

# HUB-AND-SPOKE CASES IN THE PORTUGUESE GROCERY SECTOR



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## Hub-and-spoke Cases in the Portuguese Grocery Sector

By Ana Sofia Rodrigues, Catarina Tourais, Margarida Robalo Cordeiro, Mariana Dias, Marta Roch & Rafael Longo

Resale price maintenance (“RPM”) restrictions may play an instrumental role in implementing collusive agreements downstream, in a hub-and-spoke arrangement. This is highlighted in two recent decisions by the Portuguese Competition Authority (“AdC”) on two hub-and-spoke arrangements involving large grocery stores and beverage suppliers. In these cases, the AdC opted to pursue hub-and-spoke cases rather than pure RPM cases, as that would fail to capture the actual conduct of all firms involved, as well as the seriousness of the cartels fostered by the RPM restrictions. In particular, the decision to pursue these hub-and-spoke took into account the bargaining environment between each supplier and the retailers to explain how they had aligned incentives. When retailers hold significant buyer power over suppliers, they tend to put a downward pressure on supplier prices, so suppliers gain incentives to soften competition downstream in order to reduce that pressure. We provide some of the evidence used in these decisions and identify the key elements enforcers should consider when investigating potential hub-and-spoke arrangements.

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# I. INTRODUCTION

Hub-and-spoke arrangements have attracted attention from academics and antitrust authorities. These are cartels coordinated through indirect exchanges of information between suppliers and retailers and raise several questions related to the type of evidence that is consistent with the collusive agreement and the economic incentives of all firms involved.

In this article, we discuss two decisions adopted by the Portuguese Competition Authority (Autoridade da Concorrência, “AdC”) on a number of large grocery chains and beverage suppliers for promoting downstream price coordination, in a hub-and-spoke arrangement. The theory of harm considered the negotiation context between the supplier and the retailers as a key element to explain the alignment of incentives between the supplier and the retailers. We describe the bargaining environment, the incentives of the different elements in the value chain and how and why they departed from a more standard supplier-retailer context. We also illustrate the conduct with some non-exhaustive examples of indirect exchanges of information between retailers and suppliers from the two AdC’s decisions.

We discuss the relationship between resale price maintenance (“RPM”) restrictions and hub-and-spoke arrangements. In the AdC’s decisions, the RPM restriction played an instrumental role to implement and police the downstream collusive agreement. Nonetheless, pursuing a pure RPM case would fail to capture the actual conduct of all firms involved and the seriousness of the cartel the RPM facilitated.

We further discuss the burden of proof with respect to intent and awareness of the involved players. We conclude by identifying key elements that enforcers should pay attention to when investigating a potential hub-and-spoke arrangement.

## II. HUB-AND-SPOKE CASES IN THE PORTUGUESE GROCERY SECTOR

On December 18, 2020, the AdC adopted two decisions<sup>2</sup> where it imposed a total fine<sup>3</sup> of circa €304 million on six large grocery chains, two beverage suppliers, a board member and a director for price fixing of the suppliers’ products.

Both cases now sanctioned add to other investigations underway in the large retail sector. During 2017, the AdC carried out unannounced inspections in the premises of 21 legal entities. This led to the opening of 16 proceedings, more than a dozen of which concerning large retail. Currently, investigations have led to 9 Statement of Objections for hub-and-spoke practices sent to large food retailers and to suppliers of spirits and non-spirits, packaged bread and cakes, as well as personal care, beauty, and cosmetic products.

In particular, the AdC investigated whether several supermarket chains resorted to the vertical relations with their suppliers to promote downstream price coordination regarding the supplier’s products, in a hub-and-spoke arrangement.

### A. The Decisions

The first decision adopted by the AdC concerns price fixing between the main supermarket chains (Modelo Continente, Pingo Doce, Auchan and Intermarché), as well as a major beverage supplier (Sociedade Central de Cervejas, SCC).

The investigation determined that the distributors and the supplier concerted prices of several SCC products, such as beers, ciders, and sparkling water, for over 9 years, between 2008 and 2017.

In a second decision, the AdC fined the same four large grocery chains, as well as Lidl and E. Leclerc, for concerted pricing through spirits supplier Primedrinks. The scheme lasted for over 10 years, between 2007 and 2017, and involved various products in Primedrinks’ portfolio, which includes wines, whiskies, gin, and vodka.

Through a common supplier, retailers coordinated their pricing strategies downstream, thus softening competition and harming consumers.

In both decisions, the AdC imposed an immediate halt to the practice, since it was not possible to rule out that the investigated behavior was still in place.

<sup>2</sup> AdC Sanctioning Decision in [Process PRC/2017/7](#), of December 18, 2020 and AdC Sanctioning Decision in Process [PRC/2017/1](#), of December 18, 2020..

<sup>3</sup> According to the Portuguese Competition Act - Law no. 19/2012, of May 8, 2012, fines can reach a maximum of 10 percent of the company’s turnover in the last year of the practice.

## ***B. Theory of Harm and Economic Incentives***

The hub-and-spoke type of arrangement in these cases involves a supplier (the hub) and retailers (the spokes) forming a triangular scheme aimed at reducing competition at the retail level. These practices have elements of both vertical and horizontal conducts. Retailers, while not contacting directly with each other, pass on information to each other using a common supplier.

A key element in a hub-and-spoke investigation is to understand the incentives of both retailers and suppliers to participate in the collusive scheme.

The incentives for the retailers to participate in a hub-and-spoke arrangement tend to be more straightforward and similar to those of a “traditional” cartel: softening price competition and avoiding price wars to obtain higher retail margins.

A question often raised is how retailers and suppliers align their incentives such that collusion is sustainable.

In a vertical relationship between suppliers and retailers, it is often argued that suppliers wish to promote price competition downstream to avoid the problem of double marginalization. That is, the supplier does not want the retailer to price above the competitive level because that would imply a lower volume of sales and, hence, lower revenue for the supplier. This would put the incentives of suppliers and retailers into conflict.

However, this is not always the case, as this context abstracts that retailers may hold significant *bargaining power over suppliers*, which put a downward pressure on upstream margins.

Retailers holding significant buyer power *vis-à-vis* their suppliers tend to pressure suppliers to decrease supplier prices. By doing so, retailers aim at increasing their margins, but also to gain a competitive advantage over other retailers. As retailers try to decrease supplier prices to gain an edge over another, this may lead to lower supplier and retail prices.

Under significant buyer power and retail market concentration, suppliers would have an incentive to soften price competition at the retail level, avoiding reductions in the upstream margin.

For this reason, both retailers and suppliers may have their incentives aligned to soften price competition downstream.

As noted by the OECD (2019), in a situation where retailers pressure a supplier to obtain low retail prices or margins, suppliers can see a hub-and-spoke scheme as a way to avoid a reduction in their margins. In order to maintain both wholesale and retailers' margins, the supplier has incentives to facilitate a collusive scheme.<sup>4</sup>

Suppliers and retailers, therefore, solve their conflict of incentives by extracting welfare from consumers, while increasing their respective profit margins

Thus, the negotiation context, between the supplier and the retailers, can be a key element in a hub-and-spoke scheme and should be a main aspect of an antitrust investigation.

As in any antitrust case, evidence is also a key aspect on a hub-and-spoke, namely in terms of its consistency with the theory of harm and with the alignment of incentives of all involved firms.

## ***C. The Evidence***

In these investigations, the AdC seized mostly emails, within firms and between retailers and suppliers. The examples of evidence shown below are not exhaustive of the evidence gathered in the AdC decisions and are mainly to illustrate some of the points made.

The evidence in the AdC Decisions illustrates that suppliers, rather than being worried about reducing future retail prices and increasing sales, acted towards softening competition downstream to eliminate the bargaining pressure to wholesale prices and maintain margins (both upstream and downstream) (see Example 1).

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<sup>4</sup> OECD (2019) Roundtable on Hub-and-Spoke Arrangements – Background Note (available [here](#)).

## EXAMPLE 1

*Subject: FW: Increase in Sales Prices*

*From: [Price Analyst - Retailer A]*

*To: [Director - Retailer A]*

*[...]*

*With the entry into force of the new price table and the new year, [Supplier] asked us to align our sales prices to the ones they currently recommend so that they can ensure the market also follows this increase.*

*We await your validation.*

*[Table with a list of 27 products from [Supplier] and their new sales prices]"*

*From: [Price Analyst - Retailer A]*

*To: [Director - Retailer A]*

*[...]*

*I want to reinforce [Price Analyst]'s email, namely for [Product 1].*

*Considering that the [Supplier] has the alignment set up for tomorrow at a national level.*

*Therefore I appreciate an answer so I can increase the sales price.*

*[...]"*

*From: [Director - Retailer A]*

*To: [Price Analyst - Retailer A]*

*[...]*

*This time only after [Retailer B] increases first."*

Suppliers showed concerns over retail prices below recommended prices and asked retailers to increase retail prices, often following complaints from other retailers about competitors' retail prices being too low. Example 2 shows a retailer complaining, "competition has the following products with a sales price inferior to the one of our store," to which the supplier responds, "the store has committed to change it tomorrow," indicating that it contacted the second retailer in order to raise the retail price.

## EXAMPLE 2

*Subject: Competition prices*

*From: [Store Coordinator - Retailer A]*

*To: [Manager - Retailer A]*

*[...]*

*I inform you that our competition has the following products with a sales price inferior to the one of our store.*

*I demand an alignment so we can follow them.*

*[...]"*

*From: [Director - Retailer A]*

*To: [Supplier]*

*"This Monday we must have a solution, as we can't have this more expensive."*

*[...]*

*From: [Supplier]*

*To: [Director - Retailer A]*

*[...]*

*I only saw the email today. The sales person went to the store a while ago and called me now. The store has committed to change it tomorrow. When will you perform shopping again?*

*[...]"*

AdC Sanctioning Decision in Process PRC/2017/7, of 18.12.2020, paragraphs 1065-1066, p. 262-264. Free translation made by the authors.

Evidence also shows that there was a cross-check mechanism in place with regular reporting between retailers and the supplier. Retailers used their vertical relationship with the supplier to promote the control and monitoring of prices in the market, as to ensure price alignment. Deviations from the intended retail prices were reported to the supplier, who engaged in efforts to correct them).

In addition, evidence shows instances in which retailers pressure, coerce or retaliate against the supplier – or vice versa – to guarantee a retail price “correction” from the deviant (competing) retailer and ensure an overall retail price alignment in the market.

The communications exchanged between the suppliers and the retailers show they pursued a common anti-competitive objective of aligning prices downstream. For example, in one of the emails, the supplier writes to one of the retailers: *“I understand your point of view, but this is a national strategy and we must be aligned with the other retailers.”*<sup>5</sup>

At certain times, suppliers reimbursed discounts offered by retailers downstream, absorbing the impact of those discounts on their margins. This reimbursement was often a last resort strategy when the alignment was frustrated, as shown in Example 3, and presented in the form of threat and pressure on the supplier to ensure the collusive outcome.

### EXAMPLE 3

*Subject: Shopping Report of May 25 [Product 1]  
From: [Retailer A]  
To: [Supplier]  
[...]  
Hereby I send [Product 1] shopping report.  
Considering the prices charged by some retailers, we verify that our stores are uncompetitive.  
We appreciate your attention and correction of this situation in the market.  
Alternatively, and in last case, we request promotional conditions to the benefit our clients with the best prices.  
Look forward for your feedback  
[...]*

AdC Sanctioning Decision in Process PRC/2017/7, of 18.12.2020, paragraph 1047, p. 259. Free translation made by the authors.

Hence, the collusive scheme incorporated promotional periods in the downstream markets targeted for certain products, conditioning, however, the amounts of the discount and the implementation dates (as shown in Example 4). The evidence shows that retailers informed the supplier of the date in which they would be willing to change the retail price and requested the supplier to inform them of the dates in which their competitors would apply the agreed changes in the prices.

### EXAMPLE 4

*Subject: Promotional Cycle WATERS  
From: [Supplier]  
To: [Retailer A]  
As discussed, here bellow is the time frame regarding waters.  
Everything is confirmed regarding these dates. I will let you know should something change. Please check and provide some feedback, namely regarding [Product 1].  
Please pay special attention to [Product 2], as it will take effect as from tomorrow (22/10.)”*

*From: [Retailer A]  
To: [Supplier]  
“We need the price movement regarding waters to occur on the 3<sup>rd</sup> (Monday). Can you guarantee this alignment?”*

*From: [Supplier]  
To: [Retailer A]  
“In accordance to what we have informed you, what we can guarantee is the 5th (always on Wednesdays).”  
“Regarding [Product 3], and taking into consideration the usual promotions’ constraints, please confirm that you can follow such movement on 11/11”*

AdC Sanctioning Decision in Process PRC/2017/1, of 18.12.2020, paragraph 947, p. 206.  
Free translation made by the authors.

<sup>5</sup> AdC Sanctioning Decision in Process PRC/2017/1, of December 18, 2020, paragraph 969, p. 211. Free translation made by the authors.

Evidence also showed awareness of the practice as parties requested written conversations to be destroyed and to engage, preferably, in verbal conversations (Example 5).

#### **D. The Legal Nature of the Arrangements**

##### **EXAMPLE 5**

*From: [Retailer A]*

*To: [Another group of employees from Retailer A]*

*“Good afternoon,  
FYI.*

*It seems to me as an excellent recommendation.*

*In order to avoid the disclosure of this email I suggest that you destroy it and pass on (reinforce) the message verbally.  
You should also be careful with all written documentation, whether it's emails' prints or meeting notes.”*

AdC Sanctioning Decision in Process PRC/2017/7, of 18.12.2020, paragraph 2113, p. 563.

Free translation made by the authors.

A hub-and-spoke arrangement constitutes a form of conduct that may fall within the scope of Article 9 of the Portuguese Competition Act, as well as Article 101 of the Treaty on the Functioning of the European Union (“TFEU”).

In the Portuguese legal framework there is no provision referring specifically to hub-and-spoke arrangements. Similarly to any other type of collusion, in order to find that a hub-and-spoke arrangement constitutes an infringement under Article 9 of the Portuguese Competition Act and, if applicable, Article 101 TFEU, a number of conditions have to be met. In particular, there must be (i) an agreement or concerted practice between undertakings, or a decision by an association of undertakings; (ii) which has as its object or effect the prevention, restriction, or distortion of competition; (iii) with an appreciable effect on competition; and (iv) the verification of that appreciable effect on the Portuguese market.

The AdC analyzed the hub-and-spoke arrangements through the lens of a single concerted practice which comprehends both vertical and horizontal conducts and is typically implemented through an informal cooperation mechanism. In particular, through an indirect exchange of sensitive information between two or more competitors via a common contractual partner operating at a different level of the production/distribution chain.

Based on the AdC investigations, when assessing a potential hub-and-spoke arrangement, it is important to differentiate the information flow which is considered necessary and legitimate, as part of the vertical commercial relationship, from the situations in which competing economic operators use their common contractual partner as a way to achieve a coordinated market response.

Hence, qualifying a certain conduct as an illegal (vertical/horizontal) practice will essentially depend on the type of information passed along the supply chain.

### **III. POLICY DISCUSSION**

#### **A. The Relationship (and the Differences) Between RPM Cases and Hub-and-Spoke Arrangements**

From an enforcement point of view, one of the challenges in investigating a hub-and-spoke practice is to understand the incentives of firms in maintaining supra-competitive margins at different levels of the supply chain, and the mechanisms used to curtail competition. In this assessment, it is important to let the strategies of the market players speak.

This is especially relevant in hub-and-spoke cases where vertical restraints play an instrumental role in the implementation of a horizontal restraint. One should carefully consider the features of the vertical restraint used as an instrument to implement an anti-competitive practice with a horizontal dimension.

In the two decisions by the AdC, hereby discussed, suppliers and retailers implement a hub-and-spoke arrangement to reduce competition downstream, where RPM plays an instrumental role. The retailers enjoyed bargaining power over the supplier and put a downward pressure on upstream margins. As a result, the supplier had an incentive to soften price competition in the downstream market so as to avoid reductions

in its margin, upstream. This aligned the incentives of both suppliers and retailers: increasing retail prices would increase margins for suppliers and retailers, at the cost of consumer welfare.

The alignment of incentives between the supplier and the retailers provided a common anti-competitive goal and the conditions for a cartel agreement implemented via indirect exchanges of information. In this context, for the supplier, the incentives towards the maximization of margins prevail over the usual economic justification for vertical restraints.

The OECD, in its Background Note for the Roundtable on Hub-and-Spoke Arrangements,<sup>6</sup> finds that many RPM cases pursued by European agencies in recent years included elements of hub-and-spoke arrangements (§84). The OECD also highlights that in the EU, opting for an RPM may serve as a shortcut for competition authorities (§94).

However, getting the story right is important and consequential – in terms of the parties involved and the scheme and infringement at stake. In the case of the two decisions by the AdC, pursuing a pure RPM case would not reflect the actual conduct of all firms involved, nor the seriousness of the cartel the RPM fostered. Taking the most well-established decisional practice would fail to capture the circumstances in which the hub-and-spoke agreement occurred, where suppliers and retailers both played their part willingly and successfully, hampering competition and harming consumers.

### ***B. The Burden of Proof with Respect to the Intent and Awareness of the Involved Competitors***

The proof of this concerted practice entails a common (or shared) interest of the colluding undertakings, which encompasses the reduction of the uncertainty as to their future competitive conduct.

Therefore, for example, the information on the intended price point and on the timing of the price adjustments is of a strategic nature.

The evidence collected demonstrates each parties' contribution to the anti-competitive common objective, i.e. the alignment of their behavior in correlation with one another.

In these cases, each retailer is aware, or could reasonably have foreseen, that a similar interaction with the supplier is occurring in parallel in relation to the competitor retailers. This originates the common understanding necessary for the coordination.

## **IV. CONCLUDING REMARKS**

Hub-and-spoke practices usually combine horizontal collusive behavior between competitors, aided by a firm at a different level of the supply chain that facilitates the implementation of the collusive scheme.

When investigating a potential hub-and-spoke, enforcers should pay special attention to (i) the negotiation context between suppliers and retailers and who is exerting margin pressure; (ii) the incentives of all firms involved; and (iii) whether the evidence shows a level of awareness of the retailers regarding the indirect exchange of information and that retailers are aware that their competitors are also following the agreed prices.

In our perspective, when the negotiation and the bargaining context, the aligned incentives and the evidence all tell a story that is consistent with a hub-and-spoke arrangement, there is no reason for not going forward with a hub-and-spoke concerted practice.



6 OECD (2019) Roundtable on Hub-and-Spoke Arrangements – Background Note (available at [https://one.oecd.org/document/DAF/COMP\(2019\)14/en/pdf](https://one.oecd.org/document/DAF/COMP(2019)14/en/pdf)).



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