
Frequently asked questions: how does co-operation between farm businesses fit in with competition law

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FOREWORD

Farmers may want to get together for a variety of reasons. At the most simple level it could be to share machinery and equipment. At the other end of the spectrum it could be to agree common selling practices. The aim of these FAQs is to explain the types of agreements that could breach competition law and why. And to indicate those areas that are not likely to cause problems.

This guidance was promised in the Government's response to the *Report of the Policy Commission on the Future of Farming and Food* (Cm 5709) in order to provide more certainty to the agricultural community on competition law.

The views and information given in the following answers are intended to provide general guidance and should not be relied on as a complete statement of the law. They do not bind the OFT nor are they intended as guidance or a decision in specific cases. Farmers unsure of how they might be affected by competition law should refer to our published guidance, seek their own legal advice or talk to OFT.

These FAQs are set out under the following five sections:

- introduction
- farming cooperatives and other agreements
- dominant cooperatives (including market definition)
- mergers
- other issues.

The OFT has produced various guidelines on competition law and these should be used if further guidance on the FAQ is needed.

The main booklets relating to these FAQs are:

- *The major provisions*
- *Market definition*
- *Vertical agreements*

which can be found at www.offt.gov.uk/Business/Legal + Powers/modconsult.htm

and:

- *Overview of the Enterprise Act*
- *Mergers – substantive assessment guidance*

at www.offt.gov.uk/Business/Legal + Powers/Enterprise + Act/publications.htm

Guidance booklets can also be ordered in hard copy from 0870 60 60 321.

Please note that some of the OFT's guidelines are in the process of being revised. The revised documents should be available in September 2004.

The OFT is happy to get any feedback on the views expressed in these FAQs.

Comments can be sent to:

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INTRODUCTION

Q1 Why is competition so important? Sometimes it seems that the authorities want to preserve competition at the expense of farmers or others in the food supply chain.

A1 Competition is at the heart of any successful market economy. It provides a stimulus for businesses to improve their performance and to reduce their prices in order to gain an advantage over rivals and win more business. It encourages the development of new or improved products or processes and increases economic growth and living standards.

Without competition in food production there would be less incentive for farmers to offer better produce to their customers and, ultimately, to consumers. Anti-competitive agreements and abuses of dominant market positions increase prices and harm consumer choice as well as making the supply chain less efficient and undermining the performance of the economy as a whole.

Stopping businesses from colluding to fix prices ensures choice for consumers and prices that reflect the costs of production (including a reasonable profit). An effective market economy means competing to produce in the most efficient manner. Producers cut costs so that they can meet or beat competitors' prices.

New businesses coming into a market are more likely to flourish if existing businesses do not exploit their market power in an anti-competitive way, or agree prices with others. Existing businesses should innovate to respond to new rivals.

The OFT applies competition legislation in an even-handed way to all sectors of the economy. Within the framework of competition law, no one sector receives stricter or more favourable treatment than any other.

Q2 Who does what and, in particular, what does the OFT do in administering UK competition law?

A2 The OFT is an independent organisation which plays a leading role in protecting consumers' interests throughout the UK while ensuring that business practices are fair and competitive. The OFT uses its powers under competition law to:

- root out and deter all forms of anti-competitive behaviour (e.g. price-fixing). We use our powers under the Competition Act 1998 and EC law (Articles 81 and 82 of the EC Treaty) to do this

- refer to the Competition Commission (CC) mergers that we believe may substantially lessen competition (although most of the mergers the OFT considers do not do so) or markets in which competition appears not to be working well.

The CC conducts in-depth inquiries into mergers, markets and the regulated industries. Every CC inquiry is undertaken in response to a reference made to it by another authority, usually by the OFT or the regulators. The CC has no power to conduct inquiries on its own initiative.

The Enterprise Act 2002 established the Competition Appeal Tribunal (CAT). Among other things, the CAT's functions are to:

- hear appeals against OFT decisions
- hear actions for damages from victims of anti-competitive behaviour, and
- to review decisions on merger and market references (or possible references) under the Enterprise Act.

Q3 What are the key competition rules relevant to collaboration in the farming industry?

A3 The key rules administered by the OFT are the Competition Act, Articles 81 and 82 of the EC Treaty and the Enterprise Act.

The following is prohibited under competition law:

- agreements between undertakings, decisions by associations of undertakings and concerted practices¹ which have as their object or effect to prevent, restrict or distort competition (Chapter I of the Competition Act), and
- abuse of a dominant position by one or more undertaking(s) (Chapter II of the Competition Act).

Under the Enterprise Act, the OFT reviews mergers between undertakings. It has a duty to refer to the CC for further investigation any mergers which it believes have resulted, or may be expected to result, in a substantial lessening of competition in a UK market.

¹ Agreements between undertakings, decisions by associations of undertakings and concerted practices are collectively referred to in this FAQ as 'agreements'.

The OFT recognises the particular position of the agriculture sector and in particular the aims of the Common Agricultural Policy² (CAP). When applying competition law, the OFT must respect the objectives of the CAP to ensure they are not made impossible by the application of competition law.

Q4 Are farmers and/or their co-operatives undertakings under these rules?

A4 Yes. An undertaking for the purposes of competition law is any natural or legal person engaged in economic activity, regardless of its legal status and the way in which it is financed. An undertaking includes companies, partnerships and individuals operating as sole traders, charities and trade associations. Any activity consisting of offering goods or services on a market is an economic activity. Agriculture is an economic activity and farmers and their co-operatives are undertakings or associations of undertakings.

² The aims of the CAP are contained in Article 33 of the EC Treaty and are (a) to increase agricultural productivity by promoting technical progress and by ensuring the rational development of agricultural production and the optimum utilisation of the factors of production, in particular labour; (b) thus to ensure a fair standard of living for the agricultural community, in particular by increasing the individual earnings of persons engaged in agriculture; (c) to stabilise markets; (d) to assure the availability of supplies; (e) to ensure that supplies reach consumers at reasonable prices.

FARMING CO-OPERATIVES AND OTHER AGREEMENTS

Most forms of collaboration do not raise any competition problems. It is only where co-operation could appreciably affect the competitive process (e.g. collaborating to fix prices, share markets or limit production), that the OFT is likely to be concerned. Consumers are generally harmed by such collaboration.

Q5 If an association of farmers or an agreement between associations of farmers only covers a small share of the market does that raise competition concerns?

A5 Generally not. Some agreements are judged not to restrict competition because they cover a small proportion of the relevant market (see A17 below on market definition). Apart from price fixing or market sharing agreements (see below), competition law does not forbid co-operation under these conditions.

As a rule, if the parties to an agreement are competitors that have together less than a 10 per cent market share, there will be no appreciable restriction of competition. Undertakings in a vertical (supplier/buyer) relationship may in addition benefit from an exemption (and currently an exclusion), explained in A7 below.

However, agreements that involve price fixing or market-sharing will be regarded as being likely to restrict competition appreciably even where the combined market share is low. Market sharing occurs where undertakings agree that they will not compete on some territories, type of customer or some other criterion.

For agreements involving higher shares of the relevant market there is no presumption that the law will be broken. This will depend upon the overall effects of the agreement, the market(s) in question, the parties' market power and the precise terms of the agreement.

Q6 Aren't all forms of agricultural collaboration excluded automatically from the Competition Act?

A6 No. But many are. There is an exclusion from the Competition Act for agreements between farmers or farmers' associations (or associations of such associations) which:

- concern the production or sale of agricultural products (including livestock, dairy, meat and fish products as well as fruit and vegetables and other crops), or

- the use of joint facilities for the storage, treatment and processing of agricultural products.

But the exclusion only applies if the agreements meet certain conditions. The main ones being:

- the agreements are only between farmers or associations of farmers. For example, an agreement between a group of dairy farmers and milk processors would not come within the exclusion, nor would an agreement between livestock farmers and slaughterhouses
- crucially, the agreement does not involve an obligation on the farmers to charge identical prices for their products. Arrangements whereby farmers agree to sell through a co-operative and take whatever price the co-operative realises in the market should, however, benefit from the exclusion.

The OFT can withdraw the UK agricultural exclusion where it considers that the co-operation is likely or intended substantially and unjustifiably to prevent, restrict or distort competition. The OFT would give the parties an opportunity to discuss the operation of the agreement before withdrawing the exclusion.

Q7 Agreements with buyers in the food chain help farm businesses meet their customers' needs but don't seem to be covered by the agricultural exclusion. Does the Competition Act apply to such agreements?

A7 An agreement between farmers or a farmers' association and another business may be a vertical agreement. Vertical agreements are agreements between undertakings at different levels of the supply chain, for example, between a buyer and a seller. At present vertical agreements are excluded from the Chapter I prohibition, provided that they do not include price fixing. But the law is changing. From 1 May 2005 the UK 'vertical agreements exclusion' will be revoked and businesses will need to satisfy themselves that they are able to benefit from the EC rules exempting vertical agreements, which will also apply in UK law. To benefit from these exemptions the agreement must not involve any of a (small) number of hard-core restrictions (including price-fixing) and the parties must not have market shares exceeding 30 per cent of the relevant market.

The exclusion and the exemption may cover some or all parts of an agreement. For example, an agreement between an individual milk farmer and a milk processor or between a milk co-operative and a milk processor would be covered in full. However, an agreement between a group of farmers (not acting as a

cooperative) and a milk processor would be unlikely to fully benefit. In this case part of the agreement is between farmers and is actually a horizontal agreement, that is, one between undertakings at the same level in the distribution chain..

The protection given by these rules can be withdrawn in circumstances where particular competition concerns arise.

Q8 So, what sorts of collaboration are likely to be caught by the Chapter I prohibition of the Competition Act?

A8 Agreements cannot include an obligation to charge identical prices. The 'French beef' example in the shaded box describes an actual case of anti-competitive behaviour, which was not covered by the exceptions to the EU competition rules for agricultural undertakings, by French associations in the beef sector.

French beef

On 24 October 2001 six French agricultural associations entered into an agreement in the beef sector. Four of the associations represented farmers, including the association representing the co-operative movement and the FNSEA, the main French farmers union. The two others represented slaughterhouses. Under the agreement the associations jointly set a minimum price for beef. They also undertook to suspend or at least limit imports of all types of beef. The organisations knew that their action was unlawful. During the inspections carried out by the EU Commission in December 2001 documents were found which noted that the agreements were 'a bit against the law but that can't be helped' and asked 'can we close ranks, without being caught by the DGCCRF (the French Competition Authority).

On 3 May 2003 the EU Commission imposed fines totalling euro 16.7 million on the six participants to the agreement, of which euro 12 million was on the FNSEA.

The 'French beef' agreement was found not to benefit from the agricultural exclusion to Article 81 (and to have broken the law), because it involved an obligation to charge identical prices. It is likely that a similar agreement in the UK would not benefit from the UK agricultural exclusion and would infringe the Competition Act prohibition on anti-competitive agreements.

Even where the agricultural exclusion applies, agreements between farmers or farmers' associations to fix prices or share markets are likely to restrict competition appreciably. The OFT would be likely to seek to withdraw the

benefit of the agricultural exclusion (if it was thought to apply) from these types of agreement.

More generally, where an agreement is likely, or is intended, substantially and unjustifiably to prevent, restrict or distort competition the OFT would consider withdrawal of the agricultural exclusion. This includes agreements to limit supply or production to keep prices up or where the co-operation enables the parties to maintain, gain or increase market power and thereby to cause negative market effects with respect to prices, output, innovation or the variety and quality of products.

Q9 If an agreement is likely to be caught by the Competition Act but the parties feel there are justifiable grounds for its retention, are there any criteria they can use to make an assessment against?

A9 Yes, an agreement will not be prohibited under the Competition Act if it satisfies the criteria in section 9(1). It must:

(a) contribute to

- (i) improving production or distribution, or
- (ii) promoting technical or economic progress,

while allowing consumers a fair share of the resulting benefit; and

(b) not:

- (iii) impose on the undertakings concerned restrictions which are not indispensable to the attainment of those objectives, or
- (iv) afford the undertakings concerned the possibility of eliminating competition in respect of a substantial part of the products in question.

There is no requirement for a prior decision by the OFT that an agreement meets these criteria (i.e. businesses make their own assessment) but the OFT must take into account whether or not these criteria have been met when deciding whether the prohibition against anti-competitive agreements has been infringed.

Q10 I want to agree with other small farmers to share the use of equipment. Will the OFT be concerned about this?

A10 Generally no. Small local agreements of this kind can be good for business efficiency and are very unlikely to harm competition.

Q11 I want to share farm overhead with other farm businesses to reduce my costs. Does this cause competition concerns?

A11 Generallyly no. For example farm businesses may get together to purchase or deliver training courses, recruit jointly or share support services such as accountancy, payroll services or website design. These sorts of activities can be good for efficiency and are very unlikely to harm competition especially is their scale is not large.

Q12 How would competition legislation apply to an agreement to set up a farmers' buying group in order to negotiate better prices by bulk buying?

A12 The agricultural exclusion would apply to such an agreement provided that the conditions set out in A6 are met and the types of competition problems identified in A8 are absent.

If the exclusion does not apply, competition issues might arise only if the group had a very strong position in the buying market.

Q13 How would competition legislation apply to an agreement to set up a farmers' marketing or sales group?

A13 The agricultural exclusion might apply to a marketing or sales agreement but marketing or sales groups can cover a variety of arrangements and the competition assessment will depend on the details. For example, marketing might be generic advertising or producers selling under a common brand. Alternatively, joint marketing may be needed to have the scale and professional management to meet the specifications of large customers. None of these is likely to raise competition concerns.

It is important that the parties to a joint selling agreement are free to set their own prices but they can sell through a common organisation such as a co-operative, taking whatever price it realises for their produce. The co-operative should not otherwise constrain competition for example by limiting quantities sold by its members or imposing a choice of customer on them, which might amount to market sharing. Also, joint selling arrangements should guard against providing an opportunity for exchanges of sensitive commercial information, particularly on market strategy and prices. If a joint selling agreement would be likely to lead to a substantial and unjustifiable restriction of competition the OFT would consider withdrawing the agricultural exclusion.

Q14 If employees can collaborate legally to withhold their labour in order to obtain a fairer wage, why can't self-employed farmers and growers collaborate to withhold their produce in order to obtain a fairer price?

A14 Farmers and their co-operatives are undertakings under competition law. Employees are not undertakings and are not subject to competition law. Collusion among undertakings to withhold produce to get a 'fairer' price could mean higher prices and potential shortages to the detriment of consumers as well as potentially harming the future interests of those farmers who have developed their businesses to meet the demands of the marketplace.

DOMINANT COOPERATIVES

The agricultural exclusion does not apply to the prohibition on abuse of a dominant position.

Q15 What does 'dominant position' mean?

A15 The prohibition on abuse of a dominant position applies if the farmer or the co-operative in question is dominant in a market. A dominant position exists when an undertaking has substantial market power. It is highly unlikely that any individual farmer or local co-operatives will hold a dominant position but a national co-operative may do so if the relevant market is not international. Just because an undertaking is dominant does not automatically cause concern under competition law. It is only when that dominant position is abused that the law is broken. Accordingly, in the context of co-operation agreements in the agricultural sector, this prohibition is likely to be less significant than the prohibition on anti-competitive agreements.

Q16 What sorts of behaviour may be an abuse of a dominant position?

A16 Abusive conduct may be conduct which exploits consumers either through excessively high prices or discriminatory prices, or anti-competitive conduct against actual or potential rivals (sometimes called 'exclusionary behaviour'). Examples of the latter are:

- predatory behaviour (trying to drive competitors out of the market)
- some vertical restraints, unduly limiting competitors' access to the market, and
- in some circumstances refusing to supply existing or potential customers, without justification.

Q17 How does the OFT define the market in its competition analyses?

A17 The OFT follows the principles laid down in Europe³ on the definition of the relevant market for the purpose of Community competition law. We look at whether there are constraints that would prevent the prices of the products in question from rising above competitive levels. If there are not, then that product group forms a separate market. For some agricultural products the UK would not be considered a separate market because, if prices were higher in the UK, produce would be imported from abroad. But this may not happen for all farm

³ EC Commission Notice 97/C 372/03

produce, for example where transport costs are high or the commodity is highly perishable. Defining the market is important because it helps competition analysis. For example, market shares (used to help measure market power) can be calculated only after the boundaries of a market have been defined.

Q18 My company is based in the UK but we sell all over Europe. Is that not the relevant market for calculating market shares?

A18 Not necessarily. The relevant market for assessing an undertaking's market power might not be the same as the geographical area in which the undertaking operates. For example, if suppliers elsewhere in Europe are not an alternative for UK customers then the relevant market might be the UK, even if the undertaking in question sells elsewhere in Europe.

Q19 Recommendation 10 of the Government's response to the Policy Commission's report on the Future of Food and Farming said that, 'the competition authorities should consider the wider market context, particularly the consolidation of international suppliers when looking at new or expanding collaborative ventures'. Is this done?

A19 Yes. It always has been. The OFT defines markets in the way described in A17. If markets are genuinely international then we will define them as such and assess any competition issues in an international context.

Q20 Competition authorities seem to focus on market share, usually measured by an undertaking's sales, in relation to the market total as a measure of market power. Why don't the authorities also examine profitability?

A20 Market power exists where the constraints that would usually ensure that an undertaking behaves in a competitive manner are not working effectively, allowing it to increase prices above the competitive level. An undertaking's output or sales relative to the size of the relevant market (ie its market share) is usually a good indicator of its ability to influence prices in the market. High profits might arise from market power but equally they can be due to a variety of other factors such as a sharp increase in market demand or superior efficiency. Therefore an undertaking's profitability is not necessarily a good indicator of a firm's level of market power.

Q21 How does the OFT decide whether a farmers' co-operative is dominant?

A21 Farmers' cooperatives that are empowered to make economic decisions on behalf of their members are likely to be undertakings in their own right. While the members are unlikely to have substantial market power individually, a co-

operative may have. To ascertain whether it does, the OFT first defines the relevant market.

Having defined the market, we look at whether the co-operative has the power to behave independently of competitive pressures. Its market share will be one indication of its strength relative to existing competitors. We also consider other factors which might constrain the cooperative's behaviour. Principal among these are how easy it is for entrants to come in to the market but also the strength of buyer power, which might arise if customers are large relative to the cooperative. Every case is treated on its merits.

MERGERS

Q22 How does merger control fit in?

A22 Some forms of co-operation may amount to a merger if a party transfers some or all parts of its business to another party in the collaboration. However, unless the collaboration covers 25 per cent or more of the share or supply of goods or services of a particular description or the combined UK turnover exceeds £70m., the OFT will generally not need to consider it under the mergers provisions of the Enterprise Act.

Q23 Is it true that the OFT /Competition Commission will seek to ban any mergers which will result in an enterprise having a market share of over 25 per cent?

A23 No. There is no presumption that a merger leading to a market share greater than 25 per cent raises competition concerns. Rather the competition authorities assess a merger to see if it may be expected to result in a substantial lessening of competition. OFT and CC merger guidance describe how we go about this. Each case is considered on its merits. For example, Milk Link's purchase of the UHT milk business of Express Dairies in 2002 resulted in Milk Link gaining a high share of supply in the UK of UHT milk (over 50 per cent) but the merger was cleared because imported UHT milk was thought to provide a competitive constraint on the merged enterprise.

Q24 Is there anything preventing co-operatives, including the main dairy co-operatives, from entering processing?

A24 No. The Department of Trade and Industry said in May 2000 that, on the basis of the successors to Milk Marque continuing to operate independently, it saw no reason why they should not establish or extend their processing activities. In fact, Zenith and Milk Group merged to form Dairy Farmers of Britain and Axis and Scottish Milk merged to form British Milk. In addition, Milk Link bought the UHT milk business of Express Dairies. The OFT did not object to any of these mergers. In February 2004, OFT also cleared the joint purchase by Milk Link, First Milk and Dairy Farmers of Great Britain of United Milk's Westbury milk-processing plant.

OTHER ISSUES

Q25 How does competition legislation impact on farm assurance schemes?

A25 The OFT does not consider that farm assurance schemes restrict competition if they are voluntary and do not involve obliging buyers to buy only from that particular scheme. Schemes must be open to anyone wanting to join (both producers and certifiers) and the membership terms should be transparent (and preferably published), proportionate, non-discriminatory and based on objective standards. Schemes should strive to provide their members with a choice of inspection services.

Q26 Why was Milk Marque broken up?

A26 The Monopolies and Mergers Commission in its report on the supply in Great Britain of raw cows' milk (Cm 4286 published July 1999) found that Milk Marque was exploiting its monopoly in the supply of raw milk.⁴ Milk Marque had used a variety of practices to raise raw milk prices. For example, it made smaller customers pay too much for milk and it restricted the supply of milk to the market to raise prices to artificially high levels. This resulted in consumers paying more for fresh milk than they should and in damage to the competitiveness of the dairy processing sector. Further details are in the Department of Trade and Industry's (DTI) press notice of 6 July 1999 (see [DTI PN P/99/587](#)). As reported in DTI's press notice of 5 November 1999 (see [DTI PN P/99/895](#)), Milk Marque agreed on 4 November 1999 to split into three separate entities: the split took place on 25 January 2000.

Q27 Co-operatives between producers in the food supply chains in some other countries – e.g. Denmark and New Zealand - have been allowed and yet these have created high market shares. Why has the creation of similarly-sized enterprises not been allowed in the UK?

A27 The OFT has nothing against co-operatives just because they have large market shares. Merger law would probably apply if a large co-operative was created. Each case is looked at on its own merits but the OFT would need to assess whether the merger might be expected to result in a substantial lessening of competition.

⁴ Milk Marque was responsible for nearly half of raw milk sales in Great Britain in 1997.

Q28 To what extent do competition authorities take into account the relative strengths of retailers and producers (i.e. farmers and growers) in applying competition law?

A28 Always. Competition authorities take this into account as part of any competition analysis.

Q29 I want to know whether competition law will apply to a particular agreement or conduct. Can the OFT help?

A29 Yes. The OFT is willing to give informal advice on how competition law might view a particular agreement or conduct. The OFT can advise in confidence if that is what is wanted. If in doubt seek OFT's advice.

Q30 I think I am the victim of an anti-competitive practice. Can the OFT help?

A30 Yes. You should contact the OFT for advice on whether competition law applies in your case. Call us, in confidence, on 08457 22 44 99.