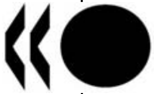
**Unclassified** **DAF/COMP(2005)44**



Organisation de Coopération et de Développement Economiques
Organisation for Economic Co-operation and Development

**01-Mar-2006**

**English/French**

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS**
**COMPETITION COMMITTEE**

**DAF/COMP(2005)44**
**Unclassified**

**Cancels & replaces the same document of 15 December 2005**

# COMPETITION AND REGULATION IN AGRICULTURE: MONOPSONY BUYING AND JOINT SELLING.

**JT03204714**

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# GERMANY

## 1 Buyer Concentration

### *1.1 Legal framework*

In Germany the prevention and restriction of buying power is guaranteed by merger control under Section 35 seqq. of the Act against Restraints of Competition (ARC), abuse control under Art. 82 of the EC Treaty and Sections 19, 20 of the ARC as well as the ban on cartels under Art. 81 of the EC Treaty and Section 1 of the ARC.

One important feature which distinguishes German competition law practice from that in other countries is that demand markets are generally dealt with as a complete analogy to supply markets (so-called "mirror image theory"). The reason for this lies in the competition concept on which the ARC is based. According to the established practice of the Federal Supreme Court the objective of the ARC is the freedom of competition, with the result that the protection of competition is pursued as an institution. Whereas in other legal systems restraints of competition are assessed in some cases exclusively for their effect on customers or consumers, in German competition law practice the restriction of entrepreneurial freedom of action is the predominant factor. By applying competition law norms to demand markets according to the mirror image theory the ARC provides a relatively high level of protection for preventing and restricting buying power.

Under merger control the Bundeskartellamt basically also examines whether the merger would have created or strengthened a dominant position in buying markets (Section 36 (1) of the ARC). Even if buying markets often play only a secondary role in mergers in other sectors, demand-side aspects have in practice gained great importance especially in mergers in the so-called rural trade, food industry and food retail trade (see following examples from the meat-processing industry and rural trade).

Art. 82 of the EC Treaty and Sections 19 and 20 of the ARC standardize the prohibition of the abuse of dominant positions or market power. The level of protection provided by the ARC in some cases well exceeds the European minimum level in Art. 82 of the EC Treaty laid down in EC Regulation 1/2003 passed by the Council on 16.12.2002 (Regulation 1/03). In particular Section 20 (2) of the ARC extends the target group falling under the prohibitions of unfair hindrance and discrimination of Section 20 (1) of the ARC to companies with powerful market positions below the dominance threshold. Section 19 (2) and (4) and Section 20 (2) of the ARC make it clear that the prohibitions of abuse apply equally to the supply and demand side.

Finally the prohibition of anticompetitive agreements under Art. 81 of the EC Treaty and Section 1 of the ARC also apply to buying markets. According to the jurisdiction on Section 1 of the ARC purchasing cooperations are prohibited if they have an appreciable effect on buying markets. In its practice with Art. 81 of the EC Treaty the European Commission is more lenient with purchasing cooperations whereby it focuses on the effects of the cooperation on the range of goods which its members provide.

In Germany a strong concentration of indirect buyers of agricultural products can be observed. The ten leading companies in the food retail sector together now make up 80 per cent of the domestic market.

### *1.2 Selected cases*

*„Ostfleisch“ (“East meat”)*

In August 1997 the Bundeskartellamt prohibited A. Moksel AG (Moksel) and Südfleisch GmbH (Südfleisch) from bringing their east German slaughtering plants into the planned joint venture Ost-Fleisch GmbH.

With annual turnovers of approx. 1.8 billion Euro (Moksel) and approx. 1.4 billion Euro (Südfleisch) Moksel and Südfleisch were the largest slaughtering companies in Germany. The traditional slaughtering houses of both companies were in southern Germany (Baden-Württemberg and Bavaria). They operated other operation plants in eastern Germany. These were to be combined within the joint venture Ost-Fleisch. In its prohibition the Bundeskartellamt defined various supply and demand markets. On the demand side (purchase of animals for slaughter, so-called “acquisition markets”) four markets came into question: Product-wise cattle were to be separated from pigs and the regional definition gave two separate markets, one in south Germany and another in south-east Germany. On the supply side different slaughtering product markets were defined at a national level. In the case of the planned formation of Ost-Fleisch it was to be assumed that Moksel and Südfleisch would coordinate their market behaviour on all directly and indirectly affected markets (so-called “group effect”.) The Bundeskartellamt based its prohibition on merger control regulations as well as on the prohibition of cartels (Section 1 ARC). The formation of Ost-Fleisch would have led to an appreciable coordination of market behaviour both on national slaughtering product markets and regional markets for the acquisition of animals for slaughter. Furthermore the coordination of Moksel and Südfleisch would have led to a dominant position on the demand markets for slaughter cattle and slaughter pigs in south Germany (their joint share of these markets were 58 per cent and 31 per cent respectively) and for this reason was to be prohibited under merger control. The parties concerned filed an appeal against this decision. However the Berlin Court of Appeals and the Federal Supreme Court confirmed the prohibition under Section 1 of the ARC so that an assessment of the case under merger control did not have to be decided in the last instance.

*“BayWa-WLZ“*

In April 2002 the Bundeskartellamt cleared the merger between BayWa AG (BayWa) and WLZ Raiffeisen AG (WLZ) only subject to conditions.

Both company groups from the so-called rural trade originate from the cooperative movement and in 2000 achieved turnovers at a national level of approx. 3.5 billion Euro (BayWa) and 0.7 billion Euro (WLZ). Due to its cooperative self-restraint BayWa was originally active only in Bavaria and WLZ only in Baden-Württemberg. As so-called central cooperatives they took on the function of wholesale for a number of smaller local cooperatives (so-called primary cooperatives). The structure has significantly changed in recent years because the central cooperatives have taken over many primary cooperatives and non-cooperative traders. Therefore BayWa/WLZ meanwhile also operate as retailers. On the demand side they buy cereal, maize, oil seeds and other field crops from farmers or primary cooperatives (so-called acquisition markets). On the supply side they sell seeds, fertilizer and pesticides, feedstuffs, tractors, building materials and mineral oil products to farmers or primary cooperatives.

On the demand side the Bundeskartellamt defined a number of local acquisition markets for grain and oil seeds on account of the high significance of transport costs. BayWa held dominant positions in the Bavarian acquisition markets and WLZ in the Baden-Württemberg acquisition markets. The dominant positions of BayWa and WLZ would have been strengthened by the merger because, inter alia, WLZ’s financial power increased and the current competition between BayWa and WLZ in the areas of activity which bordered on and in part overlapped those of the other and potential competition between BayWa and

WLZ, was eliminated. The competitive concerns were allayed by imposing obligations to divest. After the merger BayWa/WLZ had to sell between 30 and 35 trading sites to a third company.

*„Metro-Allkauf“*

In June 1998, after approval by the Bundeskartellamt, the Metro group (Metro) took over the allkauf group (allkauf). Metro is one of the largest trading enterprises in Europe. In 1997 the companies achieved a turnover of approx. 11 billion Euros (Metro) and 1.5 billion Euros (allkauf) in the German food trade. When comparing supplier conditions Metro discovered that suppliers who previously supplied both companies had in some cases agreed on more favourable conditions either with Metro or with Allkauf. This gave Metro grounds to approach these suppliers and to demand an adjustment of terms to the more favourable level for buyers backdated to January 1998. In addition to other companies, 20 companies from the food trade agreed to this demand and paid the difference to the end of 1998. In February 1999 the Bundeskartellamt prohibited Metro, inter alia, under Section 20 (2) and (3) of the ARC, from obliging the 20 companies to adjust their supplier conditions and to pay the respective compensatory amounts. The prohibition decision in this point was reversed in November 2000 by the Berlin Court of Appeals and in September 2002 by the Federal Supreme Court because the Bundeskartellamt should not have dealt with the payments already made in the past by way of a prohibition decision but in fine proceedings. However the Federal Supreme Court decided that the demand of a powerful buyer for a retrospective adjustment of conditions was to be judged as a forbidden inducement to grant it preferential terms so far as this was not a civil law claim and the buyer could not prove that this behaviour was objectively justified.

## 2 Producer “Joint-Activity” Organizations

### *2.1 Legal framework*

The production of agricultural goods enjoys exemption from the prohibition of anit-competitive horizontal and vertical agreements, both under EC law, which takes precedence, and under the ARC. Merger control and abuse control, however, find unlimited application.

Under Art. 36 of the EC Treaty the production of agricultural goods and trade with these products is only subject to EC competition law provisions where and in so far as decided by the European Council. Such a decision was laid down in the Regulation 26/62 of 4 April 1962 which provides for an exemption area for the agricultural sector in Art.2. According to paragraph 1 (1) of the regulation, Art. 81 (1) of the EC Treaty does not apply to agreements, decisions and practices which concern the production of the products listed in Annex 1 of the EC Treaty where the agreements, decisions and practices form an integral part of a national market organisation or are necessary for the attainment of the objectives set out in Art. 33 of the Treaty (i.e.: to increase agricultural productivity, stabilise markets, assure the availability of supplies, ensure the appropriateness of consumer prices and to ensure a fair standard of living for the agricultural community). In addition, Art. 2 (1) sentence 2 of the Regulation 26/62 provides that Art. 81 (1) of the EC Treaty does not apply to certain agreements, decisions and practices of agricultural co-operatives ("co-operative privilege"). However, this only applies where the respective agreements, decisions and practices do not contain price agreements and where competition is not excluded or the objectives of Art. 33 of the Treaty are not jeopardised.

In addition, further special competition regulations are laid down in the Common Market Regulations that have been created as an extensive body of European agricultural market regulations covering almost all agricultural products; these special regulations go beyond and take precedence over the provisions of the Regulation 26/62, in particular with regard to agricultural market regulations on fresh fruits and vegetables as well as on fish products.

A provision similar to the exemption area under European law was already incorporated in the first version of German competition law in 1958 and has been only slightly amended over the years. In the 6th amendment to the ARC the exemption area was aligned with European law. Under Section 28 (1) ARC the ban on cartels under Section 1 ARC does not apply to agreements between agricultural producers and their associations as well as to certain agreements between associations of agricultural producer associations unless they contain horizontal resale price maintenance agreements and unless competition is thereby excluded. In addition, under Section 28 (2) ARC the prohibition of vertical agreements (under Section 14 of the ARC) does not apply to agreements on the sorting, labelling or packaging of agricultural products. For a definition of the agricultural products concerned Section 28 (3) ARC refers to Annex 1 of the EC Treaty. Further exemptions from the prohibition of cartels and of vertical agreements are regulated outside the ARC in special provisions.

At first sight, the practical relevance of the exemption area under Art. 2 of Regulation 26/62 and under Section 28 ARC seems rather limited. Because the supply structure on agricultural markets is often fragmented (there are 390.000 farms in Germany) in many cases anti-competitive agreements do not violate Art. 81 (1) of the EC Treaty or Section 1 of the ARC because they are not appreciable. In addition the prohibition of price agreements and of excluding competition restricts the application area of this sector privilege. Just how limited the area of application is can be seen from the fact that Section 28 of the ARC only applies to co-operatives of producers (primary co-operatives) and associations thereof (central co-operatives) if their members are exclusively agricultural producers and co-operatives of agricultural producers. For example, with regard to the sale of milk and dairy products, the privilege only applies to agreements between dairies that are members of co-operatives; agreements between co-operative dairies and "private" dairies, i.e. dairies which are not organised in a co-operative, are not privileged. In addition, the exemption area is further limited by the full applicability of merger control and abuse control.

However, there have been cases where the exemption area of Section 28 of the ARC has facilitated joint sales of agricultural products by powerful unions of producer associations. The most recent example is described below; it concerned a distribution cartel for sugar between several large sugar factories in Northern Germany. Furthermore, co-operatives, such as companies in the dairy co-operative sector, are often discussing the setting up of joint sales agencies for milk and dairy products to improve their position in negotiations with the food retail trade by strengthening their power of supply. Under certain conditions the exemption area of Section 28 ARC offers a suitable competition law basis for such projects.

### *2.2 Justification of exemption area*

So far German and European legislators have considered the exemption area of Section 28 of the ARC necessary due to the length of the production process, the uncertainty of production success, the fragmented supply structure and the lack of flexible production adaptation to price signals, as well as for distribution policy reasons.

In the meantime the Federal Government considers distribution policies the most important factor. With the exemption under Section 28 of the ARC the government intends to enable farmers and producer associations to build up counterbalancing market power. Indirectly, this can lead to a price increase for farmers who supply raw materials because it limits the buying power of trade. Although the 6th amendment to the ARC abolished several other exemption areas the legislator adhered to Section 28 of the ARC. The current 7th amendment also intends to keep this exemption area.

### *2.3 Selected cases*

*"Beet sugar"*

In March 1999 the Bundeskartellamt prohibited a distribution cartel in the sugar production industry between Nordzucker AG (Nordzucker) and Union-Zucker Südhannover GmbH (Union-Zucker). The distribution cartel was organised as a joint venture in which Nordzucker held app. 87 per cent of the shares, Union-Zucker 9 per cent and a few smaller sugar producers the rest. The sugar producers opted for a joint distribution of their products to pool their supply and to "improve market opportunities". At that time Nordzucker ranked four among sugar producers in the European Union with a turnover of app. Euro 1 billion.[1] The indirect shareholders of Nordzucker and Union-Zucker were beet sugar farmers from the respective area of activity; conversely, the beet sugar suppliers of Nordzucker and Union-Zucker were usually also (indirect) shareholders. The Bundeskartellamt identified three separate markets which, not least due to the significance of transport costs, were confined to the area of activity of the distribution cartel. On these markets the distribution cartel held market shares of more than 80 per cent in the case of industrial sugar, more than 92 per cent in the case of household sugar and app. 95 per cent in the case of liquid sugar. In the Bundeskartellamt's view the conditions for an exemption under Regulation 26/62 and under Section 28 of the ARC were not given because the distribution cartel excluded competition which was (still) possible under the European Sugar Market Regulation. The Bundeskartellamt held that competition was already excluded by the dominant position of the distribution cartel. Therefore, the joint distribution was seen as an illegal cartel under Art. 81 (1) of the EC-Treaty and under Section 1 of the ARC.

The Berlin Court of Appeals reversed the prohibition of the distribution cartel in October 2001. In the Court of Appeal's view cross-border trade was not appreciably affected by the cartel between Nordzucker and Union-Zucker and therefore Art. 81 (1) of the EC-Treaty did not apply. The Court held that although the agreements constituted a cartel within the meaning of Section 1 of the ARC the cartel was subject to the exemption area under Section 28 of the ARC. Nordzucker and Union-Zucker were both producer associations and could therefore benefit from the so-called cooperative privilege. According to the Court, the demand that competition not be excluded allowed for a higher level of concentration than the criterion of market dominance. The Court continued that competition law intervention in markets as highly regulated as the sugar market could possibly result in only insignificant support of residual competition while at the same time considerably affecting the enterprises concerned.

*Plant breeder cartel "Kombiniertes System Saatgut" ("combined system seeds")*

Following a complaint the Bundeskartellamt conducted abuse proceedings from July 2000 to April 2002 against the *Bundesverband Deutscher Pflanzenzüchter e.V.* (BDP, Federal Association of German Plant Breeders) and the *Saatgut-Treuhandverwaltungs-GmbH* (STV, fiduciary seeds management company). In this context the authority achieved that numerous improvements could be realized in the practice of the so-called *Kombiniertes System Saatgut* (KSS, "combined seeds system").

As a rule the original breeder or discoverer of a plant variety is entitled to so-called plant variety protection under the *Sortenschutzgesetz* (SortSchG, plant variety protection law). However, this rule only applies to a limited extent to the so-called *Nachbau*, (subsequent reproduction), i.e. the use of harvested material grown by farmers on their holdings for subsequent reproduction by the farmers themselves. A farmer who makes use of the possibility of subsequent reproduction is obliged to pay the holder of the variety protection right an adequate fee in accordance with Section 10a (3) of the SortSchG. In order to facilitate these payments Section 10a (4) SortSchG restricts the ban on cartels provided for in Section 1 of the ARC (Act against Restraints of Competition): Agreements between holders of variety protection rights and farmers on adequate fees can be based on agreements between their respective professional

associations. Similar to the provisions in Section 28 ARC or Art. 2 of Regulation 26/62 these agreements may not exclude competition in the seeds sector.

In 1996 the *Deutscher Bauernverband e.V.* (DBV, German Farmers' Association) and the *Bundesverband deutscher Pflanzenzüchter e.V.* (BDP) agreed on the KSS system which regulates the procedure and the amount of the fee for subsequent reproduction. The STV was charged with carrying out and organising the KSS system. At the time of the investigations all 68 German plant breeders participated in the KSS or the STV. Apart from this central accounting system farmers can also enter into individual agreements with the respective plant breeders on the fee for subsequent reproduction under Section 10a SortSchG (so-called "individual procedure"). According to the Bundeskartellamt's investigations, however, all 68 holders of variety property rights had commissioned the STV to safeguard their rights, even if individual farmers wished to use an individual procedure. The STV charged a uniform rate, which exceeded the KSS rates, as subsequent reproduction fee which was meant to be agreed upon "individually". Farmers were thus practically prevented from using the individual procedure and price competition was excluded in violation of Section 10a (4) SortSchG and Section 28 (1) ARC.

The abuse proceedings could be terminated after BDP and STV had committed themselves to change this practice. Agreement on these fees and their payment can now take place in four different ways:

- A farmer can enter into an individual agreement on subsequent reproduction directly with the plant breeder and pay the fee to him.
- A farmer can enter into an individual agreement with the STV as the plant breeders' representative. However, the amount of the fee will not be fixed by the STV, but by the plant breeder.
- The farmer can be assessed under the KSS system.
- If neither an assessment nor an individual agreement can be achieved, the plant breeder has a statutory claim to payment of a reproduction fee by the farmer.

## 3 Competition Advocacy

In Germany, competition advocacy is entrusted to the Bundeskartellamt and the independent Monopolies Commission. Under section 42 of the ARC, every second year the Monopolies Commission compiles a report in which it comments on antitrust policy issues. Additionally it delivers further expert opinions both at the request of the Federal Government and at its own discretion. The Monopolies Commission has repeatedly argued in favour of abolishing sector-specific exemptions from competition law and in favour of a comprehensive market liberalisation. The last time the Monopolies Commission argued in favour of reducing competition law exemption areas was in March 2004 in its report on the current amendment to the ARC.

Contrary to the majority of competition authorities in OECD countries the Bundeskartellamt does not have any formalised rights or duties to comment on the general legislative process. However, in individual cases the Federal Ministry of Economics and Labour now and then informally asks the Bundeskartellamt to comment on competition law aspects of legislative processes outside competition law. In its public relations work the Bundeskartellamt regularly comments on general competition issues and has, contrary to the position of the Federal Government as described above but in line with the Monopolies Commission, supported a reduction of the several competition law exemption areas. The last time it did this was in the discussion paper on the meeting of the Working Group on Competition Law in September 2003. The Bundeskartellamt doubts the need for an exemption area for the agricultural sector under Section 28 and

Regulation 26/62 in particular because it sees only limited practical relevance in it. In the discussion led by the Working Group on Competition Law during the conference in September 2003 the majority of the academics present considered it advisable to take sector-specific particularities into consideration when applying the law yet at the same time clearly spoke out against maintaining or creating “per se” exemption areas.

## NOTES

1 After further mergers (inter alia with Union-Zucker) Nordzucker now regards itself as Europe's second largest sugar producer.