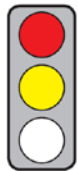


KEY ISSUES

Objective of the Green Paper: The Commission wants to prevent unfair trading practices by laying down requirements on the content of contracts between companies in the supply chain.

Parties affected: All companies in the supply chain leading to the delivery of goods to a consumer.



Pro: (1) Differing levels of information available to the parties may justify mandatory measures where one party intentionally withholds material information.

Contra: (1) Statutory interference in freedom of contract is only acceptable in the exceptional case where contractual conditions are imposed. The desire to combat unfair trading practices across the board, irrespective of whether there is market power, goes much too far.

(2) Statutory regulation is disproportionate where the companies affected are able to agree on self-regulation which is suitable for combating the problem.

CONTENT

Title

Green Paper COM(2013) 37 of 31 January 2013: **Green Paper on unfair trading practices in the business-to-business food and non-food supply chain** in Europe

Brief Summary

► "Unfair trading practices"

- The Commission wants to combat unfair trading practices in the supply chain between businesses ("Business-to-Business", "B2B") leading to the delivery of goods to consumers (p. 3).
- Unfair trading practices are practices, before, during or after conclusion of the contract, which (p. 3, 6)
 - "grossly deviate from good commercial conduct" and
 - are contrary to "good faith" and
 - are contrary to "fair dealing".
- Unfair trading practices result from (p. 6)
 - unequal negotiating power which enables the "stronger party" to impose conditions on the "weaker party" and
 - a differing level of information between the parties about the implications of the transaction.
- Increasingly over the last two decades, mergers and alliances between companies in the B2B supply chain have formed which have considerable negotiating power – not least "international retailer buying alliances" (p. 3).
- Until now, there has been no "specific" EU law to combat unfair trading practices. Existing regulations relate only to (p. 12 et seq.)
 - the relationship between businesses and consumers [Directive 2005/29/EC],
 - individual sectors such as the milk sector [Regulation (EU) No. 261/2012],
 - individual trading practices such as late payments [Directive 2011/7/EU, see [cepPolicyBrief](#)] or
 - unfair practices which distort competition (EU competition law).
- The Commission wants to combat unfair practices irrespective of the effect on competition in the market place and, in particular, irrespective of the existence of market power (p. 10).

► Justification for political action: Impact of unfair trading practices

- According to the Commission, unfair trading practices interfere with freedom of contract because contractual conditions cannot be negotiated to suit the needs of the parties (p. 6).
- They are also detrimental to investment and innovation, particularly that of small and medium-sized companies (SMEs), because
 - excessive risks are passed on to the weaker party or because the latter have to make unforeseen payments after conclusion of the contract which leads to uncertainty in business planning (p. 8-9), or
 - the stronger party refuses to sign confidentiality agreements and can therefore make unfair use of information e.g. on the development of competing products (p. 9, 19).

► **General requirements for contracts**

The Commission wants to impose general requirements on the way contracts are drawn up in order to prevent unfair trading practices (p. 18 et seq.):

- In principle, contracts must be in writing.
- They must set out the rights and duties "in a clear, transparent and unambiguous manner".
- They must specify circumstances under which subsequent contractual modifications can be made, particularly price changes, and provide for "compensation for any costs" which a party incurs as a result of contractual modifications.
- They must allow for a "fair" termination of the contract. In particular, they must prevent the "unfair termination" of business relations - such as "refusing to justify this decision" - and provide for a "reasonable" notice period.

► **Dealing with risks and costs**

- An "unfair" imposition of risks on the weaker party should not be allowed. In order to ensure that this is the case, the parties must agree that risks are not "unduly" transferred to the other party (p. 18-19).
 - The risk of theft should not be transferred "entirely" from the retailer to the supplier so as not to reduce the retailer's incentive to take preventative measures.
 - Neither party should "unduly" pass on the financing of "proprietary business activities" - such as investment in new retail outlets - to the other party.
 - Neither party should be "unduly" obliged to compensate for the losses of their trading partner.
- The Commission wants to use regulatory measures to restrict the ability of the stronger party to impose costs on the weaker party. (p. 18-19).
 - Parties can only ask for payment in respect of services already rendered or goods delivered.
 - Payments for services must "correspond with their value". In particular:
 - One-off payments by the manufacturer for its product to be included in the retailer's product range ("listing fees") must be "proportionate to the risk".
 - "Reverse margin practices" should not be "excessive".
Reverse margin practices allow the retailer to increase the margin between the cost price and the retail price by regaining part of the cost price from the supplier: it attaches additional services such as promotion and transport fees to the purchase of goods and charges the supplier for these services.
 - Contractual penalties must be "proportionate" to the damage suffered.

► **Dealing with information**

- Both contractual parties must take "reasonable" care to ensure that information provided to the other party is "correct and not misleading" (p. 19).
- Information, which one contracting party discloses to the other, must be used "fairly" (p. 19).

► **Ban on territorial supply constraints and territorial price differences**

- The Commission is considering putting a ban on territorial supply constraints because they enable territorial price differences.
 - Territorial supply constraints are bans imposed by multinational suppliers – particularly major branded goods manufacturers – on suppliers, wholesalers and retailers preventing sale of the supplied goods in other territories (p. 20).
 - The ban is intended to make the advantages of the single market available to consumers, particularly lower prices and a greater selection of products (p. 21).
- Varying prices in different territories will only be permitted if they are justified, e.g. by taxes or logistics costs (p. 21).

► **Transposition and enforcement**

- The Commission is considering setting up a regularly updated list of prohibited trade practices (p. 21).
- It is examining whether a "binding legislative instrument", a "non-binding" instrument or a "self-regulatory initiative" would be appropriate (p. 22).
- It proposes EU-wide standard "enforcement principles". National authorities would be able to (p. 17)
 - deal also with anonymous complaints, because the weaker party often "fears" that the stronger party might terminate the contractual relationship if it makes a complaint ("fear factor") (p. 7),
 - launch ex officio actions,
 - be given "investigative powers",
 - order compliance with fair practices,
 - recover damages,
 - impose appropriate sanctions such as fines and
 - report publicly on their "findings".

Statement on Subsidiarity by the Commission

There is a risk of the fragmentation of the single market where provisions to combat unfair trading practices and their enforcement diverge (p. 9, 15).

Policy Context

The Green Paper is part of the "European Retail Action Plan" being proposed concurrently by the Commission [COM(2013) 36]. The Commission already considered unfair trading practices in the food sector in 2009 [COM(2009) 591; see [cepPolicyBrief](#)]. In 2011, an Expert Platform of the "High Level Forum for a Better Functioning Food Supply Chain" formulated principles for fair trading practices. It is currently developing an "enforcement mechanism". In the Single Market Act I, the Commission announced measures to combat unfair practices between companies [COM(2011) 206]. The Commission is planning an impact assessment to evaluate the various possibilities for dealing with unfair trading practices and wants to propose further steps in 2013.

Options for Influencing the Political Process

Directorates General:	DG Internal Market and Services
Committees of the European Parliament:	Internal Market and Consumer Protection (leading), Rapporteur N.N.
German Federal Ministries:	Economy (leading)
Committees of the German Bundestag:	Committee for Economics and Technology (leading)

ASSESSMENT

Economic Impact Assessment

Ordoliberal Assessment

Unfair trading practices can result in a smaller product selection and distorted prices. They can also prevent investment and innovation activities. Nevertheless, when it comes to evaluating them, we need to differentiate between the two causes for the emergence of unfair trading practices identified by the Commission – unequal negotiating power and unequal levels of information between the contracting parties:

Unequal negotiating power, which allows the stronger party to impose contractual conditions on the weaker party, **does not justify a blanket ban on unfair trading practices because this restricts the freedom of contract for all companies**. The stronger party can do this because the weaker party has few if any alternative contracting parties. It therefore has a significant amount of market power. Nevertheless it must be decided in the individual case whether a company is actually misusing its market power. This is the task of the competition authorities.

Differing levels of information between the parties, on the other hand, **may justify mandatory measures where one contracting party intentionally withholds material information in order to make the other contracting party conclude a contract which it would not otherwise have done**. Where a party fears such conduct, it will either reduce its investment to a minimum in order to be able to back out of the contract more easily, or it will only conclude contracts with companies that it trusts. This restricts its contractual possibilities however. New and smaller companies will be particularly penalised because they do not have the required reputation.

The Commission's desire to combat unfair trading practices irrespective of the existence of market power therefore overshoots the mark by a long way.

Transposition by way of a list of prohibited trading practices – drawn up in case of doubt by the Commission – combined with the broad definition of "unfair trading practices", means that there is a risk of the Commission using the list to pursue other aims – particularly of a socio-political nature.

The provision in the enforcement process for companies to make anonymous complaints will not noticeably reduce the "fear factor" because companies know that they will have to identify themselves at some point in the future during a due process.

Impact on Efficiency and Individual Freedom of Choice

Setting out rights and duties clearly and in writing may, on the one hand, prevent unfair trading practices because it allows the level of information of the contracting parties to be equalised. On the other hand, the mandatory written form increases the bureaucratic burden on companies.

The blanket ban on the "unfair" imposition of risks and costs goes too far. It is only appropriate to ban parties from transferring risks which lie within their own sphere of influence. This is because the transfer of such risks is inefficient for the overall economy since the party in question can minimise these risks with lower costs. Thus passing on the risk of theft from the retailer to the supplier reduces the incentive for the retailer to take preventative measures and thus leads to more thefts. The Commission's expectation that the ban on transferring risks and costs will help the weaker party, is certainly too optimistic because the stronger party will seek to neutralise a transfer ban by way of higher retail prices or lower cost prices. A ban on the "unfair" imposition of risks and costs can only improve the situation for the weaker party if, at the same time, prices are also regulated. The very broadly worded term "unfair" also creates legal uncertainty.

The duty to ensure that information provided to the other party is "correct and not misleading" equalises the level of information between the parties and may thus prevent unfair trading practices.

The requirement that information must be used "fairly" is too general. The aim should only be to prevent a contracting party from misusing information to develop a competing product. If there is no such requirement, companies themselves will invest less in research and development. Instead they will wait until other companies have developed new products and then copy them (free rider behaviour).

Territorial supply constraints allow major branded goods manufacturers to vary final consumer prices according to the territory. **A ban on territorial supply constraints** will have the effect of aligning the prices – apart from differing taxes or logistics costs. This **is not necessarily advantageous for the consumer** however since, although more uniform prices lead to a reduction in price in some territories, in others there will be an increase. If consumers do not want to pay the higher price in these territories, there is also a danger that the product will disappear completely from those markets. **Territorial supply constraints should not therefore be subject to a blanket ban**, but should only be prohibited where market power is misused.

Legal Assessment

Legislative competence

The Commission wants to take action against unfair trading practices irrespective of whether they have an effect on competition in the market place. It cannot therefore base the planned measures on EU competition law because this only prohibits the misuse of a dominant market position (Art. 102 TFEU). The EU may however adapt national legislation in order to remove obstacles to companies in the internal market. The planned measures may contribute to removing obstacles and can therefore be based on the competence to adopt measures for the approximation of laws in the internal market (Art. 114 TFEU).

Subsidiarity

Unproblematic.

Proportionality

Statutory regulations are not necessary and therefore **disproportionate**, if unfair trading practices can be suppressed using less stringent methods. This is the case, **where the companies affected are able to agree on self-regulation which is suitable for combating the problem.**

Other compatibility with EU law

Statutory regulations for contracts interfere with freedom of contract (Freedom to conduct a business, Art. 16 Charter of Fundamental Rights of the EU, CFREU). **Interference may be justified, in the exceptional case, if otherwise** the imbalance between the contracting parties means that **contractual conditions would be imposed** and one party would have to bear a contractual burden unilaterally [cf. Art. 16 CFREU in conjunction with German Federal Constitutional Court (Bundesverfassungsgericht) Case No. 1 BvR 2501/04]. In all other cases, interference with freedom of contract is not justified.

Impact on German law

Not currently foreseeable. Depending on how the regulations are drafted, amendments may be necessary to the Civil Code (Bürgerliches Gesetzbuch), the Act against Restraints of Competition (Gesetz gegen Wettbewerbsbeschränkungen) and the Act against Unfair Competition (Gesetz gegen den unlauteren Wettbewerb).

Alternative action

Unfair trading practices arising due to a high level of market power on the part of one party should not be subject to a blanket ban. This should be dealt with by competition law. If competition law is unable to do this, it should be modified.

Conclusion

The Commission's desire to combat unfair trading practices irrespective of the existence of market power overshoots the mark by a long way because it restricts the freedom of contract for *all* companies. Differing levels of information between the parties may justify mandatory measures, however, where one contracting party intentionally withholds material information in order to make the other contracting party conclude a contract which it would not otherwise have done. The requirement that information must be used "fairly" is too general. The aim should only be to prevent a contracting party from misusing information to develop a competing product. A ban on territorial supply constraints is not necessarily advantageous for the consumer and should not therefore be subject to a blanket ban. Statutory regulations interfere with freedom of contract. This may be justified, in the exceptional case, if otherwise contractual conditions would be imposed. Statutory regulations are disproportionate where the companies affected are able to agree on self-regulation which is suitable for combating the problem.