

Executive Summary

Introduction

The first Groceries Order was made in 1956 and was designed to abolish resale price maintenance and otherwise to apply a set of fair trading rules to the grocery trade. The Order did not include a ban on below cost selling which was considered unnecessary by the then Fair Trade Commission.

Subsequent Orders were made in 1958, 1973 (twice), 1978 (twice), 1981, and, finally, in 1987. The 1987 Order remains in force to this day.

In the intervening years, the retail grocery trade in Ireland, and the operation of the Order, have both been the subject of many official reports, reviews and enquiries as follows:

- The Fair Trade Commission¹ Reports of 1966, 1972, 1975, and 1980, which either did not consider, or which recommended against, the introduction of a ban on below cost selling;
- The Fair Trade Commission Report of 1987 which recommended the introduction of such a ban, and their Report of 1991 which recommended that it be repealed;
- Internal reviews in the Department of Enterprise, Trade & Employment in 1993 and 1995, each of which supported the ultimate repeal of the Order;
- The Report of the Competition & Mergers Review Group in 2000, which recommended the revocation of the ban on below cost selling;
- The Joint Oireachtas Committee on Enterprise & Small Business Report of March 2005, which supported the retention of the ban on below cost selling;
- The Report of the Government appointed Consumer Strategy Group in 2005, which recommended that the Order be revoked in its entirety.

¹ Reference here comprehends the Restrictive Practices Commission by which this body was also known at different periods over the years. The two titles are used interchangeably in the course of this Report.

Key Provisions of the Order

These include:

Article 3

Prohibits resale price maintenance. This provision was part of the original 1956 Order and was designed to prohibit a practice prevalent in the trade at that time whereby suppliers acted collectively to set minimum prices below which certain products could not be sold by retailers. The Article allows a supplier to withhold supplies from a retailer who sells below net invoice price and he may also require a wholesaler to do likewise.

Article 4, 5 & 6

The provisions of these Articles effectively prohibit price fixing arrangements between parties in the trade. A supplier is permitted to recommend a resale price for any product but such a recommendation shall not be binding as a minimum resale price.

Articles 7, 8, 9 & 10

These provisions prevent unfair discrimination in the trade. A trade association or any combination of persons is prohibited from inducing a supplier or wholesaler to withhold supplies. They may, however, bring matters to the attention of suppliers or wholesalers which they believe would entitle them to withhold goods.

Articles 11 & 12

These prohibit sale below net invoice price and advertising for sale below net invoice price.

Article 13 - 17

Requires a supplier to prepare a statement of terms and conditions of sale and to sell according to those terms, and to provide details to the Director of Consumer Affairs when required.

Articles 18

Prevents the payment of advertising allowances and “hello money” to retailers.

Article 19

Technical provisions designed to facilitate enforcement.

Article 20

Excludes certain seasonal goods from the prohibition on sale below invoice price.

Below Cost Selling

The 1987 Order is often considered to include a ban on below cost selling. Article 11, however, is constructed as a ban on selling below the net-invoice price. The distinction is critical because the definition of net invoice price is not a true reflection of cost. It does not include (a) overhead/operating costs incurred by a retailer and (b) discounts, rebates and other allowances paid to the retailer by his supplier but which are not shown on the invoice.

Such payments, known as off-invoice discounts, are a significant feature of the trade but we have not received sufficient information as a result of this Consultation Process to allow us to quantify them.

The term “net invoice price” has no economic rationale and was introduced into the 1978 Order as an administrative convenience. The definition of the term is based on a legal interpretation of its meaning as set down in a later High Court judgement in 1979.

The term “net invoice price” was retained in the 1987 Order on the assumption that it would result in all discounts, rebates and other allowances being reflected on the invoice. The fact that this has not happened represents a potential abuse of the legislation.

It also means that Article 11 of the Order is not working in the manner anticipated by the Restrictive Practices Commission (a view confirmed in a submission from the former Chairman of the Commission), the Minister or, in our view, the Oireachtas.

The Restrictive Practices Commission recommended in 1991 that the Order be revoked. A decision in this regard was postponed by the then Minister pending a settling-in period for the new Competition Act, 1991. As a result, serious reservations unanimously expressed by the Commission in regard to the use of the term “net invoice price”, and in particular in regard to the fact that it could lead to an abuse of the legislation, have never been reflected in the form of a legislative amendment to the Order. This is a matter of concern.

Terms & Conditions in the Grocery Trade

Article 13 of the Order, which requires a supplier to maintain a statement of terms and conditions of sale, is not working in the manner envisaged by the Fair Trade Commission, the Minister or the Oireachtas. The Commission

concluded as far back as 1987 that there was only token compliance with the provisions of this Article.

The Article permits the use of supplementary terms which are operated generally in a secretive, arbitrary and discriminatory way. Although such characteristics are not of themselves a cause of concern, the provisions of this article also facilitate and encourage the use of off-invoice discounting.

Structure of the Irish Grocery Trade

The Irish grocery market shows a high degree of concentration.

Market concentration has grown in the period since the Groceries Order was introduced. Much of this increased concentration has taken place below the level of the multiples and, particularly in the period since 1994, would seem to have been driven by consolidation in the symbol/independent segment.

The Irish market demonstrates similar structures and levels of concentration to the UK market, where, of course, no ban on below cost selling exists. If anything, we believe that the Irish market is marginally more concentrated.

We believe that within the main urban areas, a dualistic structure exists with multiples catering for the “one-stop” shopper and the smaller symbols/independents catering for the convenience “niche” market.

A similar dualistic structure is unlikely to operate in more rural locations due to the fact that many multiples are not attracted to areas of low population density. Thus the symbols/independents are servicing both the “one-stop” and the convenience markets in these locations.

In the UK, the convenience sector is the fastest growing sector of the grocery market as is evidenced by the recent entry into the market by many multiples and by Irish symbol group operator, Musgraves. Turnover in the convenience sector is expected to grow by 25% over the next four years.

Consequently, and given the similar market structures that operate, there is no reason to believe that the convenience market in Ireland would suffer as a result of the removal of the ban on selling below net invoice price.

Off-invoice Discounting

The Director of Corporate Enforcement has submitted that the practice of off-invoice discounting may not be advantageous from a company law perspective and sees it as desirable that the Order be amended to remove any direct or indirect inducements to engage in such practice.

We consider it likely that some proportion of off-invoice discount income earned by the retail grocery trade is offset against operating costs and as

such is passed on to the consumer. Information provided by the trade is, however, disappointingly vague and, as a consequence, we are not in a position to calculate either the extent of such discounts or how much of the income earned from such discounts is passed on to consumers.

The Order does not protect suppliers from the buying power of larger retailers, although such power is likely to be reflected in demands for higher discounts rather than lower invoice prices.

Nonetheless, because of the prohibition in Article 11 on selling below net invoice price, off-invoice discounts cannot be passed on to the consumer in the form of lower prices on products covered by the Order. This is a serious restriction on the freedom to trade.

Off-invoice discounting is a practice that, in consequence, acts against the interests of consumers.

Impact on Competition

The ban on selling below the net invoice price means that a form of resale price maintenance operates in the Irish grocery trade. This is in serious conflict with other provisions of the Order. Resale Price Maintenance is also an anti-competitive practice that can attract criminal sanctions under the terms of the Competition Act, 2002.

The Order has the effect of eliminating price competition from the market and that, in turn, is driving market concentration. That is unlikely to be advantageous to consumers.

The ban also represents a serious restriction on competition that could only be justified by clearly identifiable benefits accruing to traders, consumers and the economy as a whole.

We cannot draw the conclusion that such benefits exist.

Predatory Pricing

It has been represented to us as part of the Consultation Process that the Groceries Order should be retained because it prevents predatory pricing.

Selling below cost is not of itself an act of predation. There are many legitimate reasons for temporarily selling goods below cost and consumers should be allowed to benefit from them.

In general, below cost selling is only harmful to consumers if it is predatory.

Loss-leading is a legitimate business practice which operates in many business sectors and can be a logical outcome of the competitive process. It

is a practice that can operate without distorting the market and without producing any consumer detriment.

The practice of persistent below cost selling of grocery products, when operated in a manner that does not meet the definition of predatory pricing, is not prohibited by the Act. It is possible to conceive of rare instances in which the practice might act against the public interest if its effect is, or is likely to be, an alteration in market structure resulting in less choice for consumers.

We consider that great care needs to be exercised to ensure that vigorous competition (which encourages lower prices and benefits consumers) is not mistaken for predatory pricing.

The current Groceries Order is a virulently anti-competitive and disproportionate response to the threat of predatory pricing.

H. Williams

We have found no evidence to confirm that the 1987 Order was introduced as a direct result of the collapse of the H Williams Group, as has been suggested.

Neither can we conclude that H. Williams went out of business solely on account of predatory tactics employed by its competitors or at all. The 1991 report of the Restrictive Practices Commission, contemporaneous media reports and contributions to an Oireachtas debate at the time all suggest that other factors, including the fact that the company was in a vulnerable financial position, had a significant part to play in determining the company's future.

Impact on Inflation and Prices

We have received conflicting submissions in regard to the impact of the Groceries Order on inflation figures. These differences can be explained by the reference periods and product groupings on which the parties have chosen to base their submissions.

In our view, it is very difficult to determine, either historically, or into the future, the impact of the Groceries Order on either the rate of inflation, the absolute prices of grocery products at retail level in Ireland, or the comparative prices of such goods relative to those in other jurisdictions. This is because other determinants, such as input costs, taxation policies, consumer demand, the impact of competition and efficiencies in the distribution chain, make it impracticable to isolate out the impact of any one factor such as the Groceries Order.

Nonetheless, we note that Irish food inflation in the period since 1996 is the third highest in the EU (pre-accession 15) and is almost three times higher

than in the UK.² We do not believe that this can be adequately explained by higher input costs in the Irish retail sector.

At a minimum, there are certain anomalies shown up by our analysis of inflation trends which are not readily explained and which are highly suggestive of the retail food sector being protected from competition. In particular, it would be unsafe to draw a conclusion that there is *no* connection between these anomalies and the Order.

Consequently, while we are reluctant to draw firm conclusions in regard to the impact of the Order on inflation and price levels, we consider that our analysis of inflation trends would support the case for repeal of the Order.

We conclude that the removal of the Order would amount to removing a floor under the price of the vast majority of food items sold in grocery stores.

While we cannot quantify the impact of this and do not believe that such a quantification is possible, we regard it as self-evident that such a move would stimulate competition, drive increased efficiencies at all levels of the distribution chain and produce a consequent downward pressure on retail prices from which consumers would ultimately benefit.

Consequently, we believe that the removal of the Groceries Order would act in the interests of consumers.

Regulations in Other Jurisdictions

The argument has been made in many submissions received that Ireland's prohibition on below cost selling is in line with practice and law in other jurisdictions.

We have conducted research into the regulation of below cost selling in other jurisdictions, and in particular in the 14 other pre-accession member states of the European Union and in Canada, the United States, Australia and New Zealand.

In seven other jurisdictions (Belgium, France, Greece, Italy, Luxembourg, Portugal and Spain), bans exist on below cost selling but most contain notable exceptions which make them, in our view, different to the 1987 Order in terms of likely impact. We have not researched the structure or characteristics of the trade in these member states and so direct comparisons in terms of the operation and impact of bans in these jurisdictions are not possible.

Of the seven, the prohibitions existing in France and Greece most resemble our Groceries Order. The French prohibition, the Loi Galland, is hugely controversial and has been significantly amended in the course of 2005.

² Source: Eurostat

In the remaining countries examined, including those outside the Union, we have identified no specific ban on below cost selling but all prohibit predatory pricing as an anti competitive practice. The terms of such prohibitions are very different to the Groceries Order and are broadly comparable to the abuse of dominance provisions in Article 82 of the EU Treaty.

We note that the eight countries of the EU who operate bans, of one form or another, on below cost selling have experienced the eight highest rates of food inflation in the Union in the period since 1996.³

Ghost Town Britain

A large majority of submissions received in favour of retaining the Order have argued that its removal will result in small independent retailers going out of business. It is suggested in these submissions that Ireland will end up like the UK where, it is alleged, 7 out of 10 towns and villages have no local shop.

We have researched the provenance of this statistic in some detail on account of the frequency of its appearance in individual submissions. We conclude that the statistic is wrong and is a serious and manifest misrepresentation of actual research undertaken by a UK Government agency.

The repeated use of these figures in submissions is, we find, suggestive of a concerted campaign to create unwarranted concerns as to the possible impact of the removal of the Groceries Order.

Almost 87% of rural households in England live within 4km of a petrol station – most of which have a convenience store attached.

79% of rural households in England live within 4km of a supermarket.

The Ghost Town Britain II Report published in 2003 actually argues that prices of fresh meat and vegetables in edge-of-town supermarkets are often *higher* than in local independently owned retail outlets.

Societal Impact

We acknowledge the concerns of poverty groups about the possible impact that removal of the Groceries Order might have in terms of access to groceries for those on low incomes. We do not dismiss such concerns lightly but we believe that these fears are unfounded. Independent research conducted by the Competition Commission in the UK suggests that there is no reason to suspect that access to groceries would be more difficult in the absence of a ban on below cost selling.

³ Source: Eurostat

Otherwise, the submission made on behalf of the poverty groups raises serious issues but ones which require a much broader policy response than can be offered in the scope of this Report.

We consider the Groceries Order to be an inappropriate mechanism by which to seek to control the level of alcohol consumption in Ireland.

Legal Status of the Order

Although a Ministerial Order, the 1987 Groceries Order like its predecessors was confirmed by an Act of the Oireachtas. As such, it has itself acquired the status of an Act of the Oireachtas. Therefore, it can only be repealed by primary legislation. Neither can the Order be amended by a further Ministerial Order. That too can only be achieved by primary legislation.

We consider it desirable, at a minimum, that drafting errors, anomalies and uncertain definitions in the existing provisions require clarification if the Order, as currently framed, is to be enforced in the future.

Conclusions and Recommendations

The provisions of the Order, and particularly the use of the term “net invoice price” are a form of Resale Price Maintenance, do not adequately define cost, are anti-competitive and act against the interest of the consumer.

In particular, we conclude that there is significant reason to believe the existence of cause and effect in the chain between the 1987 Groceries Order, the lack of price competition in the grocery trade, increased market concentration and higher rates of food inflation in Ireland relative to other retail sectors and relative to food inflation in the UK.

The terms of the Competition Act, 2002 are sufficient to prevent predatory pricing in the grocery trade.

The provisions of the Order are a disproportionate response to the threat posed by other forms of persistent below cost selling.

We do not believe, in any event, that that case is proven that instances of persistent below cost selling are likely to emerge to such an extent and in a way so harmful to the public interest as to justify the introduction of regulatory measures beyond the prohibition on abuse of dominance already contained in Section 5 of the 2002 Competition Act.

The fear that the removal of the Groceries Order will herald the emergence of large scale hypermarkets at the expense of the small independent retailer is,

we consider, unfounded and suggests a misplaced faith in both the intention and scope of the Order.

Limiting the size of individual retail outlets is a function of the planning process.

Consequently, we can establish no valid case for retaining the Groceries Order and we recommend that it be repealed in its entirety.

We believe that regulatory measures designed to prevent instances of non-predatory but persistent below cost selling would be a serious interference with the freedom to trade and could only be justified by demonstrating conclusively that either competition or consumers would be seriously harmed by their absence.

In particular there is a serious risk that any such measures would be incapable of distinguishing between vigorous, pro-competitive price competition and instances of persistent below cost selling that might, in some circumstances, be harmful to the public interest.

We have concluded, however, that any alternative prohibition on persistent below cost selling that would operate in a less egregious way than the current Groceries Order runs a serious risk of operating in a manner more harmful to the public interest than is the threat of persistent below cost selling (loss-leading) in the grocery trade.

We recommend, therefore, that no alternative prohibition on persistent below cost selling be introduced consequent upon the repeal of the 1987 Order.

We recommend also that the Competition Authority, in cooperation with the Director of Consumer Affairs, be asked to review and monitor the structure and operation of the grocery trade on an ongoing basis over the next number of years by means of a Monitoring Unit to be established within the Authority.

We recommend, as part of their review, that the Competition Authority be asked to comment and make recommendations on guaranteeing access for all sections of society to as wide a range of grocery products as possible.

We also recommend that the Retail Planning Guidelines continue to operate in a pro-competitive way and so as to ensure the existence of an appropriate mix of small and large retail development throughout the country.

Objections to new retail development should be based on sound planning principles and vested interests should not be allowed to use the process to prevent the emergence of competition and so damage the interests of consumers.

We consider that the Competition Act, 2002 captures all of the anti-competitive practices which the Groceries Order was originally designed to prevent.

We recommend, however, that the 2002 Act be significantly strengthened in order to specifically prohibit resale price maintenance, unfair discrimination and “hello money”.