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### COMPETITION AND POVERTY REDUCTION

#### Contribution from Japan

-- Session I --

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## COMPETITION AND POVERTY REDUCTION

-- Japan --

### **Reduction of the poor of small enterprises through the enforcement of the Subcontract Act by the Japan Fair Trade Commission: Introduction**

1. Micro, small and medium enterprises (hereinafter, SMEs) that engage in transactions with large enterprises are often exploited by large enterprises, and may encounter economic hardship. In Japan, a typical example is where small and medium subcontractors are hit by delay in the payments of subcontract proceeds by large “parent” enterprises” (main subcontracting enterprises), and this has long been a problem in Japanese society.

2. Over the years, the Japan Fair Trade Commission (hereinafter, the JFTC), Japan’s competition authority, has dealt effectively with this problem through enforcement of the Act against Delay in Payment of Subcontract Proceeds, Etc. to Subcontractors (hereinafter, the Subcontract Act), which serves as a supplementary law to the Act on Prohibition of Private Monopolization and Maintenance of Fair Trade (hereinafter, the Antimonopoly Act). This paper explains reduction in the impoverishment of SMEs through the JFTC’s application of the Subcontract Act.

#### **1. Dual structure of the economy and the impoverishment of SMEs**

3. A phenomenon called the “Dual structure of the economy”, whereby a high productivity sector comprised mainly of large enterprises and a low productivity sector comprised of SMEs exist side by side, is likely to happen during “periods of economic growth”. Under such a structure, large enterprises and SMEs exist side by side, and a large gap exists between the two of them in aspects such as capital intensity, productivity, technology and wage levels.

4. Whereas large enterprises introduce advanced capital equipment and achieve high labor productivity, SMEs mainly used traditional production methods and their labor productivity is low. The wage gap between large enterprises and SMEs widens, reflecting this gap in productivity, and the wage gap persist for a long time due to disunited labor market liquidity and the segmentation of the labor market into the large enterprise segment and the SME segment.

5. Consequently, large enterprises use SMEs as subcontractors and gain a cost advantage by exploiting these low wages, sometimes using them to cushion the impact of economic downturn.

6. This dual structure of the economy is a problem that has faced in common with developing countries, and resolving this problem of the impoverishment of exploited SMEs and their workers is an important government issue.

7. In Japan, the dual structure of the economy is thought to have existed since the 1920s, but during the period of high economic growth after World War II, this gap widened significantly, and what is peculiar to Japan is that it performed the function of supporting Japan’s economic development.

## 2. Challenge faced by the JFTC in an era of industrial policy supremacy

8. Confronted by economic devastation following its defeat in World War II, The Antimonopoly Act was introduced in Japan as a part of the economic democratization policies of the Allied Powers in 1947. The Antimonopoly Act was introduced, which was considered stricter than the U.S. antitrust laws that were its parent laws, and the JFTC was established as Japan's competition authority. At that time, Japan was faced with the urgent issue of developing and strengthening the domestic industry to achieve economic independence.

9. The Government therefore introduced a various protective measures and financial aid for industrial activities to strengthen the industrial infrastructure and rationalize or modernize enterprises. Under the administrative guidance of the government office dealing with industrial matters, the Government also often introduced measures for restricting competition in response to a trend towards overproduction occurring as a result of deterioration in economic conditions, and there was also pressure for substantial relaxation of the regulation of cartels from business circles. As a result, in the 1950s, the JFTC was forced to significantly roll back its regulation of cartels and the JFTC's inspection activities also slowed significantly. This period was referred to as the "winter years" for the JFTC.

## 3. Introduction of regulation of abuse of superior bargaining position

10. While relaxing regulation of cartels, the 1953 amendment of the Antimonopoly Act tightened regulation of unfair trade practices in the area of SMEs.

11. In other words, because the provision on the elimination of unfair economic power gap<sup>1</sup> was deleted, there was also the risk that large-scale enterprises might abuse their position and exert unfair pressure on SMEs, and to address such a situation, a new type of practice was added to unfair trade practices.

12. The newly added unfair trade practice was "abuse of bargaining position", and this is linked to the current regulation on abuse of superior bargaining position.

13. With the introduction of this regulation, trade practices whereby large enterprises use their position to impose an unfair disadvantage on SMEs became the subject of regulation. Such practices include delays in the payment of subcontract proceeds, which had become a social problem at the time, and abuse of the superior bargaining position of department stores over suppliers.

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<sup>1</sup> The Antimonopoly Act enacted in 1947 included a provision to prevent excessive concentration of economic power to the effect that a transfer of commercial facilities, etc. can be ordered in cases where there is "unfair economic power gap". More specifically, the act defined "unfair economic power gap" as where "there is a significant gap between enterpriser's economic power and its competitors", "the superior economic power of the enterprise cannot be justified on technological grounds" and "the gap enabled the enterprise to create a private monopoly", and prescribed that the transfer of commercial facilities, etc. can be ordered when such a situation exists.

However, this provision did not regulate anti-competitive practices. It was a "structural control" measure aimed at improving the market structure itself in terms of market competitiveness.

This provision was abolished as a result of the 1953 amendment of the Antimonopoly Act on the grounds that it was not suited to the present state of the Japanese economy.

#### **4. The JFTC's proactive response to subcontract transaction issues**

14. Under the dual structure of the economy, it became common for large “parent” enterprises to use SMEs as subcontractors. As explained before, this was because there was substantial difference in wages between large enterprises and SMEs and because this arrangement acted as a control valve against economic fluctuation. Subcontractors usually tended to be forced into accepting severe trading conditions by their parent enterprises.

15. Especially in the process of economic adjustment, a subcontractor affiliated with a large enterprise was made to function as its parent enterprise's economic control valve, and was put in a situation where it was fully exposed to the stresses of recession, including reduction in order volume, decline in order value, delays in the payment of subcontract proceeds, and draft in long-term notes.

16. At the time, the hardship of micro, small and medium subcontractors became a major social problem centering on the issue of delays in the payment of subcontract proceeds, and the Government also examined countermeasures.

17. Based on the 1953 amended the Antimonopoly Act, the JFTC designated a new type of unfair trade practice as follows, “establishing or changing trade terms or executing transactions in a way disadvantageous to the other party, unjustly in light of the normal business practices by making use of one's superior bargaining position over the said party”.

18. As part of the implementation of the newly introduced regulation of abuse of superior bargaining position, the JFTC actively worked on regulation in areas related to SMEs which are in a weak competitive and bargaining position, including regulation of delays in the payment of subcontract proceeds and the unreasonable return of goods to suppliers by department stores.

19. The JFTC conducted a survey of the payment of subcontract proceeds, targeting ten sectors where there were considered to be a high level of subcontract transactions and significant delays in the payment of subcontract proceeds at the time, including the machinery sector, the manufacture and repair sector for automobiles, etc. Based on the results of this survey, in December 1953, the JFTC announced in the name of Chairman that delay in the payment of subcontract proceeds was a violation of the Antimonopoly Act and that the JFTC would make parental entrepreneurs seen to delay payment improve the situation. The JFTC then gave guidance for improvement in payment of subcontract proceeds to the 10 industries surveyed.

20. However, due to the subsequent increase in calls for further tightening of control over delays in the payment of subcontract proceeds from within government departments and small and medium enterprise associations, in March 1954, the JFTC announced “criteria for defining delays in the payment of subcontract proceeds” and decided to use these as a basis for tackling the problem of delays in the payment of subcontract proceeds.

21. These criteria applied new criteria for the aforementioned abuse of superior bargaining position to the subcontract transactions of the ten types of industries targeted in the survey, and gave specific examples of violations to speed up the processing of cases, and this became the prototype for the Subcontract Act enacted later.

22. From fiscal 1954, the JFTC began expanding the number of cases surveyed based on the aforementioned criteria, and actively applied the Antimonopoly Act to improve and prevent delays in the payment of subcontract proceeds.

23. It is fair to say that while cartel regulation was relaxed, people's understanding and support for the JFTC's antimonopoly measures gradually increased as a result of the tightening of unfair trade practices regulation in the area of SME transactions.

## **5. Enactment of Subcontract Act**

24. From 1955, Japan's economy began to boom, and with the JFTC's promotion and guidance for the payment of subcontract proceeds, the terms for payment of subcontract proceeds to subcontractors were also expected to improve.

25. However, the strains imposed on subcontractors by parental enterprises tended to worsen year by year. In other words, the rate of use of drafts as a means of payment of subcontract proceeds increased, and the proportion of long-term drafts also increased. What is more, there was an increasing tendency for parental enterprises to demand subcontractors to lower the amount of subcontract proceeds payable.

26. Given this further deterioration in the business situation of subcontractors, many of which were SMEs, it became necessary to adopt more rigorous and effective measures than before to tackle the problem of delays in the payment of subcontract proceeds, etc.

27. Upon examination, the Government reached the conclusion that it was necessary to regulate subcontract transactions by means of a special act, and not by means of the Antimonopoly Act. This conclusion was based on the following three reasons:

1. In subcontract transactions at the time, parental enterprises placed orders with subcontractors verbally or without clearly stipulating the terms of transactions, and when parental enterprises had to pay the subcontract proceeds, there were cases where the parental enterprises enforced one-sided disadvantageous terms on the subcontractor. Based on the assumption of regulation under the Antimonopoly Act, it was necessary to somehow objectively make clear the terms of the transaction between the parental enterprise and the subcontractor, but clarification of transaction terms pursuant to the provisions of the Antimonopoly Act was impossible to achieve, and special legislation was considered necessary.
2. Since, in a subcontract transaction, the subcontractor is heavily dependent on the parental enterprise, the subcontractor cannot be expected to make a complaint to the JFTC, demanding measures against violation by the parental enterprise without preparation to end its business relationship with the parental enterprise. It was, therefore, considered, necessary for the speedy resolution of problems associated with subcontract transactions to make a survey with the cooperation of relevant government agencies, on a permanent basis, not on the basis of complaints of violations, and to actively seek correction, and new legislation to this end was considered necessary.
3. With respect to delays in the payment of subcontract proceeds, which was the main problem associated with subcontracting, promoting the voluntary cooperation of parental enterprises was considered a more effective way of improving the situation than administrative measure in accordance with the Antimonopoly Act proceedings to order payment, and the enactment of separate proceedings from the proceedings under the Antimonopoly Act was considered necessary.

28. Given the economic background and legal reasons surrounding subcontract transactions described above, the Subcontract Act was enacted and promulgated in June 1956.

29. The Subcontract Act has been amended repeatedly since its enactment to the present day, to reflect changes in the economic conditions surrounding subcontract transactions, but the original Subcontract Act enacted in 1956 is outlined below.

### **5.1 *Clarification of trading relationship***

30. On the assumption of controlling violations related to subcontract transactions, the act obligated the parental enterprise to deliver to the subcontractor a written statement (written order) specifying the amount of subcontract proceeds, etc. for the transaction to clarify the terms of transactions, and also obligated the parental enterprise to prepare and retain documents related to the transaction with the subcontractor.

### **5.2 *Clarification of prohibited conduct of parental enterprises***

31. The act clarified that the parental enterprise must not unreasonably refuse to receive the work, delay payment of subcontract proceeds, unreasonably reduce the amount of subcontract proceeds, or unreasonably return the work, thereby expecting self-restraint from parental enterprises and actively taking enforcement actions against enterprises in violation of the act.

### **5.3 *Strengthening of supervisory structure***

32. The act stipulated that the JFTC, the Director-General of the Small and Medium Enterprise Agency and the competent ministers had the right of on the spot investigation, since subcontractors cannot be expected to actively file complaints about violations related to subcontract transactions, and also stipulated that the Director-General of the Small and Medium Sized Enterprise Agency had the right to request the JFTC for measures under the Subcontract Act.

### **5.4 *Adoption of recommendation system***

33. The act stated that the provisions of the Antimonopoly Act shall not be applied in cases where the administrative measure of recommendation was adopted against a parental enterprise that failed to comply with prohibited conduct provisions and measures such as the payment of subcontract proceeds was adopted by the parental enterprise in accordance with the recommendation, thereby giving the parental enterprise the opportunity to make voluntary efforts to improve the violation so that cases can be processed speedily and smoothly.

## **6. *Outline of current Subcontract Act***

34. Already, more than fifty years have passed since the Subcontract Act was introduced in 1956 as an effective countermeasure against delays in the payment of subcontract proceeds. With the content of its provisions being amended in line with changes in economic conditions since its introduction, the Subcontract Act exists as important legislation governing subcontract transaction relationships under the dual structure of the economy which exists even today, and it is also actively applied by the JFTC. The current Subcontract Act is outlined below.

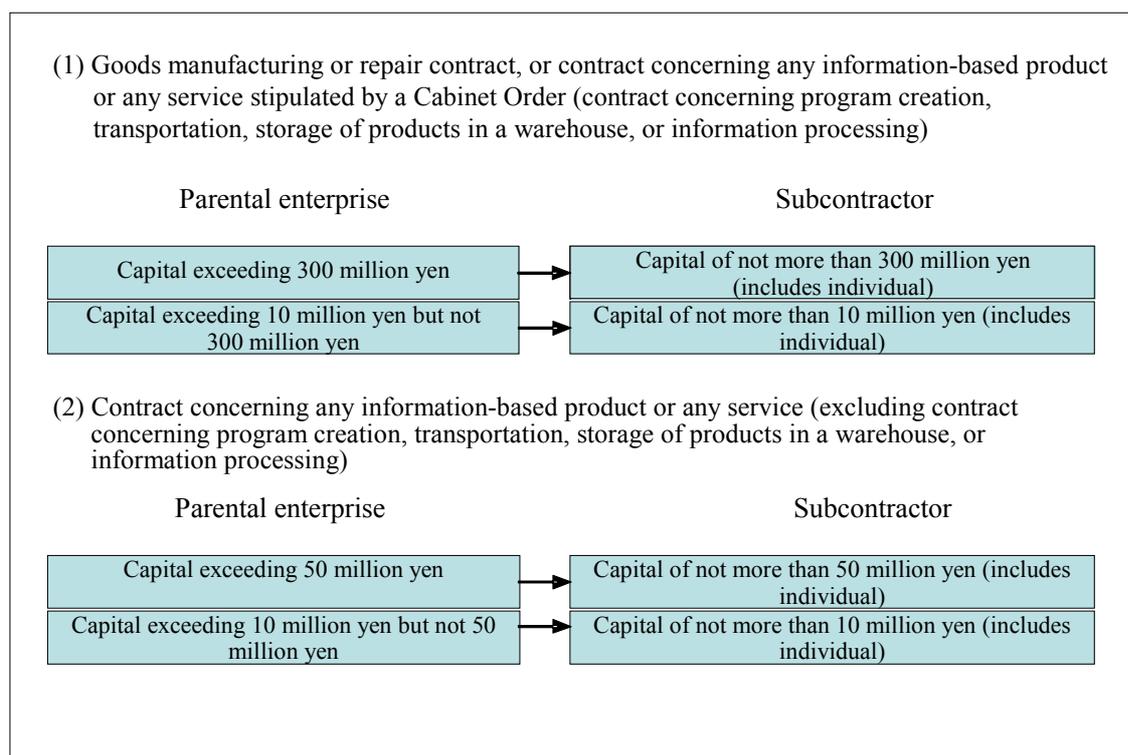
### **6.1 *Regulated transactions***

35. Transactions regulated by the Subcontract Act are transactions whereby a juridical person enterprise with capital exceeding a certain amount makes a “manufacturing contract,” “repair contract,” “information-based product creation contract,” or “service contract” with an individual enterprise or a juridical person enterprise with capital of not more than a certain amount.

36. The Subcontract Act states that out of the aforementioned four contract transactions, transactions where the capital of the parties to the transactions meets certain criteria, as shown below, are regulated by the act.

37. It goes without saying that, for regulation purposes, there is no need to determine the relevant market or define the dominant position in the relevant market or superior bargaining position.

**Definition of parental enterprise and subcontractor**

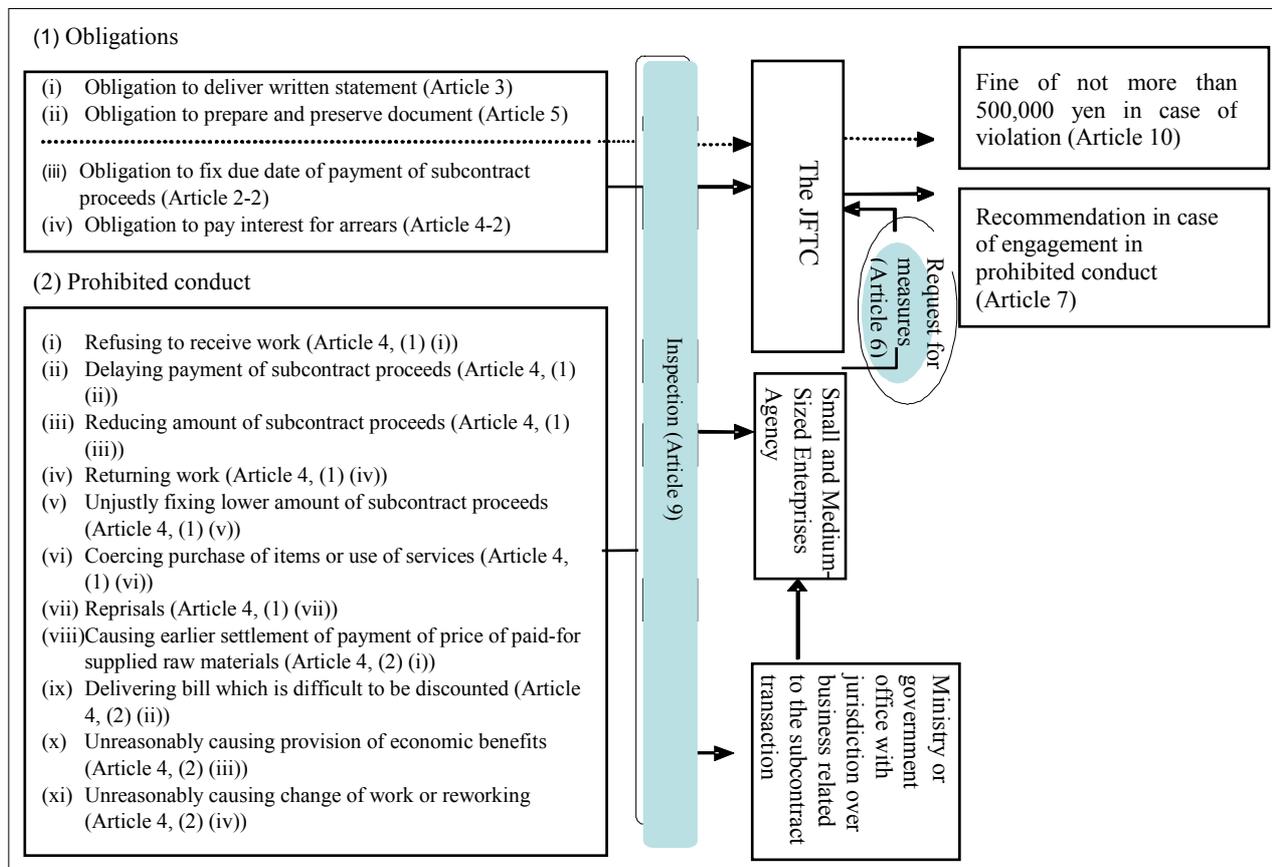


**6.2 Obligations and prohibited conduct of parental enterprise, and measures taken by the JFTC**

38. The obligations and prohibited conduct of the parental enterprise and measures taken by the JFTC are shown below.

39. Depending on the gravity of the case, the JFTC may issue corrective guidance in the form of administrative guidance, in addition to the following legal measures.

**Obligations and prohibited conduct of the parental enterprise and measures taken by the JFTC**



**7. Enforcement Situation of the Subcontract Act**

40. With respect to the enforcement of the Subcontract Act, due to the nature of subcontract transactions, even if a subcontractor suffers disadvantage as a result of violation of the Subcontract Act by the parental enterprise, the subcontractor cannot be expected to provide information voluntarily. Consequently, to uncover suspected violations of the Subcontract Act, the JFTC regularly sends questionnaires to parental enterprises and subcontractors, demanding reports.

41. The number of such document-based inspections has increased consistently every fiscal year, and in FY2012, the JFTC conducted document-based inspections of 38,781 parental enterprises and 214,000 subcontractors.

42. In relation to parental enterprises who were in violation of the Subcontract Act, the JFTC ask them for correction by means of issuing recommendations under the Subcontract Act, or administrative guidance.

43. In FY2011, the JFTC issued recommendations in 18 cases, and issued administrative guidance in a record number of 4,326 cases, indicating that the act is being actively applied.

44. Furthermore, the JFTC actively engaged in promotional and educational activities, as it is essential that parental enterprises and subcontractors understand the content of the Subcontract Act, in order to try to prevent violations of the Subcontract Act. Every year, the JFTC holds seminars and explanatory meetings about the Subcontract Act in regions throughout Japan.

45. Also, towards the end of each year, the JFTC issues a letter under the joint signatures of the the JFTC Chairman and the Minister of Economy, Trade and Industry to more than 30,000 parental enterprises and more than 600 relevant trade associations, demanding thoroughgoing compliance with the Subcontract Act.

## **8. Relationship between the Antimonopoly Act and the Subcontract Act**

46. The Subcontract Act is an act to supplement the Antimonopoly Act. By establishing capital classifications and contractor classifications like manufacturing and repair contract with respect to practices included in unfair trade practices prohibited by the Antimonopoly Act that fall under “abuse of superior bargaining position,” the Subcontract Act indicates the scope of transactions in which abuse of superior bargaining position is likely to occur, and it specifies as prohibited conduct the types of practices that may constitute abuse of superior bargaining position. The Subcontract Act also prescribes matters to be observed by parental enterprises (obligation to deliver document, obligation to fix due date for payment of subcontract proceeds, etc.).

47. Unfair trade practices are practices that fall within the scope of regulation of unilateral conducts under the Antimonopoly Act and that are practices provided by the Antimonopoly Act or designated by the JFTC from among the types of practices that “pose a risk of impeding fair competition”, and currently 17 types of practices<sup>2</sup> have been provided or designated.

48. The meaning of “fair competition”, which forms the basis of unfair trade practices regulation, rests on the notion of a fair competition order through the satisfaction of the following three conditions: (1) ensuring free competition, (2) ensuring the fairness of competitive means, and (3) ensuring the basis for free competition.

49. Of these, (3) ensuring the basis for free competition is taken to mean that the basis for free competition is ensured, wherein transactions are undertaken with trading entities judging freely and independently whether to trade and trading terms, and the regulation of “abuse of superior bargaining position” is classified as falling under this.

50. The Subcontract Act is a law enacted to supplement the aforementioned regulation of abuse of superior bargaining position under the Antimonopoly Act.

51. However, unlike the Antimonopoly Act, the Subcontract Act does not state that it aims to ensure fair and free competition or to ensure the interests of general consumers. Instead, the Subcontract Act states that it aims to make transactions of parental enterprises with subcontractors fair and to protect the interests of the subcontractors. The Subcontract Act also has the nature of a law protecting enterprises beyond the framework of competition law.

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<sup>2</sup> Unfair trade practices that are provided by the Antimonopoly Act or designated by the JFTC are as follows: concerted refusal to trade, other refusal to trade, discriminatory consideration, discriminatory treatment on trade terms, etc., discriminatory treatment, etc. in a trade association, unjust low price sales, unjust high price purchasing, dealing on exclusive terms, resale price restriction, dealing on restrictive terms, deceptive customer inducement, customer inducement by unjust benefits, tie-in sales, etc., interference with competitors’ transactions, interference with internal operation of a competing company, abuse of superior bargaining position, unjust interference with the appointment of a counterparty's officers.

## **9. The JFTC's enforcement of the Subcontract Act**

52. A typical example of where the competition authority is in charge of the execution of policy/law besides the enforcement of competition policy and competition law is consumer policy. Competition policy and consumer policy are similar in the sense that they are both policies for ensuring the interests of consumers, and strong synergies are expected when the competition authority is in charge of both.

53. However, consumer policy is also an area that the competition authority cannot take charge of completely as some aspects, such as consumer safety policy, are highly technical. Therefore, depending on the content of the consumer policy, a different organization from the competition authority may take charge, and a policy decision is made to determine which consumer policies to put the competition authority in charge of.

54. Similarly, a policy decision is made to determine which authority is put in charge of responding to the impoverishment of SMEs that are the vulnerable players in a competitive market and their workers, and to determine which policy means are to be used.

55. For example, a problem with a specific transaction arising in connection with the contract such as delay in the payment of subcontract proceeds, which has been mentioned as a problem in this paper, is ultimately a civil problem between the specific enterprises, and some believe that the parties involved should themselves seek to resolve the problem through judicial proceedings, and that there is no need for administrative agencies to intervene.

56. However, apart from exceptional cases where it has become the norm to resolve specific trading disputes in a court of law and there are well-established judicial services for this, usually, SMEs are likely to be put in a situation where they have to accept, without resistance, unjust practices by large enterprises. Accordingly, it is fair to say that some degree of intervention by administrative agencies is necessary to improve the situation.

57. It is true, the drawbacks that arise when an administrative agency intervenes in specific trading problems must also be borne in mind.

58. For example, arrangements established as social safety nets, such as assistance for failed SMEs, livelihood assistance for low-paid workers and unemployment insurance benefits, are not interventions in specific autonomous business activities themselves and can be seen as competitive neutrality policy arrangements. However, regulation under the Subcontract Act is different from such competitive neutrality policy arrangements, as it is intervention in the actual trading process between the parent enterprise and the subcontractor.

59. Excessive administrative intervention in transactions between parental enterprises and subcontractors deters parental enterprises from using subcontractor transactions and impedes the free entry and withdrawal by subcontractors, indeed it risks having consequences that go against the aim of the Antimonopoly Act of promoting fair and free competition. Consequently, the balance between protection of SMEs and freedom of the business activities of enterprises needs to be taken into account in policy application.

60. It is, therefore, necessary to appropriately establish the subjects of regulation and to ensure the transparency of regulation content to avoid having a deterrent effect, i.e. causing parental enterprises to refrain from using subcontractors. From the viewpoint of smooth continuity of business activities, it is also necessary to strengthen compliance among parental enterprises and reduce the actual occurrence of violations, to prevent damage suffered by subcontractors as a result of violations, as far as possible.

61. The JFTC came to be in charge of enforcing the Subcontract Act due to the act's historical background. As already explained, the JFTC's involvement began when, in the 1950s, the JFTC started providing assistance to SMEs that were in economic hardship under the dual structure of the economy, by using the administrative measures under the Antimonopoly Act of unfair trade practices to take enforcement actions against delays in the payment of subcontract proceeds. This received strong support from the Government and the Japanese people and led to the enactment of the Subcontract Act.

62. In addition, the JFTC, the competition authority whose main duty is to promote fair and free competition, is in charge of enforcing the Subcontract Act, which has the nature of a law protecting entrepreneurs. From a theoretical point of view, the demonstration of strong synergy can be expected in terms of achieving a balance between competition policy and policies for the protection of SMEs, and ensuring the economic basis for fair and free competition.

## 10. Conclusion and implications

63. As explained above, in Japan, the competition authority the JFTC performs the function of rescuing SMEs from economic hardship and creating a base for them to be able to conduct autonomous business activities by regulating unfair practices of parental enterprises against subcontractors through application of the Antimonopoly Act and the Subcontract Act, which was enacted as a supplemental law to the Antimonopoly Act.

64. The following three points should be identified as points to bear in mind so that activities to support SMEs such as the above are sufficiently effective and do not go against the aim of the competition law of maintaining and promoting competition.

1. Even if SMEs suffer disadvantage through the abuse of superior bargaining position by large enterprises, due to the nature of such transactions, SMEs cannot be expected to file for legal proceedings to improve the problem, and even if the administrative agency regulates such unfair practices by law, the SMEs that are the victims cannot be expected to actively provide information because they fear the possibility of reprisals from the parental enterprises. Therefore, some ingenuity in the detection of suspected violations is necessary. The JFTC detects suspected violations of the Subcontract Act by issuing questionnaires on a regular basis each year and demanding reports so that parental enterprises can not know who provides the information.
2. If parental enterprises continuously engage in unfair practices against subcontractors, this will have serious adverse economic effects, not only impeding the investment of subcontractors and causing them to withdraw from the market, but also impeding the efforts of parental enterprises to improve productivity (see Annex). Consequently, ensuring compliance by parental enterprises to prevent the occurrence of violations is more important than the detection of violations. It is, therefore, necessary to make the content of regulation clearer and more transparent and to put effort into dissemination and awareness rising activities in relation to relevant enterprises. The JFTC has also accumulated broad expertise in this field.
3. Needless to say, it is important for competition policy to maintain active market entry/withdrawal by SMEs in the competition process and to ensure that transactions between large enterprises and SMEs are conducted based on the autonomous judgment of the specific enterprises. Accordingly, excessive intervention on the pretext of relief for impoverished SMEs should be avoided.

The Subcontract Act regulates only specified transactions between enterprises with capital exceeding the amount prescribed by law and entrepreneurs with capital of not more than the said

amount, and is not the kind of legislation that regulates transactions between large enterprises and SMEs across the board. Also, although the government office with jurisdiction over the business is granted a certain degree of authority under the Subcontract Act, the act states with regard to measures in response to violations that only the competition authority JFTC shall issue recommendations.

**ANNEX: THE “COMING OUT” OF ABUSE OF  
SUPERIOR-BARGAINING POWER IN THE ANTITRUST WORLD\***

**By Frederic Jenny\*\***

(PP.8-9)

Even though it is unlikely to occur frequently, we have to consider the possibility that the coercee has market power. For example, a small supplier with no close competitor is faced with the following alternative by a large retailer: either the supplier meets some unjustified demand (such as, for example, an additional discount) or the retailer will refuse to carry the supplier's products. In such a case, the threat forces the supplier to lower his price. Thus, when the coercee has market power, coercive threats may have a consumer welfare increasing effect.

However, coercive threats may also have negative effects on efficiency.

First, as mentioned earlier, through coercion retailers can shift over to suppliers the burden of some functions that would otherwise be thesis as retailers. They have an interest in doing so, irrespective of whether or not the suppliers are more or less efficient at providing those functions than they are. Thus burden shifting may take place, even if it means a loss of productive efficiency.

Second, and more importantly, when faced with the prospect that retailers will capture their efficiency gains through additional coercive threats and demands, upstream firms will be discouraged from seeking productivity gains, from investing or even from staying in the industry. The only firms that will consider staying in the industry at the upstream level are firms which for some reason (the strength of their brand, for example) have a countervailing bargaining power. New entrants or small firms will usually not have such a countervailing bargaining power in the initial stages of their entry on a market and will therefore be at a disadvantage. As a result, bargaining power on the retailer side is likely to create or increase barriers to entry in the upstream industry, and to lead to an increase in concentration and a decrease in consumer choice and competition. There are allegations in Europe that the increase in concentration in the European food industry is partly a response to concentration (and buyer power) at the retail level.

It has been argued that powerful retailers are unlikely to engage in coercion since by doing so they would promote concentration among their suppliers and thereby undermined their own interests. But they will do so because of the externality involved. In an oligopolistic situation in the retail sector; a large scale retail chain cannot be sure that its competitors will not engage in coercive practices which might ultimately lead to more concentration of suppliers, irrespective of whether or not it engages in such practices itself. Yet if the others do not engage in such practices, each oligopolist retailer has an incentive to engage in such practices since it will gain competitive advantage by shifting some costs to suppliers.

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\*\* Professor of Economics and Co-Director of the Centre Européen du Droit et de l'Économie (ESSEC), and Chair of the OECD Competition Committee

In this scenario, even if we assume that consumers may benefit in the short run (if, for example, the additional advantages secured through coercion are passed on to them), they will ultimately bear the cost of the increase in concentration (and therefore the decrease in the intensity of competition) between the suppliers in the medium to long run.