cost selling was in all circumstances a serious restriction upon competition and upon the free play of market forces and should be revoked.¹³ Among the reasons given were the following:

“A further issue of concern to the two members is that off-invoice discounts appear to be quite significant in some cases, and to have increased in magnitude since the introduction of the ban. The net invoice price now prescribes the minimum resale price. Off-invoice discounts are not taken into account and so the minimum resale prices of products are higher than they would be in the absence of a ban. This feature also restricts the scope for price competition. Of even more concern, the two members consider that there is evidence that some suppliers have used the legislation to operate a form of resale price maintenance. The Commission has always recognised that a ban on below cost selling would be tantamount to official resale price maintenance with the net invoice price as the minimum resale price. More perniciously, some suppliers appear to have excluded all discounts from the invoice and have shown only their desired resale price on the invoice. While they have paid substantial discounts (up to 25% and 30%) off the invoice, the ban has meant that nobody could sell at below the net invoice/desired retail price without infringing the Order, and that retailers were obliged to take high gross margins on these products, with the invoice and retail prices being the same, or virtually the same, in all outlets.

The two members regard this practice, which amounts to resale price maintenance and which could grow in extent, as being a serious abuse of the legislation.”¹⁴

3.6 The Minority View

The Minority view was that of Mr Myles O’Reilly, the third and only other member of the Commission. His view was that the ban restricted competition *“...only to the extent that the competition is harmful and has distorting and anti-competitive effects...”*¹⁵ He concluded that the ban had been beneficial to consumers, to grocers and to suppliers and should not only be retained but should be extended. Nonetheless, he accepted that there had been *“..some difficulties with the ban as operated since 1987, notably with the use of net*

¹²The FTC was a three person body. The majority view was that of the Chairman, Mr Patrick M Lyons, and of Mr Patrick Massey, a member of the Commission.

¹³ FTC 1991 Report, Para. 7.124, P.84.

¹⁴ FTC 1991 Report, Paras 7.131 and 7.132, P.87.

¹⁵ FTC 1991 Report, Para. 7.182, P.101.

invoice price...¹⁶ He agreed that 'net invoice price' was "...an unsatisfactory substitution for 'cost'.¹⁷

Mr O'Reilly expanded on his reasoning in the course of his minority report. He said:

"The 1987 Report stated that 'it seems likely that competition will drive the invoice price down to the real price and if it does not do so, it would follow that the market is not as competitive as it appears.' As has been stated, in most cases, discounts, rebates and other allowances were not transferred onto the invoice so that the Commission's expectation was not realised. As will be seen, it is proposed to use 'cost' instead of 'net invoice price' as the point below which sales cannot take place, so overcoming this difficulty."¹⁸

Elsewhere in his minority report, Mr O'Reilly stated:

"Mr O'Reilly believes that the only satisfactory level for a prohibition on below cost selling should be the true or real cost of the goods, i.e. the price after taking into account all discounts or rebates related to those goods. This definition will make it more difficult for inspectors to satisfy themselves whether goods are being sold below cost or not. The proofs to be given in court will also be more complex. However, because of the disadvantages outlined above with the use of 'net invoice price' instead of 'cost' it is believed that the real definition should be cost."¹⁹

And in an utterly definitive comment on the matter, Mr O'Reilly concluded that:

"...the present definition of cost, i.e. net invoice price, cannot be permitted to continue. While (Mr. O'Reilly) believes that little damage has so far been suffered by consumers or by trade participants as a result of the present definition, nevertheless, the definition may lead to abuse by some sectors of the trade in the future."²⁰

3.7 Consensus that "Net Invoice Price" is Unsatisfactory Definition of Cost

Consequently, what is striking about the 1991 FTC Report is that, although the three Commission members were unable to agree on whether or not the ban on below cost selling should be revoked, they were unanimous that the use of 'net invoice price' as the definition of cost was unsatisfactory and likely to lead to abuse of the legislation.

¹⁶ FTC 1991 Report, Para. 7.149, P.94

¹⁷ FTC 1991 Report, Para. 7.197, P.105

¹⁸ FTC 1991 Report, Para. 7.166, P.98

¹⁹ FTC 1991 Report, Para. 7.223, P.109

²⁰ FTC 1991 Report, Para.7.217, P.108

Equally, the view in the 1991 Report that the use of the term ‘net invoice price’ had facilitated a form of resale price maintenance is consistent with the view expressed previously in the Reports of 1987, 1980 and 1972.

3.8 Consideration of the 1991 FTC Report

In examining this matter today, more than 13 years after the event, it does appear odd that no action whatsoever was taken, either to amend or revoke the 1987 Order, following the FTC Report in 1991.

Even had it been decided to accept the minority recommendation and retain the Order, it might have been expected that some consideration at least would have been given to the minority view that the use of ‘net invoice price’ should not be allowed to continue. This is particularly so given the strong language used in the minority report that the use of the term might lead to the legislation being abused.

We now examine why no changes were made to the Order in the wake of the 1991 Report.

3.9 Likely overlap with 1991 Competition Act

The 1991 Review and subsequent Report on the operation of the Groceries Order coincided in large part with the coming into force of the 1991 Competition Act, which was signed into law by the President in July of that year and which was subsequently commenced by Order of the Minister for Industry & Commerce on 24 September, 1991.

Section 5 of the Act prohibited any undertaking in the State from abusing a dominant position by “*directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions.*” This was seen as prohibiting predatory pricing – one of the key reasons for the introduction of a ban on below cost selling.

There is little doubt that the majority recommendation in favour of revoking the Order was influenced by the view that “*...the anti-competitive aspects of below cost selling would be covered by the Competition Act...*”²¹

Indeed, the majority within the FTC believed that having a parallel Order might even weaken the Act.²²

We have examined the files of the Department of Industry & Commerce from the period and it is clear that the Department favoured accepting the FTC majority recommendation that the ban on below cost selling be revoked

²¹ FTC 1991 Report, Para. 7.147, P.93

²² FTC 1991 Report, Para.7.148, P.93

because the main provisions of the Order were to be superseded by the Competition Act.

3.10 Decision to Keep Order Under Review

The files record, however, that on 9 December, 1991, the Minister decided that he would not make a decision to revoke the Order, but would keep the situation under review.

This decision was recorded in the following terms:

“In view of the fact that the Competition Act has only recently come into force and in order to give interested parties an opportunity to study the Report, the Minister has decided to keep the question of retention of the ...Order...under review.”²³

The Minister’s view of the matter was confirmed early the following year:

“The new legislation (i.e. the Competition Act)...has a much wider scope than the Restrictive Practices legislation (i.e. the Groceries Order) and there is therefore no cause to retain legislation parallel to the Competition Act indefinitely.”²⁴

There is little doubt, based on a reading of the files, that the Minister’s intention in the early part of 1992 was that the Groceries Order would ultimately be revoked. This would have involved accepting the majority recommendation in the 1991 Report.

And that, in essence, seems to be the reason why no consideration was given to amending the net invoice price provision in the Order as had been so strongly recommended in the minority 1991 Report.

Little point was seen in amending an Order that was destined to be ultimately revoked.

As a result, the use of “net invoice price” as a definition of cost was retained notwithstanding the unanimous view of the Fair Trade Commission that it was unsatisfactory and could lead to abuse of the legislation.

3.11 1993 Departmental Review

Subsequent to this point, there were a number of informal reviews of the operation of the Order conducted internally in the Department of Enterprise,

²³ Press release issued by Government Information Services on behalf of the Department of Industry & Commerce on 13 December 1991 – see Appendix Seven.

²⁴ Retail News Directory 1992, Foreword by Desmond O’Malley, T.D., Minister for Industry & Commerce – see Appendix Eight

Trade & Employment. In May, 1993, the Competition Policy Section of the Department wrote:

“The Department takes the view that the Order should be revoked. It contains rigid rules, such as the ban on below cost selling, which are inappropriate to present circumstances and deals with some issues such as credit terms which should either be left purely to the market place or regulated across sectors and not confined to the grocery trade. As long as the Grocery (sic) Order exists those engaged in the grocery trade will rely on the enforcement powers of the Director (of Consumer Affairs) rather than action under the Competition Act as was intended to be the case. The rigid structure of the Groceries Order can produce some absurd results. For example, since the reference point for cost is the net invoice price as shown by the supplier, the supplier can artificially influence upwards the retail price by, for example, excluding discounts or other benefits actually received by the retailer. Such retail (sic) price maintenance flies in the face of accepted norm of competition...In effect the grocery trade is operating under a set of competition rules different to those that operate elsewhere in the economy.”

The Minister’s ultimate intentions in this regard were made known internally within the Department as well as publicly and so all interested stakeholders would have been aware that the Order was not viewed as having a future in the long term.

Consequently, over this period, business, retail and producer interests, all of who campaigned for retention of the Order, extensively lobbied the Minister and the Department.

In September, 1993, the Director of Consumer Affairs told the Department that he favoured removing the Order “at some stage” subject to his being granted powers to enforce the relevant provisions of the Competition Act.

The Department continued to support the case for revocation but at the end of October, 1993, they expressed concern at the loss of market share by Dunne’s to Quinnsworth and said that: *“In the light of recent difficulties within the Dunne’s management structure the volatility of the market share has to be a cause of some concern.....It would not be useful to add to the uncertainty in the retail grocery trade at this time.”* The Department recommended that the Order be retained for a period of twelve months.

On 31 December, 1993, the Minister for Enterprise & Employment, acting on the recommendation of his Department, announced that he had decided to retain the Order for a further twelve months and added that any decision on the future of the Order *“..will be taken in the context of the overall review of the Competition Act...”*

3.12 1995 Departmental Review

The Department of Enterprise, Trade & Employment continued to take the view that the Order was anti-competitive and favoured its ultimate revocation.

However, in February, 1995, The Minister for Enterprise & Employment, Richard Bruton, announced that he had decided to retain the Order for a period of two years on the basis that the then existing Competition Act was deficient in that it gave the Competition Authority no powers of enforcement and provided no penalties for abuses.

The Minister said he intended to amend the Act to deal with these defects and added:

“When this legislation is on the statute books and in operation, I will then consider revoking the Groceries Order...I am convinced that the Groceries Order is not the best instrument for dealing with competition in this sector in the long-term...I am also concerned that there is some evidence that the Groceries Order may be inhibiting desirable price competition to the disadvantage of the consumer.”²⁵

3.13 The Competition & Mergers Review Group

The Competition (Amendment) Act, 1996 was enacted in July of that year and introduced the changes promised by the Minister particularly with regard to enforcement of, and penalties for, anti-competitive offences.

In September 1996, The Minister established the Competition and Mergers Review Group (CMRG) under the Chairmanship of Michael Collins S.C. Their terms of reference required them to review and make recommendations on, inter alia, *“The effectiveness of competition regulation and associated regulations.”*

This was understood by the Group to refer in particular to the Groceries Order.²⁶ Indeed, according to the files of the period, the Minister specifically asked the Group to look at the Order. A report was expected from the Group during 1997 but, in fact, not received until March 2000.

The Group published a discussion paper on the subject of the Groceries Order in December, 1999 and invited submissions on the topic. In their final Report they examined the operation of the Order in some detail, particularly the ban on selling below net invoice price. Very little argumentation emerged which had not been aired more than once over the many years since 1956 when the matter was first considered by the then Fair Trade Commission.

²⁵ Press release issued by the Department of Enterprise, Trade & Employment on 28 February, 1995 (See Appendix Nine)

²⁶ Report of the Competition & Mergers Review Group (Stationery Office, Dublin, March 2000. PN: 8487), Para 1.6, P.7

In the final analysis, the Group acknowledged that they were “...deeply divided on this issue.”²⁷

Nonetheless, the majority of the Review Group recommended that the Groceries Order be repealed and that “any legislation or regulation introduced in relation to the grocery trade should not include a ban on below cost selling.”²⁸

This recommendation now fell to the Tánaiste and Minister for Enterprise, Trade & Employment, Mary Harney, to consider. She decided, in the manner of her predecessors, to retain the Order but to keep it’s operation under review.

Announcing her decision the Tánaiste said

“I have carefully considered all the arguments and I have consulted widely with interested parties on both sides of the debate.

I am interested in where the consumer’s interest lies. However, the question is a finely balanced one. On the one hand the Competition Authority has sought the abolition of the ban on below cost selling while the Consumers’ Association of Ireland favours retention of the ban. Furthermore, the Competition Commission in the UK has recently concluded, following an extensive enquiry into the retail sector in the UK, that continuous below cost selling is not in the public interest.

I have come to the view that it is not in the consumer’s interest to remove the ban on below cost selling at the present time. I am particularly concerned that below cost selling could be used to eliminate competition in local markets.

*Of course, the groceries sector is changing very rapidly and I will keep the position under review in the light of developments.”*²⁹

And so, the future of the Groceries Order remained under review. A review which might best be described as “ongoing” ever since.

²⁷ Para 10.4.1, P.316. Membership of the CMRG included representatives of IBEC (Messrs Owen Killiain & Myles O’Reilly), ISME (Dr Robert Berney), ICTU (Mr Paul Sweeney), The Bar Council, (Mr David Barniville BL), The Law Society (Mr Gerlad Fitzgerald), The Consumers Association of Ireland (Mr Peter Dargan) as well as the Office of the Attorney General and the Department of Enterprise & Employment.

²⁸ Para 10.4.17, P.325

²⁹ Press release issued by the Department of Enterprise, Trade & Employment, 24 October, 2000 (See Appendix Ten)

3.14 1987 Order Can Only be Amended by Primary Legislation

The principal fact to emerge in the intervening period is that, on the advice of the Attorney General, the 1987 Order can only be amended or repealed by primary legislation and not by further Ministerial Order (see Chapter Twelve).

3.15 Conclusion

The decision in 1987 to retain the term net invoice price (and its definition) was not without reservation on the part of the Fair Trade Commission or the Minister and an assumption was made by both that the Order would encourage the trade to place all allowances, discounts and rebates on the invoice.

That this had not in fact resulted, forced the Commission in 1991 to a unanimous view that the use of the term net invoice price was unsatisfactory.

Notwithstanding the decision to retain the Order, the failure to amend its terms to reflect this view must be a cause of concern.

The continuing use by the trade in the intervening period of off-invoice discounts means that the Order has not operated in the manner that was envisaged in 1987 by the Commission, the Minister and the Oireachtas.

In the circumstances, we believe that there has existed since 1987 a potential for the terms of the Order to be abused.