Joint Purchasing: Assisting the Survival of Small Retailers in Small Markets

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Introduction

Competition regulators have concerns about joint purchasing arrangements because they can be a disguise for price fixing agreements. Sometimes, joint purchasing arrangements are entered into in order to counteract the strength of suppliers and are often used to purchase raw materials. In such cases the danger of reduced price competition for the finished product is seen to be greater, especially where the cost of raw materials is a significant component of ultimate cost.¹

In an age of globalisation and confronted with the might of big business, it may, however, be essential for small businesses to seek to pool their purchasing power. Small retailers or service providers may engage in joint purchasing arrangements in order to compete horizontally, rather than to counteract the strength of suppliers. This article asserts that joint purchasing arrangements should be assessed under Irish competition law with greater focus on their competition-enabling characteristics, rather than with a focus on their potential anti-competitive effects. In support of that assertion, the European Community, United States and New Zealand analyses of joint purchasing are reviewed in this article, as are the more prominent Irish cases.

Oligopsony differentiated

Roger G. Noll describes buyer power as involving the exercise by buyers of market power over sellers, and describes that as including an ability to force sellers to reduce prices below the level which would prevail in a competitive market.² This article focuses on efficiencies of scale scenarios—joint purchasing arrangements which are designed to allow horizontal competition. In many ways, the argument that is made is the corollary of art.82 of the EC Treaty’s treatment of discounts.³ The assumption is that the market remains competitive but the volume of the jointly purchased order justifies the discount. The discount in turn facilitates meaningful competition by smaller retailers and in some cases even ensures the supply of goods or services to more remote geographic areas, due to the ability of the retailers to continue to trade at a profit. The joint purchasing agreements allow the members to buy jointly and in larger volumes, thus allowing them to compete. There may be no buyer power in a joint purchasing arrangement, simply transport cost efficiencies and volume discounts, and so there is no real negative impact upon the seller.

Joel Davidow opines that a joint purchasing group is a restraint of competition where a member of a group of buyers is nominated to negotiate on behalf of all, and has delegated authority to agree a price within a certain band. If the negotiator can refuse to deal above a certain price, Davidow suggests there is a threatened boycott of the seller.⁴ However, for the purposes of European and Irish competition law, that per se analysis does not justify any prohibition of these arrangements. While in *Live Poultry Dealers Protective Association v United States*, the judge applied the Sherman Act provisions in a per se manner, stating that the defence of a lower price resulting for consumers was “surprising” (it having been settled “that the Sherman Act forbade all agreements preventing competition in price among a group of buyers”), the provisions of art.81(3) of the EC Treaty⁵ and s.4 of the Competition Act 2002 render that defence argument more relevant. The rule of reason bases of the European and Irish provisions necessitate a deeper analysis. Part I of this article describes the European Community and Irish approaches to joint purchasing arrangements, and Part II reviews the decisions of the United States and an alternative approach taken by the New Zealand legislation. Part III makes the case for a more liberal analysis of joint purchasing by Irish authorities.

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⁵ Live Poultry Dealers Protective Association v United States 4 F.2d 840(2d Cir. 1924).
⁶ Article 81(3) of the EC Treaty provides an exemption for anti-competitive agreements which meet certain efficiency criteria and as a result have pro-competitive effects.
had the effect of preventing, restricting or distorting competition. Where the joint purchasing was carried out by a group of small independent retailers competing in a market also occupied by multi-national retail operations, they could not realistically be said to have an objective of such prevention, restriction or distortion.

According to the Commission’s Decision 75/482 (IV/28.838-Intergroup) [1975] OJ L212/23:

“... joint purchasing by a voluntary association of retailers which imposes no exclusive purchasing obligations on its members will not ordinarily infringe Article 81(1)”.

Eminent EU lawyers Bellamy & Child opine that the Commission would exempt such joint buying “if the agreement enabled the retailers to obtain fair terms and put no undue pressure on suppliers”. Joint purchasing agreements which involve an arrangement as to the price to be paid would infringe art.81(1) of the EC Treaty because there would be no competition between purchasers, but joint purchasing agreements of a large number of purchases may lead to a common purchase price.

In the Intergroup decision, the Commission stated that a joint purchasing agreement could fall outside art.81(1) of the EC Treaty where it involved small and medium-sized undertakings with small market shares and consequently no distortion of competition. However, an agreement which obliged all or most purchases to be made under the arrangement would be held to constitute a breach of art.81(1). A fixing between them of maximum purchase prices would have the same effect.

However, the decision in Gottrup-Klim & Grovareforeninger v Dansk Landbrugs Grovareselskab AmbA is a more commercially sound one in this author’s view. In that case the European Court of Justice (ECJ) focused on whether the restrictions imposed on the parties to the joint purchasing agreement—including an obligation to purchase a certain percentage of requirements through the group—were proportionate and necessary to the operation of the buying group. The Court was therefore able to find that there was no infringement of art.81 of the EC Treaty.

Joint purchasing arrangements may be exempted where they allow for rationalisation, provided that

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7 Decision 80/917 relating to a proceeding under art.85 of the EEC Treaty (IV/27.958-National Sulphuric Acid Association) [1980] OJ L260/24. A joint buying pool in that case, which required members to buy 25% of their requirements from the pool, was held by the Commission to infringe art.81(1) of the EC Treaty but to have been capable of exemption under art.81(3).


don’t prevent access for competitors. The Notice on Agreements of Minor Importance suggests that a market share of less than five per cent will preclude the Commission’s interest. However, the percentage is a guideline and is not absolute, so it is of limited assistance to any group of retailers considering pooling their purchase orders. Furthermore, the Commission notification system which prevailed before Regulation 1/2003 [2003] OJ L1/1[11] is no longer available. Now a view must be taken on the legal provisions, and there is no mechanism to ascertain any reassurance or comfort from the Commission in advance of operating the agreement.

Irish Law

Irish competition law contains a provision equivalent to art.81 of the EC Treaty in the form of s.4 of the Competition Act 2002.[15] Unlike the situation under EC law, there is no de minimis provision in respect of s.4 of the Irish Competition Act 2002. That section prohibits agreements and practices which prevent, restrict or distort competition in goods or services within the state or in any part of the state. The previously applicable provisions were set out in the Competition Act 1991; s.4(1) of which prohibited anti-competitive agreements and s.4(2) of which empowered the Competition Authority to grant a licence in respect of an agreement which met the efficiency criteria equivalent to those in art.81(3) of the EC Treaty.

The question of joint purchasing has not often fallen to be considered by the Competition Authority (CA) or the Irish courts, but the approaches of those bodies appear overly cautious when compared with the EC approach in Guttrup-Klim.

The more significant decision arose under the earlier regime of the 1991 Act which allowed for the notification of agreements to the CA and their licensing by that Authority in the circumstances described above. The decision was made by the CA on September 19, 1994 and related to Musgraves Ltd Licensee and Franchise Agreements, which concerned exclusive purchasing and elements of group buying.[17]

In Musgraves Ltd Licensee and Franchise Agreements, the CA focused on the proportion of the market affected by the group purchasing agreement. In its notification to the CA, which resulted in the decision of September 19, 1994, the Musgraves stores were described as having a 16 per cent share of the relevant market.

The CA referred back to the European Union Decision 80/917 [IV/27.958-National Sulphuric Acid Association] [1980] OJ L260/24. However, in the Intergroup decision on joint purchasing, the Commission held that art.81(1) of the EC Treaty did not apply because the retailers were free to source goods through the centralised service (or not), and free to determine prices and resale terms. The CA noted that the Commission found no substantial effect on competition and that the purchases represented a very small proportion of the sales from the Spar shops. The CA then held that such considerations did not apply here and that the exclusive purchasing arrangements therefore infringed s.4(1). The CA made no distinction, in the end, as between the exclusive purchasing and group buying.

The exclusivity of the purchasing requirement resulted in a finding that the arrangements infringed s.4(1). In this author’s view that was too rigid a formula to adopt and the approach of the ECJ in Guttrup-Klim might have been a preferable one.

Furthermore, whether the terms of an agreement include exclusive purchasing obligations may be immaterial in a practical sense as the commercial incentive for the joint purchasing clearly exists to some extent where any joint purchasing arrangement is in place, exclusive or otherwise. Clark C. Havighurst makes the point that it will only be in exceptional circumstances that actual or potential competitors, or firms with absolutely no competitive relationship, “will find it expedient to arrange these buying co-operatives”. If the doctrine of ancillary restraints is applied, exclusive purchasing or an obligatory “percentage of requirements” purchasing obligation can be upheld as a necessary by-product of the arrangement—an ancillary restraint.

The litmus test of the arrangement ought to be the impact on market share of the joint purchasing arrangements and so the net questions would be: what market share do the joint purchasers have at the start of the operation of the agreement; what increase in market share is permissible; and at what point do questions of possible prevention, restriction or distortion of competition become relevant? Where the aggregate market share of the joint purchasers is below 20 per cent at the outset, it seems reasonable to conclude that the object of the joint purchasing agreement is not to prevent, restrict or distort competition. In an era of globalisation and when multinationals have been drawn to Ireland, it might be more commercial to hold that where the joint purchasing agreement has been operated for more than 12 months and the market share of members has increased by more than 10 per cent, then an infringement of s.4(1) is a possibility. At that stage the question might be whether the agreement has had the effect of preventing, restricting or distorting

[17] Musgraves Ltd Licensee and Franchise Agreements Dec No 354 and Norths CA/18/92E and CA/19/92E.