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Working Paper

# The interface between EU competition policy and the Common Agriculture Policy (CAP):

# Competition rules applicable to cooperation agreements between farmers in the dairy sector

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## INTRODUCTION - THE CURRENT CHALLENGES FACED BY THE DAIRY SECTOR

Milk is produced in every single EU Member State without exception, and dairying is an economic activity that has an important social and environmental role to play. In fact dairy is the most prominent farming sector in many regions of the EU, which are often regions of particular value for their landscape, environment and cultural heritage. Dairy farming gives many rural areas their distinctive character, and a thriving milk sector is important for the local economy and employment. Locally produced dairy specialities are also an essential part of the European food heritage. In many parts of Europe, such as mountain areas and in northern climates, there is simply no viable production alternative to dairy farming.

The dairy market situation deteriorated dramatically from mid 2008 until summer 2009. After a price spike in 2007 alongside the high food prices in general, prices and international demand dropped substantially affecting milk farmers' income. In many cases producer prices sunk to a level that did not even cover the production costs. To make matters worse, several farmers had invested heavily in the high-price situation of 2007 and faced poor returns on capital or even insolvency, as market conditions deteriorated. While the overall situation of the dairy market has been continuously improving since July 2009 with a gradual increase in farm gate prices for milk, the crisis has highlighted structural problems in dairy production, which affect the competitiveness of the sector on a market where EU milk farmers are confronted with increasing pressure from efficient and highly organised producers outside the Union.

The reform of the Common Agricultural Policy (CAP) has taken a market oriented approach of helping farmers to better respond to market signals. Farm subsidies have been decoupled from production to a large extent and farmers have been given incentives to develop more innovative and business oriented market models. Along with the phasing out of the milk quota system by the end of 2015 this policy development is a major challenge for the dairy sector. Milk farmers are in many cases less flexible than other farmers to adjust their production to changes in the market: the production is constant and cannot be reduced or re-orientated in the short term while high stranded investment costs in installations and production animals make it difficult to change the nature of production. As milk is a highly standardised product, apart from switching to organic production, milk farmers have limited opportunities to improve their competitive position by diversifying their offer.

Structural measures in particular within the EU rural development policy have helped dairy producers to modernise production structures and increase profitability by lowering unit costs. The productivity of dairy farms has increased over the last years, the number of dairy farms has decreased and the production has concentrated in fewer farms with more animals per farm. Despite these developments in many Member States production is atomised and dispersed with a low degree of supply concentration. Those farmers are more exposed to the fluctuations of market conditions than farmers who have achieved higher efficiencies by developing various forms of cooperation. The market pressure on small producers with a low degree of cooperation can be expected to intensify with the abolition of quotas, as the most effective and best organised

producers can place their production on the market without being restricted by maximum quantities.

Therefore structural and other support measures targeting single farms cannot alone equip milk farmers to face the challenges of the increasingly liberalised and competitive market within the EU and on an international scale. Fostering cooperation between milk farmers can help rationalising the supply chain and making it more efficient. By creating better efficiencies, more intensive cooperation will improve the farmers' position in relation to the other market players and, depending on the degree of cooperation achieved, add value to their products.

Competition policy has an important role in promoting cooperation between farmers themselves and farmers and other actors in the milk chain. Competition rules allow intensive cooperation, both at producers' level and between farmers and market players at marketing and processing levels, as long as this cooperation creates efficiencies and does not jeopardise the competitive process in the sector to the detriment of consumers. This means that cartels are not the solution to the problems faced by the milk sector. In fact, agreements restrictive of competition and void of any efficiencies are caught by Article 101 of the TFEU. However, competition policy should not be seen as an obstacle to cooperation between farmers but as a tool that helps them to improve their production and marketing structures and strengthen their position in the supply chain, while ensuring a level-playing field where operators have equal access to the benefits of a liberalised market. This supports the objectives of the CAP and EU rural development policies to encourage structural development in dairy farming and to enable farmers to actively respond to market developments.

The legislation applicable to agricultural products[1] provides for a limited number of derogations form the applicability of competition rules to certain agreements and decisions of farmers and farmers' associations. However, in light of the interpretation that European Courts have given to such derogations, the vast majority of the agreements and decisions of farmers do not fulfil the conditions for such derogations to apply. Therefore, these agreements must be analysed under the regime of the general competition rules applicable to undertakings. For this reason, this Working Paper focuses on the possibilities for cooperation between farmers that are available in the context of the general competition rules (e.g. joint production, joint commercialisation, and cooperation involving both). The Paper also makes reference to cooperation between farmers and other operators in the milk supply chain.

This Working Paper provides further details regarding the interpretation given to the interface between the existing agricultural and competition rules by the European Courts. It also incorporates initial considerations concerning other issues of interest to farmers such as the development of standardised contracts as a tool to strengthen farmers' bargaining power and the impact of greater price transparency on the milk supply chain.

[1] Council Regulation 1234/2007 ("Single CMO Regulation") and Council Regulation 1184/2006 – for further details please refer to Section A.

## A. PRODUCER ORGANISATIONS – SCOPE FOR COOPERATION BETWEEN FARMERS UNDER THE EXISTING RULES

A "producer organisation" ("**PO**") is defined in Article 122 of Council Regulation (EC) No 1234/2007, of 22 October 2007, establishing a common organisation of agricultural sectors and on specific provisions for certain agricultural products (the "**Single CMO Regulation**")[2] as being "constituted by" and "formed on the initiative of" producers. A PO pursues specific aims which may include: ensuring that production is planned and adjusted to demand, particularly in terms of quality and quantity; concentration of supply and the placing on the market of the products produced by its members; and optimising production costs and stabilising producer prices.

The assessment of the compatibility of the creation of POs and other forms of farmers' associations with competition rules firstly requires analysing the legal framework applicable to this type of cooperation agreements in light of the relevant existing case law of the European Courts (i.e. the Court of Justice and the General Court) and of the Commission practice. This legal framework is composed of: (i) particular EU competition rules applicable to the agricultural sector, and (ii) the general EU competition rules implementing Articles 101 and 102 of the TFEU.

### I. Particular EU competition rules applicable to the agricultural sector

### I.1 Introduction

Article 42(1) of the TFEU grants the Council and the European Parliament (the latter after the Treaty of Lisbon) the power to determine the extent to which EU rules on competition apply to the production and trade of agricultural products under the following terms:

> "*The provisions of the Chapter relating to rules on competition shall apply to production of and trade in agricultural products only to the extent determined by the European Parliament and the Council within the framework of Article 43(2) and in accordance with the procedure laid down therein, account being taken of the objectives set out in Article 39.*'

In light of this provision, two Regulations adopted by the Council and governing the application of competition rules to the agriculture sector are currently in force:

(i) The Single CMO Regulation, which establishes a common organisation of the markets for certain sectors included in Annex I to the TFEU (among them, milk and milk products).[3]

[2] OJ L 299, 16.11.2007, p.1.

[3] The sectors concerned are cereals, rice, sugar, dried fodder, seeds, hops, olive oil and table olives, flax and hemp, fruit and vegetables, processed fruit and vegetables, bananas, wine, live plants and products of floriculture, raw tobacco, beef and veal, milk and milk products, pigmeat, sheepmeat and goatmeat, eggs, poultrymeat and other

(ii) Council Regulation (EC) 1184/2006, of 24 July 2006, applying certain rules of competition to the production of, and trade in, agricultural products ("**Regulation 1184/2006**").[4] Regulation 1184/2006 applies to agricultural products listed in Annex I to the TFEU with the exception of the products covered by the Single CMO Regulation. Regulation 1184/2006 repealed the prior Regulation governing the application of competition rules to the agricultural sector: Council Regulation 26/62, of 4 April 1962, applying certain rules of competition to production of and trade in agricultural products ("**Regulation 26/62**").[5] However, the provisions on competition rules contained in Regulation 26/62 remained unchanged in Regulation 1184/2006.

Both the Single CMO Regulation and Regulation 1184/2006 provide for the same substantive competition rules applicable to the agricultural sector, whereby the present note will indistinctively refer to both norms (and also to the repealed Regulation 26/62) when analyzing the relevant case law or prior Commission practice in which the interface between competition and agricultural rules has been addressed.

## I.2 Competition rules laid down by the Single CMO Regulation

Article 175 of the Single CMO Regulation provides for the general application of competition rules to the agricultural sector:

> "*Save as otherwise provided for in this Regulation, Articles 81 to 86 of the Treaty and implementation provisions thereof shall, subject to Articles 176 to 177 of this Regulation, apply to all agreements, decisions and practices referred to in Articles 81(1) and 82 of the Treaty which relate to the production of, or trade in, the products covered by this Regulation.*"

This general application of competition rules to the agricultural sector is subject to three exceptions which are further specified in Article 176(1) of the Single CMO Regulation. These three exceptions only concern Article 101 of the TFEU. Article 102 of the TFEU therefore remains fully applicable to the agricultural sector.

In particular, Article 176(1) of the Single CMO Regulation sets forth that:

> "*Article 81(1) of the Treaty shall not apply to the agreements, decisions and practices referred to in Article 175 of this Regulation which are an integral part of a national market organisation or are necessary for the attainment of the objectives set out in Article 33 of the Treaty.*

products. The Regulation also establishes specific measures for ethyl alcohol of agricultural origin, apiculture products and silkworms.

[4] OJ L 214, 4.08.2006, p.7.

[5] OJ P 30, 20.04.1962, p. 993.

*In particular, Article 81(1) of the Treaty shall not apply to agreements, decisions and practices of farmers, farmers' associations, or associations of such associations belonging to a single Member State which concern the production or sale of agricultural products or the use of joint facilities for the storage, treatment or processing of agricultural products, and under which there is no obligation to charge identical prices, unless the Commission finds that competition is thereby excluded or that the objectives of Article 33 of the Treaty are jeopardised*."

In accordance with Article 176(2) of the Single CMO Regulation the Commission has sole power to determine which agreements, decisions and practices fulfill the conditions required by the above exceptions. The Commission shall undertake such determination either on its own initiative or at the request of a competent authority of a Member State or of an interested undertaking or association of undertakings.

Before entering into the analysis of these three exceptions, it should be noted from the outset that their potential application to a PO or farmers' cooperation agreement only becomes relevant when the agreement at issue may fall under the scope of application of Article 101(1) (that is, when it may actually or potentially affect trade between Member States). If such is not the case (because, for instance, the PO or farmers' association has a limited geographical scope in the territory of a Member State), a derogation from Article 101(1) would not ultimately make sense since the agreement would not be capable in any event of triggering the potential application of this provision.[6]

(i) 1st exception: agreements falling under national market organisations

As regards the first category of agreements contemplated by Article 176(1), that is to say those forming part of national market organizations, it is clearly of very limited importance given that the majority of products (including milk) are now covered by a single CMO, which has superseded market organizations operating at national level.[7]

(ii) 2nd exception: agreements necessary for the attainment of the objectives of Article 39 of the TFEU

The second derogation applies to agreements necessary for the attainment of the objectives of the Common Agricultural Policy ("**CAP**") as set out by Article 39 of the TFEU. These objectives are the following:

"*(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;*

[6] For further explanations concerning the effect on trade concept, please see Section II.1 below.
[7] This exception was applied, for instance, in relation to the French market organization of potatoes by Commission Decision of 18 December 1987, Case IV/31.735, *New potatoes*, OJ L 59, 4.03.1988, p. 25.

*(d) to assure the availability of supplies;*
*(e) to ensure that supplies reach consumers at reasonable prices*."

When analysing the potential application of this 2nd exception, the relevant case law has followed a restrictive interpretation. According to this approach, the objectives of the CAP are already generally ensured by the means provided for by the rules applicable to a common market organization. If a particular private action or agreement is not expressly included among these means, it is generally not deemed to be "*necessary*" for the attainment of the objectives of Article 39. Such was the reasoning followed by the General Court, for instance, in the Joined Cases T-70/92 and T-71/92, *Florimex*, in which it endorsed the prior practice of the Commission in this regard:[8]

"*147. Until now, the Commission has never found that an agreement between the members of a cooperative which affects free access by non-members to agricultural producers' channels of distribution is necessary for attainment of the objectives set out in Article 39 of the Treaty.*

*148. Furthermore, the Commission's practice in earlier decisions has generally been to conclude that agreements not included amongst the means indicated by the regulation providing for a common organization in order to attain the objectives set out in Article 39 are not 'necessary' within the meaning of the first sentence of Article 2(1) of Regulation No 26, as observed by Advocate General Tesauro in his Opinion in Oude Luttikhuis, cited above (at p. I-4480).*"

An additional condition required by the case law to apply this exception is that the agreement or action at issue must be necessary for the attainment of <u>all</u> the objectives of Article 39. If such is not the case, the second exception provided for by Article 176 would not be applicable. Thus, in the Joined Cases T-70/92 and T-71/92, *Florimex*, the General Court established that:

"*153. Finally, as the applicants have submitted, it is settled case-law that the first sentence of Article 2(1) of Regulation No 26 applies only if the agreement in question is conducive to attainment of <u>all</u> the objectives of Article 39 (see Frubo v Commission, cited above, paragraphs 22 to 27, and Oude Luttikhuis, cited above, paragraph 25). It follows that the Commission's statement of reasons must show how the agreement at issue satisfies each of the objectives of Article 39. In the event of a conflict between those sometimes divergent objectives, the Commission's statement of reasons must, at the very least, show how it was able to reconcile them so as to enable the first sentence of Article 2(1) of Regulation No 26 to be applied.*"

[8] Judgment of 14 May 1997, Joined Cases T-70/92 and T-71/92, *Florimex BV and Vereniging van Groothandelaren in Bloemkwekerijprodukten v. Commission*, [1997] ECR II-00693. See also Commission Decision of 14 December 1998, Case IV/35.280, *Sicasov*, OJ L 4, 8.01.1999, p. 27: "*68. Lastly, it must be concluded that agreements which are not included among the means provided by the Regulation on the common organization for the attainment of the objectives set out in Article 39 of the Treaty are not necessary within the meaning of Article 2(1) of Regulation No 26/62. The common organization of markets in seeds does not provide for the conclusion of licensing agreements.*
*69. Accordingly, an exception under Article 2 of Regulation Nº 26 must be ruled out in this case and, by the same token, Article 85(1) of the Treaty is applicable.*"

This attempt to reconcile all the objectives of Article 39 of the TFEU is found for instance in the *French beef* case, where the Commission considered that a price fixing cartel between French farmers and slaughterhouse federations could only fulfil one of these objectives (ensuring a fair standard of living for farmers) but not the rest of the goals set down under the above provision. The reasoning of the Commission was endorsed by the General Court in the Joined Cases T-217/03 and T-245/03, *FNCBV*,[9] in which it stated that:

"*In the light of the foregoing, it must be found that the disputed agreement can be regarded as necessary only in relation to the objective of ensuring a fair standard of living for the agricultural community. On the other hand, the agreement is likely at least to jeopardise the setting of reasonable prices for supplies to consumers. Lastly, the agreement had no connection with, and was therefore all the more unnecessary for, the stabilisation of markets, ensuring the availability of supplies and increasing agricultural productivity. Therefore, in view of the case-law referred to in paragraph 199 above, the Court considers that the Commission did not err in finding that bringing those different objectives into balance did not justify the conclusion that the derogation provided for by the first sentence of Article 2(1) of Regulation No 26 was applicable in the present case.*"

From an economic point of view, in a static sense, it is not possible to achieve the five objectives set out in Article 39 simultaneously, as "*fair standards of living for the agricultural community*" may conflict with "*reasonable prices to consumers*". However, in a dynamic sense, the five objectives can be met if there are sufficient efficiencies or productivity gains that are passed onto consumers in the form of reasonable prices, while entailing higher farming incomes.

In light of the interpretation of this 2nd exception under Article 176(1), it would seem difficult to apply it to arrangements concluded between farmers in the form of POs or other form of associations, in which price mechanisms regarding the purchase or sale of raw milk were to be agreed. Such agreements may indeed respond to the need of ensuring a fair standard of living for farmers, but the rest of the objectives foreseen under Article 39 of the TFEU would also have to be met.

(iii) 3rd exception: agreements between farmers, farmers' associations and associations of farmers' associations belonging to a single Member State

Even though it may be considered that the second sentence of Article 176(1) of the Single CMO Regulation is a particular example of the two prior exceptions contained in the first sentence (by reason of the word "*in particular*"), the Court of Justice has finally considered that it has an independent meaning with respect to the first two prior exceptions and, therefore, amounts to an independent 3rd exception.[10]

[9] Judgment of 13 December 2006, Joined Cases T-217/03 and T-245/03, *FNCBV and others v. Commission*, [2006] ECR II-04987.

[10] Judgment of 12 December 1995, Joined Cases C-319/93, C-40/94 and C-224/94, *Dijkstra*, [1995] ECR I-04471: "*17 It should be noted in that regard that, for the purposes of interpreting the second sentence of Article 2(1), it is necessary to take into account its genesis and the reasons on which Regulation No 26 is based.*

In order to apply this 3rd exception, three cumulative conditions must be met:

(a) The agreements must be concluded between farmers, farmers' associations or associations of farmers' associations belonging to a single Member State.

(b) The agreements must concern the production or sale of agricultural products (the terms used by the Preamble (§ 85) of the Single CMO Regulation in this regard are "joint production or marketing of agricultural products") or the use of joint facilities for the storage, treatment or processing of agricultural products, and under which there is no obligation to charge identical prices.

(c) Thirdly, the agreements may not exclude competition or jeopardize the objectives of the CAP.

This 3rd exception seems to have been so far of very minor relevance in light of the limited case law and Commission practice in which its potential application has been analysed. No particular decision or case has been found in this regard in which it has been fully accepted. Some of the underlying reasons taken into account in this regard have been the following:

- The agreement at issue involves not only farmers, farmers' associations or associations of farmers' associations but also third parties or trade associations. If third operators (other than farmers, farmers' associations or associations of farmers' associations) participate to the agreement at issue, the latter would not qualify for being exempted.

  Such was the approach taken by the Commission in its Decision of 26 November 1986 in the *Meldoc* case[11]: when analysing a horizontal agreement between four dairy cooperatives and one private company introducing a quota system, consultations on prices and mechanisms to restrict imports from other Member States in the Netherlands, the Commission concluded that this 3rd exception was not applicable to the agreement at issue to the extent that a private company (which was not an association of farmers) was also involved: "*(55) (…) Since ML is a private company and not an association of farmers, it cannot be maintained that the Meldoc agreement is covered by the exception provided for in the second sentence of Article 2 (1).*"

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*18 It is apparent, first of all, from the genesis of that regulation that, by adding that second sentence, which did not appear in the Commission' s original proposal for a regulation, at the behest of the European Parliament, the legislature sought to introduce an exception applying in favour of agreements, decisions and practices of farmers where they fulfil the criteria laid down in it, unless the Commission finds that competition is thereby excluded or that the objectives of Article 39 of the Treaty are jeopardized.*

*19 Next, that desire to protect agricultural cooperatives is apparent from the reasons given for the regulation, and in particular from the fourth recital in the preamble to Regulation No 26, which states that special attention is warranted in the case of farmers' organizations.*

*20 To interpret the second sentence as having no independent meaning would run squarely counter to the wishes of the legislature, inasmuch as it would result in more stringent conditions being applied to agreements which are to be made more flexible, since they would have to fulfil the conditions laid down in both the first and second sentences. Moreover, the Commission could scarcely find that an agreement jeopardized the objectives of Article 39 of the Treaty if, by virtue of the derogation set out in the first sentence, it had already been established that that agreement or decision was necessary for the attainment of those objectives.*"

[11] Commission Decision of 26 November 1986, Case IV/31.204, *Meldoc*, OJ L 348, 10.12.1986, p. 50.

Similarly, in its Decision of 7 December 1984 in the *Milchförderungsfonds* case,[12] the Commission refused to recognise the exception to the extent that the arrangements at issue (i.e. management of a private fund aimed at promoting the quality and sales of milk and dairy products) had been implemented by several associations of farmers' trade associations which could not qualify as farmers' associations as such: "*(22) (…) The association formed by the German Farmers' Union and German Raiffeisen Association and their respective Land associations and the Central Association of Private Dairies to administer the MFF is an association of trade associations serving the common economic interests of its members. It is not, however, an association of farmers' associations within the meaning of the second sentence of Article 2 (1) which, like farmers' cooperatives, carry on behalf of their members common commercial activities in the field of the production or sale of agricultural products or the use of joint facilities for the storage, treatment or processing of agricultural products.*"[13]

- The restriction of competition at issue (even though stemming from a decision of a farmers' association) is afterwards included in a contract with a third party which becomes subject to such restriction. Such was the reasoning followed by the Commission to reject the application of this exception in its Decision of 26 July 1988 in the *Bloemenveilingen Aalsmeer* case[14] in which, when analysing the compatibility of certain auction rules and charges adopted by a cooperative society of plant and flower growers, it stated that: "*152. The exception provided for in the second sentence of Article 2(1) applies only to agreements between farmers and/or their associations. Although the Auction Rules and the Scale of Charges are decisions of a farmers' association, the restriction of competition stems from the fact that wholesalers subject themselves to these provisions by contract and thus individual agreements come into being between a farmers' association and wholesalers.*"

- The agreement at issue refers to prices. That was the conclusion of the Court of Justice in the Case C-399/93, *Oude Luttikhuis*,[15] in which it stated that: "*28. The third derogation is subject to three cumulative conditions. For the derogation to be applied, it must be confirmed, firstly, that the agreements in question concern cooperative associations belonging to a single Member State, secondly that they do not cover prices but concern rather the production or sale of agricultural products or the use of joint facilities for the storage, treatment or processing of such products, and thirdly that they do not exclude competition or jeopardize the objectives of the common agricultural policy.*"

  Similarly, in its Decision of 2 April 2003 in the *French beef* case the Commission refused the application of the exception to an agreement between several federations

[12] Commission Decision of 7 December 1984, Case IV/28.930, *Milchförderungsfonds*, OJ. L 35, 7.2.1985, p. 35.
[13] See also in this same regard Commission Decision of 2.12.1977, Case IV/28.948, *Cauliflowers*, OJ L 21, 26.01.1978, p. 23.
[14] Commission Decision of 26 July 1988, Case IV/31.379, *Bloemenveilingen Aalsmeer*, OJ. L 262, 22.9.1988, p. 27.
[15] Judgment of 12 December 1996, Case C-399/93, *H.G. Oude Luttikhuis*, [1995] ECR I-04515.

of farmers and slaughterers including a minimum purchase price for identical reasons: "*137. (…) The exception at (c) is excluded twice over: the agreement involves parties other than farmers, namely the slaughterers' federations; and it does indeed impose an obligation to charge identical prices*."[16]

In light of the above precedents, the relevance of the second sentence of Article 176(1) of the Single CMO Regulation to assess POs or other forms of associations between farmers would seem to be quite limited. Indeed, in many cases the agreements may involve in practice farmers' trade associations (e.g. *Milchförderungsfonds*) or third parties other than farmers (i.e. collectors, processors, etc.), which would automatically exclude the application of the second sentence of Article 176(1) (e.g. Cases *Meldoc* and also *French beef*). In addition, if the agreement involves price arrangements (which would be the case, for instance, when the PO or association buys the raw milk from its members to sell it to processors at an identical price), the application of this derogation is excluded (e.g. Cases *Oude Luttikhuis* and *French beef*). The fact that the potential restriction of competition between farmers (in the form of an identical sale price agreed in the framework of a PO) be included in subsequent individual contracts concluded with 3rd parties (i.e. collectors, processors, etc.) would also seem to be an additional reason to justify the non-application of this exception (e.g. *Bloemenveilingen Aalsmeer*).

Cooperation agreements between farmers not meeting the requirements laid down by Article 176(1) of the Single CMO Regulation would still be required to be analysed under Article 101(1) of the TFEU in order to determine whether they are deemed to be restrictive of competition and capable of affecting trade between Member States. If such is the case, it would thus be necessary to analyse whether these agreements could still benefit from a block or individual exemption under Article 101(3) of the TFEU.

Such has been the approach taken by the Commission practice which, when it has come to the conclusion that Article 176(1) of the Single CMO Regulation was not applicable, has also analyzed whether the agreement at issue may fall under the scope of application of Article 101(1) of the TFEU and, if so, whether it could benefit from the exception provided for by Article 101(3) (for instance, in Cases *Milchförderungsfonds* and *Meldoc*). Similarly, when the Court of Justice has concluded that Regulation 26/62 did not apply in a particular case, it has ruled that Article 101 remained fully applicable (Case C-250/92, *DLG*).[17]

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[16] Commission Decision of 2 April 2003, Case COMP/C.38.279/F3, *French beef*, OJ L 209, 19.08.2003, p. 0012. This Decision was confirmed in essence by the General Court judgment of 13 December 2006, Joined Cases T-217/03 and T-245/03, *FNCBV and others / Commission*, already cited. The General Court judgment was also upheld by the Court of Justice judgment of 18 December 2008, Joined Cases C-101/07 P and C-110/07 P, *FNCBV and others / Commission*.

[17] Judgment of 15 December 1994, Case C-250/92, *Dansk Landbrugs Grovvareselskab AmbA*, [1994] ECR I-05641. However, it should also be noted that in other cases the Court of Justice has firstly considered whether an agreement may fall under Article 101(1) and benefit secondly from the "exemptions" of Articles 176/1) of the Single CMO Regulation or 101(3) of the TFEU. See, for instance, Court of Justice Joined Cases C-319/93, C-40/94 and C-224/94, *Dijkstra*: "*(22) (…) where it is found that an agreement or a decision falls within the scope of Article 85(1), that the criteria for exemption referred to in the second sentence of Article 2(1) of Regulation No 26 are not fulfilled and that it does not qualify for exemption under Article 85(3) of the Treaty, it is void in accordance with Article 85(2). Such*

## II. General EU competition rules applicable in the agricultural sector

### II.1 Legal framework applicable – Effect on inter-State trade

As above indicated, the prohibition rule of Article 101(1) applies to restrictive agreements and concerted practices between undertakings and decisions by associations of undertakings in so far as they are capable of affecting trade between Member States. As an exception to this rule Article 101(3) provides that the prohibition contained in Article 101(1) may be declared inapplicable in case of agreements which contribute to improving the production or distribution of goods or to promoting technical or economic progress. At the same time, such agreements must allow consumers a fair share of the resulting benefits, and must not impose restrictions which are not indispensable to the attainment of these objectives. Furthermore, such agreements must not enable the undertakings involved to eliminate competition in respect of a substantial part of the products concerned.

The application of Article 101(1) of the TFEU to any cooperation agreements between farmers requires therefore as a pre-condition that such agreements are capable of appreciably affecting trade between Member States.

A case-by-case analysis is necessary in order to determine if this condition is fulfilled, taking account of the particular characteristics of the agreements and markets at issue. In this regard, as laid down in the Guidelines on the effect of trade concept contained in Articles 81 and 82 of the TFEU,[18] trade between Member States is not deemed to be appreciably affected if the parties to the agreement have a combined market share of less than 5% on any relevant market affected by such agreement, as well as an EU aggregate turnover in these markets of less than 40 million euro. If these conditions are cumulatively met, cooperation agreements between farmers, even in the form of collective bargaining groups deciding on common prices and/or volumes, will not fall under the scope of EU competition rules which will consequently not be infringed. Such will normally be the case of agreements involving small farmers who act in markets of regional or local scope, with respect to which it can be assumed that they will not be capable of affecting trade between Member States to any significant extent. However these agreements will be subject to the national competition rules of the Member States. National Competition Authorities ("**NCAs**") can thus assess these cooperation agreements under their own legal competition systems which may include legal provisions or exceptions differing from EU competition rules in certain cases. In their analysis, NCAs will also take into account the specificities and structural conditions which characterise milk markets at national level.

Above the aforementioned thresholds, a more careful, case by case examination is required to determine to what extent an agreement is capable of having a minimum level of cross-border effects within the Union.

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*nullity has retroactive effects (…)*". See also, for instance, Commission Decisions of 26 July 1988, Case IV/31.379, *Bloemenveilingen Aalsmeer*, or of 14 December 1998, Case IV/35.280, *Sicasov*.

[18] OJ C 101, 27.04.2004, p. 81.

With respect to those agreements between farmers capable of appreciably affecting trade between Member States and therefore subject to EU competition law, the analysis under Article 101(1) and (3) should be made under the general competition rules applicable to horizontal agreements between competitors. These rules are contained in the Guidelines on the applicability of Article 81 of the TFEU to horizontal cooperation agreements ("**Horizontal Guidelines**").[19]

As indicated in the Horizontal Guidelines (paragraph 20), whether the agreement is able to cause negative market effects depends on the economic context taking into account both the nature of the agreement and the parties' combined market power which determines – together with other structural factors – the capacity of the cooperation to affect competition to a significant extent. The nature of the agreement relates to factors such as the area and objective of the cooperation, the competitive relationship between the parties and the extent to which they combine their activities. These factors indicate the likelihood of the parties coordinating their behaviour in the market.

As far as the assessment of cooperation agreements between farmers in the framework of POs or other forms of associations is concerned, two main categories of agreements could be distinguished depending on the aims pursued and the level of integration of activities: joint production agreements and commercialisation agreements.

## II.2 Joint production agreements

By means of a joint production agreement, two or more parties agree to produce certain products jointly or to carry out certain processing activities jointly.

Joint production always entails an integration of economic activities, capacities or assets between the parties to the agreement, albeit its nature, scope and form can vary in practice. In the milk sector joint production agreements can be differentiated on the basis of the degree of integration of farmers' activities and be structured in different forms and levels. For instance, cooperation between farmers can be limited to joint collection at the upstream phase of the milk supply chain. In these cases, farmers agree on jointly collecting their respective raw milk production outputs by exploiting together some collection equipment (e.g. trucks, tanks, storage facilities, etc.) either directly or through an intermediate vehicle association or a collection cooperative organisation. Cooperation between farmers can go beyond milk collection and involve a downstream integration of production activities, including for instance the creation of a production joint venture. Such is typically the case of production cooperatives whereby farmers group together their complementary milk outputs at upstream level with the aim of producing processed dairy products (e.g. cheese, butter, fresh and long-life milk, etc.). Cooperation can also extend beyond production to include the distribution of the relevant products. Moreover, cooperation may also take the form of a full-function joint venture in the form of a jointly controlled company that runs one or several production facilities and also carries out a joint distribution of the product. In these last cases, it is likely that the structural cooperation between the parties would fall under the relevant merger control rules (either at EU or national level).

[19] OJ C 3, 06.01.2001, p. 2.

(i) Favourable treatment of certain types of farmers' organisations involving a joint production arrangement, such as cooperatives

A typical joint production agreement in the agricultural sector would be a cooperative whereby farmers group together their complementary milk productions at an upstream level with the aim of producing dairy products (butter, cheese, long-life milk, etc.) at a subsequent processing stage. A cooperative is *de facto* a PO.

When assessing the application of Article 101(1) of the TFEU to this type of farmers' organisations, the Court of Justice has clearly recognised in several occasions the pro-competitive effects stemming from cooperatives and established that the prohibition principle of Article 101(1) does not apply to agreements that contribute to the improvement of the competitive conditions of the markets, insofar as these agreements are indispensable for the achievement of such results.

For instance, in Case C-399/93, *Oude Luttikhuis*, it was mentioned that:

> "*12. ( ) organizing an undertaking in the specific legal form of a cooperative association does not in itself constitute anti-competitive conduct. As the Advocate General noted in point 30 of his Opinion, that legal form is favoured both by national legislators and by the Community authorities because it encourages modernization and rationalization in the agricultural sector and improves efficiency*."[20]

The Court of Justice has also highlighted the economic benefits of cooperatives in the Joined Cases T-70/92 and T-71/92, *Florimex:*

> "*161 (…) it is true that the concentration of supply achieved by the VBA helps in particular to improve the organization of marketing by enabling a large number of small producers to participate in the economic process on a wider-than-regional scale, thus fulfilling certain objectives of Article 39 (…)*".

A similar approach was also taken in the Case C-250/92, *DLG* (related to a cooperative purchasing association through which farm supplies were provided to its members). The Court of Justice established that:

> "*30 A cooperative purchasing association is a voluntary association of persons established in order to pursue common commercial objectives.*

[20] The Opinion of Advocate General Tesauro to which the judgement refers stated that: "*It should also be borne in mind that, in general, the establishment of a cooperative for the processing of or trade in agricultural products brings into being a type of cooperation between undertakings viewed favourably both by national legislature and by the Community authorities, in that it helps to modernize and rationalize the agricultural sector and, ultimately, contributes to the efficiency of undertakings and effective and efficient competition between them.*"

*31 The compatibility of the statutes of such an association with the Community rules on competition cannot be assessed in the abstract. It will depend on the particular clauses in the statutes and the economic conditions prevailing on the markets concerned.*

*32 In a market where product prices vary according to the volume of orders, the activities of cooperative purchasing associations may, depending on the size of their membership, constitute a significant counterweight to the contractual power of large producers and make way for more effective competition.*"

Although strengthening bargaining power of one of the two sides of the vertical chain will determine the distribution of rents, this is not a competition concern as such. Nevertheless, the above case law emphasises the benefits in terms of efficiency gains that may stem from the establishment of cooperatives.

Moreover, the same type of favourable treatment that the Court of Justice has granted to cooperatives may be extended to other types of POs or farmers' associations. Such entities may also entail a certain level of integration of activities and contribute to the modernization and rationalization of the milk supply chain. This would be the case for instance for joint milk collection, which may involve efficiency enhancing effects to the extent that it allows small farmers to group together their individual milk outputs in larger quantities, thereby meeting the needs of large buyers who may not want to deal with a wide number of suppliers.

(ii) Market power and market structure

The above observations highlight the favourable approach which is generally taken under competition rules in respect of cooperation agreements. However, a full-fledged assessment of such agreements requires in any event to determine whether the creation of this type of farmers' organisations may entail any actual or potential restriction of competition within the meaning of Article 101(1). Two steps are necessary:

- First, to verify that there are no restrictions of competition by object. In general, agreements which involve price-fixing, limiting output or sharing markets or customers have the object of restricting competition within the meaning of Article 101(1).

- The second step is to determine whether there are any restrictions of competition by effect. The starting point for this analysis would be the position of the parties in the markets affected by the cooperation. This would allow to determine whether or not they are likely to maintain, gain or increase market power through the cooperation. The individual market position of the entity resulting from the cooperation between farmers, the level of market concentration (i.e. position and number of competitors) and barriers to entry should be taken into account in this exercise.

It is interesting to note in this regard that issues concerning market power exercised by large cooperatives have been addressed by the Court of Justice in the Case C-137/00, *Milk Marque*,[21]

[21] Judgment of 9 September 2003, Case C-137/00, *Milk Marque*, [2003] ECR I-07975.

in which it recognised that NCAs can also apply national competition law in situations in which a dairy cooperative has a powerful position in the market:

> "*61. As the common organisations of the markets in agricultural products are therefore not a competition-free zone, it must be pointed out that, in accordance with settled case-law, Community competition law and national competition law apply in parallel, since they consider restrictive practices from different points of view. Whereas Articles 81 and 82 EC regard them in the light of the obstacles which may result from trade between Member States, national law proceeds on the basis of the considerations peculiar to it and considers restrictive practices only in that context (see, inter alia, Wilhelm and Others, paragraph 3, and Joined Cases 253/78 and 1/79 to 3/79 Giry and Guerlain and Others [1980] ECR 2327, paragraph 15). (…)*
>
> *63. Admittedly, in a sector covered by a common organisation of the market, a fortiori where that organisation is based on a common price system, the Member States are under an obligation to refrain from taking any measures which might undermine or create exceptions to it (see, inter alia, Case 111/76 Van den Hazel [1977] ECR 901, paragraph 13, Pigs Marketing Board, cited above, paragraph 56, and Case C-462/01 Hammarsten [2003] ECR I-781, paragraph 28). In particular, Member States can no longer take action, through national provisions taken unilaterally, affecting the machinery of price formation at the production and marketing stages established under the common organisation (see, inter alia, Toffoli and Others, cited above, paragraph 12).*
>
> *64. However, having regard to the fact that, as is clear from paragraphs 57 to 60 of this judgment, the maintenance of effective competition is one of the objectives of the common organisation of the market in milk and milk products, it must be observed that any measure adopted by the authorities of a Member State in application of national competition law cannot be regarded, by its very nature, as undermining or creating exceptions to the functioning of the common organisation of the market. Moreover, national measures which seek to eliminate a distortion of competition which is the result of abuse of the powerful position enjoyed by an agricultural cooperative on the national market cannot a priori be regarded as measures affecting the machinery of price formation established under the common organisation at Community level, within the meaning of the case-law cited at paragraph 63 of this judgment.*"

A production agreement is unlikely to lead to restrictive effects on competition if the parties to the agreement do not have market power in the market on which a restriction of competition is assessed. The starting point for the analysis of market power is the market share of the parties. Companies are unlikely to have market power below a certain level of market share. Therefore, joint production agreements including certain integrated commercialisation functions such as joint distribution are block exempted by the Commission Regulation (EC) No 2658/2000, of 29 November 2000, on the application of Article 81(3) of the Treaty to categories of specialisation agreements[22] ("**Specialisation block exemption regulation**"), if they are concluded between parties with a combined market share not exceeding 20% in the relevant market(s), and provided that the other conditions for the application of this Regulation are fulfilled. It is only where the

[22] OJ C 3, 6.1.2001, p. 2–30.

parties' combined market share exceeds 20% that the restrictive effects have to be analysed on a case-by-case basis as the agreement does not fall within the scope of the Specialisation block exemption regulation.

(iii) Contractual ties between the cooperative and its members

When assessing the market power of a cooperative, it should also be necessary to determine whether such market power could be strengthened by individual contractual ties imposed upon its members. In particular, it is required to analyse the members' possibilities to exit or withdraw from the cooperative (so that they can operate autonomously or potentially join another competing cooperative) and their freedom to supply third parties other than the cooperative itself. These were the conclusions of the Court of Justice in Case C-399/93, *Oude Luttikhuis*, in which it stated that:

> "*13 However, it does not follow that the provisions in the statutes governing relations between the association and its members, in particular those relating to the termination of the contractual link and those requiring the members to reserve their milk production for the association, automatically fall outside the prohibition in Article 85(1) of the Treaty.*
>
> *14 In order to escape that prohibition, the restrictions imposed on members by the statutes of cooperative associations intended to secure their loyalty must be limited to what is necessary to ensure that the cooperative functions properly and in particular to ensure that it has a sufficiently wide commercial base and a certain stability in its membership (see Case C-250/92 Gottrup-Klim v Dansk Landbrugs Grovvareselskab [1994] ECR I-5641, paragraph 35).*
>
> *15 With regard, next, to the effects of the agreements or the clauses in the statutes, a combination of clauses such as those requiring exclusive supply and payment of excessive fees on withdrawal, tying the members to the association for long periods and thereby depriving them of the possibility of approaching competitors, could have the effect of restricting competition.*
>
> *16 Such clauses are liable to render excessively rigid a market in which a limited number of traders operate who enjoy a strong competitive position and impose similar clauses, and of consolidating or perpetuating that position of strength, thereby hindering access to that market by other competing traders*."

(iv) Price fixing and output limitation necessary for the integration of different activities in a joint production agreement

As previously stated, agreements which involve price-fixing, limiting output or sharing markets or customers have, in general, the object of restricting competition within the meaning of Article 101(1). However, in the context of production agreements, this does not apply where:[23]

[23] See, for instance, Article 5(2) of the Regulation 2658/2000.

– the parties agree on the output directly concerned by the production agreement (e.g., the capacity and production volume of a joint venture or the agreed amount of outsourced products); or

– a production agreement that also covers the joint distribution of the contract products foresees the joint setting of the sales prices for these products, provided that this is necessary for integrating the production and distribution functions of the agreement.

Exceptionally, in these two cases the agreement on output or prices will not be assessed separately as restrictions by object but in the light of the overall effects of the joint production agreement on the market in order to determine the applicability of Article 101(1).

Subject to certain conditions, such provisions are specifically exempted by the Specialisation block exemption regulation if the combined market share of the participating undertakings to the agreement does not exceed 20 % of the relevant market.[24] Above such market share threshold there is no automatic presumption of illegality but such joint production agreements will have to be assessed on a case-by-case basis.

Last, such cooperation agreements have also the potential to contribute to the achievement of all the objectives of Article 39, including securing supplies, stabilising markets and enhancing productivity growth (e.g. by solving commitments problems associated with efficiency enhancing investments that may be jeopardised by opportunistic behaviour in the absence of such agreements).

## II.3 Commercialisation agreements

Commercialisation agreements cover cooperation agreements between competitors in the selling, distribution or promotion of their products. These agreements can have a widely varying scope, depending on the marketing functions which are being covered by the cooperation. As far as the milk and dairy sectors are concerned, one of the most relevant type of commercialisation agreements between farmers not integrated in cooperatives refers to the joint selling of raw milk. On the basis of information provided by NCAs in the framework of the analysis of the milk supply chain, this joint selling is normally made through collective bargaining groups or an intermediary PO or farmers' association which buys-in the raw milk from its members to sell it afterwards to third parties (i.e. collectors, processors, etc.).

A distinction should be made in this regard depending on whether a joint commercialisation agreement between farmers involves price fixing or not.

(i) Commercialisation agreements not involving price fixing

Commercialisation agreements between competitors which do not involve horizontal price fixing are only subject to Article 101(1) if the parties to the agreement have some degree of market power. In most cases, it is unlikely that market power exists if the parties to the agreement have a

[24] See Article 4 of the Specialisation block exemption regulation.

combined market share below 15%. At that level of market share it is also likely that the conditions of Article 101(3) are fulfilled by the agreement in question.[25] Above such market share threshold there is no automatic presumption of illegality but such commercialisation agreements shall be assessed on a case-by-case basis.

An example of a commercialization agreement not involving price fixing between competing farmers could be the appointment by farmers of a joint structure or a broker acting as commercial agent on their behalf. In this scenario, producers would retain the ownership of their milk until it is sold to the buyers, and each one of them individually would inform the agent of the reserve price which he wants to obtain. The agent, who would not bear any significant financial or commercial risk in relation to the contracts concluded and/or negotiated on behalf of the participating farmers, would pool together the volumes of all the producers and negotiate the best possible price with each interested buyer. The milk would be then sold at the best price negotiated with each buyer. If the selling price is below the reserve price of one or more individual producers (which can however change over time according to the conditions agreed in the contract with each producer concerned), the corresponding volumes would remain unsold.

Having said that, it shall also be recalled that commercialisation agreements involving a common agent may fall under Article 101(1) if they facilitate collusion between farmers. In accordance with the Guidelines on Vertical Restraints ("**Vertical Guidelines**"),[26] this could for instance be the case when a number of farmers use the same agents while collectively excluding others from using these agents. Similarly, such would also be the case when farmers use the agents to collude on marketing strategy or to exchange sensitive price information with each other. In general, a case-by-case assessment may be necessary, taking into account the market power of the agent, entry/exit barriers, the position of other competitors on the same market, the countervailing power of customers, etc. The objective of this analysis would be to ensure that competition between milk suppliers is preserved and that farmers have alternative supply channels to turn to if they so wish.

(ii) Commercialisation agreements involving price fixing

Commercialisation agreements that involve price fixing will always fall under Article 101(1) irrespective of the market power of the parties. Indeed, the principal competition concern about a joint selling agreement is price fixing to the extent that it entails a coordination of the pricing policy of competing manufacturers.[27] In these cases the conclusion of commercialisation agreements entailing in practice a mere cartel between competitors can never be exempted under Article 101(3) since they entail a prohibited hardcore restriction.

This notwithstanding, in certain specific circumstances commercialisation agreements between competing undertakings involving a certain level of integration of activities for which price fixing is indispensable may be exempted under Article 101(3) provided that certain conditions are met. Such would be the case if:

[25] Paragraph 149 of the Horizontal Guidelines.
[26] OJ C 291, 13.10.2000, p. 1. See in particular paragraph 20.
[27] Paragraph 144 of the Horizontal Guidelines.

(a) price fixing is indispensable for the integration of other marketing functions,

(b) this integration generates substantial efficiencies,

(c) these efficiencies are not savings which result only from the elimination of costs that are inherently part of competition, but result from the integration of economic activities,

(d) the agreement does not impose restrictions that are not indispensable to the attainment of the abovementioned benefits, and

(e) the parties do not have market power which allows them to eliminate competition (see paragraphs 151 and following of the Horizontal Guidelines).

EU competition rules acknowledge that a number of efficiencies may result from such commercialisation agreements and may offset potential anticompetitive effects in a limited number of cases. As illustrated by the Horizontal Guidelines, price fixing in such cases can be regarded as indispensable and, therefore, excepted under Article 101(3). Such limited exceptions arise in two cases:

(i) if a large buyer does not want to deal with a multitude of prices and requests a single supply price, the common setting of a sale price is allowed since it is considered indispensable;

(ii) similarly, price fixing is also permitted if farmers agree on jointly launching new products, such as a common brand of milk, which can only be credibly achieved if all aspects of marketing, including price, are standardised.

This favourable assessment depends however on the collective bargaining group not holding significant market power (aggregated market shares of the group being below 15%).

## B. ASSESSING THE MARKET POWER OF LARGE COOPERATIVES

As indicated in Section A above, the formation or operation of a very large dairy cooperative could raise competition concerns if it has a significant level of market power which allows it to restrict competition in the relevant market. The starting point to assess such market power in this context should be the position of the cooperative in the market and the concentration ratios of that market.

The definition of relevant product and geographic market for performing this exercise should be guided by the general principles contained in the Commission Notice on the definition of relevant market for the purposes of Community competition law (97/C 372/03).

An illustrative example of the application of the definition of the relevant market in the milk production sector is found in a recent merger case (COMP/M.5046 *Friesland Foods/Campina*), in which the Commission had the opportunity to look at the market for raw milk in detail. Since the notifying parties were co-operatives, the relevant product market was defined as the "procurement of raw milk" to be further distinguished into "procurement of conventional raw milk" and "procurement of organic raw milk" because of a lack of supply and demand-side substitutability. Concerning the relevant geographic market, the Commission took into account several factors in its analysis like perishability of raw milk, the conditions of competition across different geographic areas and the costs of collecting raw milk, which are affected by several factors like transport distances, the density of farms in a given area, size of the processing plant as well as the farms in a given area. For the purpose of the case at hand, it was concluded that the relevant geographic product market was national in scope (i.e. The Netherlands).

However, this does not exclude that in other cases the geographic scope could be wider or narrower. For example, as indicated by some NCAs (i.e. German NCA) in the recent meeting of the ECN Joint Working Team on Milk of 26 November 2009, the geographic scope of the market would be regional in Germany (~ 150 km around a dairy).

The above indicates that a case-by-case analysis is necessary in order to determine the market power of dairy cooperatives as well as the potential competition constraints that they may face in a particular relevant market.[28]

[28] An illustrative example of this analysis is found in the above mentioned case COMP/M.5046 *Friesland Foods/Campina*, which concerned a merger between two cooperatives with a combined market share of [70-80%] on the market for the procurement of raw milk in the Netherlands and similar shares on several downstream markets for dairy products. Despite this strong position, the Commission found that, because of the cooperative structure (which obliged the parties to purchase the entirety of their milk requirements from their members), it was unlikely that the new merged cooperative (which would retain such purchasing commitment) would have the ability or the incentive to reduce the price paid for raw milk purchased from its members. Consequently, it was also unlikely that the merger would lead to a reduction of input purchases and a subsequent reduction of output and increased prices further downstream. However, the Commission considered that the entity resulting from the merger would have the ability and the incentive to leverage its strong position in the procurement market for raw milk to foreclose existing or potential downstream rivals, by limiting or raising the costs of their access to raw milk. In order to remove such concerns, the parties offered certain commitments ensuring such access which were taken into account to clear the transaction.

If such a market power exists and is deemed to be exploited in an anticompetitive manner, Competition Authorities are empowered to adopt the necessary measures to restore effective competition on the markets affected. This was confirmed in the aforementioned *Milk Marque* case, in which the Court of Justice stated that, in a sector governed by a common market organisation as it is the case of milk, NCAs retain jurisdiction to apply competition law to a milk producers' cooperative in a powerful position at national level.[29] The Court of Justice also established that, when applying competition rules in this sector, NCAs are under an obligation to refrain from adopting any measure which might undermine or create exceptions to that common market organisation or impede the working of its machinery (See Section II.2(ii)).

[29] In the *Milk Marque* case a milk cooperative with significant market power (between 40%-60%) was divided into three separate and independent cooperatives. The objective of this action was to eliminate such market power in order to create a more competitive market for the supply of milk and provide fresh opportunities for producers and processors to develop commercial relationships that served their interests as well as the interests of consumers.

## C. THE ROLE OF INTERBRANCH ORGANISATIONS

### I. Definitions

An "**interbranch organisation**" ("**IPO**") is defined in Article 123 of the Single CMO Regulation as an organization made up of representatives of economic activities linked to the production of, trade in, and/or processing of products in a number of sectors. Currently for IPOs there is a Community framework for 5 sectors: fruit and vegetables, tobacco, wine, olives/ olive oil and cotton.

As stipulated in Article 123, such organizations must:

> *(b)* [be] *formed on the initiative of all or some of the organisations or associations which constitute them;* and
> *(c) pursue a specific aim, which may, in particular relate to:*
> > *(i) concentrating and coordinating supply and marketing of the produce of the members;*
> > *(ii) adapting production and processing jointly to the requirements of the market and improving the product;*
> > *(iii) promoting the rationalisation and improvement of production and processing;*
> > *(iv) carrying out research into sustainable production methods and market developments."*

### II. Recognition and mode of operation

Unless IPOs are to be given a specific role or powers under EU legislation, there is no legal obligation to create an IPO under EU law. Member States may recognise IPOs in other sectors, on the basis of national law, provided such IPOs respect EU law (Article 124(1) of the Single CMO Regulation) - such is for example the case for milk where IPOs exist in a number of Member States (e.g. France, Hungary, Spain, etc.).

### III. General competition rules applicable to IPOs

As indicated in previous Sections, Article 175 of the Single CMO Regulation stipulates that, save otherwise provided in this Regulation, Articles 101 – 106 of the TFEU apply to all agreements, decisions and practices referred to in Articles 101(1) and 102 of the TFEU, which regulate the production of and trade in agricultural products.

Given that IPOs go beyond a "*farmers' association or an association of such associations*" within the meaning of Article 176 (1), second paragraph, this means that, in the absence of any specific derogation contained in other provisions of the Single CMO Regulation, Article 101 of the TFEU applies to IPOs. Consequently, absent a specific derogation, the agreements/ concerted practices

taken by an IPO would have to be analysed under Article 101(1) and any possible efficiency enhancing effects under 101(3).

There are currently a number of public calls for IPOs to be able to issue price recommendations or to agree on the minimum prices to be paid to producers. It is crucial to recall that, following the case law of the European Courts and the Commission Guidelines on the application of Article 81(3), an agreement that would have a horizontal and vertical dimension bringing together operators at various steps of the supply chain, having an effect on inter-State trade, and leading to a price fixing agreement deprived of any efficiencies would be prohibited. Such an agreement would be regarded as a hardcore restriction of competition and would not likely benefit from an exception under Article 101(3). As seen above, the Courts have upon several instances insisted that price fixing agreements would run against the very objectives of Article 39 of the TFEU. For example, as seen above when details of the *French beef case* were provided, the Court ruled that such agreements would under no circumstance be necessary for stabilising markets. Moreover, the Court ruled that ensuring a fair standard of living for the agricultural community is not sufficient to justify a price fixing agreement and that fixing minimum prices cannot be regarded as neutral in relation to the objective of Article 39 that supplies reach consumers at reasonable prices.

## IV. Derogations in specific circumstances as provided by the Single CMO Regulation

The Single CMO Regulation provides for a limited number of exceptions concerning the application of EU competition rules to certain agreements and/or decisions taken by IPOs in a number of product sectors. These exceptions are construed narrowly, on the basis of the specificities of the production of and trade in these particular products. In all these exceptions, it must be recalled that price fixing, output restrictions and market partitioning are prohibited.

Since there are currently a number of calls to extend to the milk sector certain exceptions that are available for other product sectors, it may be useful to recall the most relevant sectors which benefit from these specific exceptions:

- For **fruit and vegetables (Article 176a)**, Article 101(1) shall not apply to agreements, decisions and concerted practices of recognised IPOs, provided that such agreements have been notified to the Commission and that within 2 months, the Commission has not found them incompatible with Community rules.

  Agreements and practices leading to market partitioning; affecting the sound operation of the market organisation; which may create distortions of competition and which are not essential to achieving the objectives of the common agricultural policy; which entail fixing of prices (*without prejudice to activities applying specific Community rules*); which may create discrimination or eliminate competition in respect of a substantial proportion of the products in question, are in any case to be declared incompatible with Community rules.

If following the expiry of the 2 months period, the Commission finds that the derogation conditions have not been met, it shall take a Decision declaring that Article 101(1) is applicable to the agreement/ practice in question.

Furthermore, according to Article 125l–m, in cases where an IPO operating in a specific region or regions of a Member State is considered to be representative of the production, trade or processing of a given product, the Member State concerned may, at the request of that IPO, make binding some of the agreements/ decisions/concerted practices agreed upon within that IPO, for a limited period, on other operators operating in the regions in question, whether individuals or groups, who do not belong to the IPO.

The rules for which extension to other operators (*the so-called "extension of rules" principle*) may be requested shall have one of the following aims:

*(i) production and market reporting;*
*(ii) stricter production rules than those laid down in Community or national rules;*
*(iii) drawing up of standard contracts which are compatible with Community rules;*
*(iv) rules on marketing;*
*(v) rules on protecting the environment;*
*(vi) measures to promote and exploit the potential of products;*
*(vii) measures to protect organic farming as well as designations of origin, quality labels and geographical indications;*

Such rules shall have been in force for at least one marketing year, may be made binding for no more than three marketing years, and shall not cause any damage to other operators in the Member State concerned or the Community. Member States shall notify the Commission of the rules which they have made binding on all operators. The Commission shall decide that a Member State shall repeal an extension of the rules where it finds that the extension in question excludes competition in a substantial part of the internal market or jeopardises free trade or that the objectives of the CAP are endangered; where it finds that Article 101(1) applies to the rules extended to other producers (Article 125h).

Furthermore, as provided for by Article 125n, the Member State which has granted recognition to the IPO may decide that individuals or groups which are not members of the IPO but which benefit from those activities shall pay the organisation all or part of the financial contributions paid by its members to the extent that such contributions are intended to cover costs directly incurred as a result of pursuing the activities in question (*the so-called "financial contribution of non-members principle"*).

- For **tobacco,** according to Article 177, there is the same type of derogation available from the application of Article 101(1) as there is for fruit and vegetables, and a 3 months period available for notification to the Commission. The same procedure for a Commission Decision is provided for.

There is also an extension of rules possibility provided for in Article 178, according to which IPOs in the tobacco sector may request that certain of their agreements or

concerted practices be made binding for a limited period on individuals and groups in the economic sector concerned which are not members of the trade branches which they represent, in the areas in which the branches operate.

Extension of rules shall be subject to approval by the Commission. The rules for which an extension of scope is requested shall have been in force for at least one year and shall relate to one of the following objectives:

*(a) knowledge of production and the market;*
*(b) definition of minimum qualities;*
*(c) use of cultivation methods compatible with the protection of the environment;*
*(d) definition of minimum standards of packing and presentation;*
*(e) use of certified seed and monitoring of product quality*.

As in the case of fruit and vegetables, in the tobacco sector, a Member State may decide that individuals or groups which are not members of the IPO but which benefit from those activities shall pay the IPO all or part of the subscriptions paid by its members to the extent that such subscriptions are intended to cover costs directly incurred as a result of pursuing the activities in question.

- For **wine**, Article 113c provides a particular exception regarding marketing rules to improve and stabilise the operation of the common market in wines. According to this Article, producer Member States may lay down marketing rules to regulate supply, particularly by way of implementing decisions taken by the IPOs referred to in Articles 123(3) and 125o. Such rules shall be proportionate to the objective pursued and shall not relate to any transaction after the first marketing of the produce concerned; allow for price fixing, including where prices are set for guidance or recommendation; render unavailable an excessive proportion of the vintage that would otherwise be available; provide scope for refusing to issue the national and Community certificates required for the circulation and marketing of wines where such marketing is in accordance with those rules.

## D. ARE STANDARDISED CONTRACTS THE ADEQUATE TOOL TO STRENGTHEN THE POWER OF PRODUCERS?

The views of NCAs as expressed at the first meetings of the Joint Working Team on Milk (November 2009 and January 2010) converge on the following points:

- The primary objective of EU competition policy is to contribute to the functioning of the internal market and to the benefit of citizens and businesses in the EU. EU antitrust law is not concerned with particular outcomes of contractual negotiations between parties unless such terms would have negative effects on the competitive process and ultimately reduce consumer welfare. It is not the aim of EU competition rules, as currently devised, to interfere in the bargain struck between contractual parties, in the absence of proven competitive harm. As indicated in the "Commission Communication on a better functioning food supply chain in Europe" of October 2009 (the "**Food Supply Chain Communication**"),[30] it is necessary to draw in this regard a clear distinction between concerns about potentially unfair trading practices – related to the imbalances in bargaining power of contracting parties – and concerns about anti-competitive practices.

- Competition Authorities consequently tackle buyer power to the extent that it harms, or could potentially harm, the competitive process and thereby consumer welfare. In this regard, it should be noted that contractual imbalances associated with unequal bargaining power does not always present a "*buyer power*" problem, in terms of competition law; therefore, the two concepts should be carefully distinguished.

- "***Unequal bargaining power***" is present whenever one party to a proposed contract, be it either the seller or the buyer, can "drive a hard bargain"; that is, can impose upon the other contracting party terms and conditions that are deemed unfavourable by that other party. There can be numerous reasons for the first party's ability to do so without risking that its counterpart decides not to enter into the proposed contract: significant difference between the relative sizes and turnover of the contracting parties (e.g., atomised small sellers), economic dependency arising out of long term business relationships (e.g., sole supplier/off-taker relationship), significant sunk costs already incurred by one of the parties (e.g., upfront investments), and last but not least changing supply/demand conditions in the relevant market. Unequal bargaining power often leads to commercial dealings, which are unlikely to restrict competition to any significant extent, but which appear to be unjust, unfair or undesirable from a social or political point of view. This has in turn triggered legislative responses in many Member States such as, for example, the adoption of laws on unfair trading practices or abuses of contractual dependency aiming to subdue the behaviour of the powerful contracting party (e.g., Austria, Belgium, France, Hungary, Germany, Greece, Italy, Ireland, Latvia, Portugal, Slovakia) or the introduction or envisaged adoption of codes of good practice establishing a set of rules in the transactions between large retailers and their suppliers (e.g. Czech Republic, Hungary, Lithuania, Portugal, Romania, Slovakia, Spain, UK).

[30] COM(2009) 591.

- "***Buyer power***" may have either beneficial or adverse effects on consumers. Buyer power is often exercised by buyers as a countervailing power to achieve better prices and terms from suppliers. When such savings are passed on to consumers downstream in the supply chain, buyer power has beneficial effects for consumers. Buyer power may also increase output in the upstream markets and thus increase the welfare of consumers on the long run. The exercise of buyer power which leads to lower prices upstream is therefore not to be considered per se anti-competitive. Generally, with sufficiently intense competition on downstream markets, lower prices obtained on upstream markets will be passed on to consumers. On the other hand, if a buyer possesses monopsony power (i.e., he is the only buyer in the relevant market) or considerable buying power/ market power on the upstream purchasing markets, which is coupled with significant market power on the downstream resale markets, a competition problem may arise if the buyer does not pass onto consumers any significant part of the benefits obtained on the upstream market from his suppliers. Moreover, if the exercise of buyer power is found to lead to a lower profitability for suppliers (e.g. suppliers' sale price being below their costs), this may, in specific circumstances, induce suppliers to invest less in new products and may lead to a loss in product diversity and quality for end consumers. Likewise, the exercise of buyer power may lead in specific circumstances to a concentration of players in downstream markets (which may entail as effect a subsequent concentration of the supply-side), ultimately resulting in higher prices and a reduction of product diversity. These aspects are also taken into account by EU competition policy when assessing the impact of the exercise of buyer power on consumers. Consumer welfare encompasses prices, diversity and quality.[31]

- The exercise of buyer power in an anti-competitive manner is contrary to EU competition law where there is a proven detriment to downstream consumers. Much of the current political interest is in fact focused on issues of "unequal bargaining power" which should be distinguished from issues of "buyer power", and actually highlights problems faced by small suppliers in the context of contractual negotiations with stronger buyers. This is also the case in the milk supply chain to a certain extent. It is worth recalling therefore that contractual imbalances associated with unequal bargaining power and unlikely to restrict competition to any significant extent are tackled through policy tools other than competition law instruments, such as, for example, contract law, common agricultural policy, SME policy, or unfair commercial practices laws. Most Member States have already enacted specific laws dealing with such issues and have established legal protective mechanisms for all contractual parties in the context of their commercial laws.

- NCAs concur in arguing that contracts should remain voluntary and their terms freely agreed between parties. NCAs would in principle be favourable to the adoption of voluntary codes of conduct/ good practice by operators in the milk supply chain. Such codes of conduct may emphasise that contracts should contain the same criteria (core requirements of the contract such as duration, penalties for breach, etc). NCAs insist that

[31] Issues related to buyer power have been a key element in the analysis contained in Commission merger decisions concerning the grocery retailing sector (see, for instance, Cases No. COMP/M.1684, *Carrefour / Promodés*, of 25.01.2000 and No. COMP/M.5047, *Rewe / ADEGK*, of 23.06.2008).

this process should not lead to a standardisation of the contents of the contracts, which would run counter the principle of contractual freedom and would put an unnecessary burden on the freedom of negotiation between parties.

- In this context NCAs agree that in order to strengthen the bargaining power of producers, who are often the weak contracting party, Member States should allow for the concentration of offer, strengthening of POs and development of cooperatives. Such measures, which are compatible with the Single CMO framework would help modernise and rationalise the agricultural sector and ultimately contribute to the efficiency of undertakings whilst stimulating competition between them.

## E. IS INCREASED TRANSPARENCY BENEFICIAL TO STRENGTHEN THE BARGAINING POWER OF FARMERS?[32]

In this regard, certain NCAs have warned that insisting upon achieving greater price transparency in the milk sector may be problematic. In Member States where the price of raw milk is almost completely transparent across regions, it has been noted that this is not advantageous to farmers, since buyers have an increased knowledge of supply pricing and they consequently use this information in negotiations with farmers[33].

This increased transparency may generate an anticompetitive effect in the sense that there is reduced uncertainty for buyers about their competitors' strategies, since all competitors know at all times the exact sale prices for raw milk, across regions in a given market. This would mean in practice that as soon as the lowest price is known to all buyers, it immediately becomes the reference price (this is particularly relevant for oligopolistic markets such as dairy processing and retail). Consequently this leads to an alignment to the lowest purchase price, to the detriment of farmers. The buyers' incentives to compete become lower and the farmers' possibility to differentiate their products is lessened.

On the other hand, as stipulated by the Food Supply Chain Communication the idea of Member States creating price observatories that would collect and aggregate price data could be envisaged since this may be useful in detecting broad malfunctions of the milk supply chain.

[32] For further analysis related to competition concerns linked to transparency and exchanges of information, please refer to: Case T-35/92, *Deere v Commission*, [1994] ECR II-00957; Case C-194/99 P, *Thyssen Stahl v Commission*, [2003] ECR I-10821; Case C-8/08, *T-Mobile Netherlands and Others*, [2009] ECR I-0000.

[33] The German NCA for instance observed that price transparency has mostly been beneficial to the buyers within the milk supply chain, to the detriment of producers.