



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

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**ROUNDTABLE ON MONOPSONY AND BUYER POWER**

**-- Note by Hungary --**

*This note is submitted by Hungary to the Competition Committee FOR DISCUSSION at its forthcoming meeting to be held on 22-23 October 2008.*

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1. The Hungarian Competition Authority (Gazdasági Versenyhivatal (GVH)) has very limited experience in cases related to buyer power. However, it could be interesting that the issue of buyer power can come up in Hungary in the context of two laws, the Competition Act<sup>1</sup> and the Act on Trade.<sup>2</sup> Regarding to the former the GVH deals with buyer power with regard to dominance, merger and non-hardcore agreements, while the Act on Trade has a different approach on buyer power and imposes additional obligations on firms having “significant buyer power”. The Act on Trade primarily aims to help the survival and development of suppliers (primarily SMEs) and the GVH is responsible for the enforcement of only a part of the Act.

## 1. Definition

2. On the one hand, based on the Competition Act and according to the jurisprudence, the GVH would conclude that buyer power or dominance exists if the following conditions hold:

- the buyer has significant share from the overall sales of suppliers,
- the suppliers have no real alternatives to sell to other customers,
- the suppliers cannot replace the drop of sales of the given product with other type or variety of product(s).<sup>3</sup>

3. Whereas the second condition refers to demand-side substitutability, and the third condition refers to supply-side substitutability, i.e. the possibility to switch with use of the existing equipment to the production of other products.<sup>4</sup> So the relative size of the downstream firm to the upstream firm does not necessarily implies buyer power. In this case (GE) the Competition Council of the GVH stated that the asymmetric bargaining power between firms does not necessarily constitutes buyer power in the upstream market, e.g. when the dealer faces competition in the downstream market.

4. The issue of buyer power can arise in the context of merger cases in connection with countervailing buyer power, discussed in detail later.

5. On the other hand according to the Act on Trade it is prohibited to abuse “significant buyer power” (SBP) *vis-à-vis* suppliers. The regime of the Act on Trade resembles to some extent that of the EC telecommunications framework regulation, which relies on the concept of significant market power. According to the Act a retailer has SBP if its consolidated turnover derived from its retail activities in the previous year was higher than HUF 100 billion (approximately EUR 414 million). A retailer or a group of retailers also has SBP when it, or the purchasing association it belongs to, is in “*a one-sidedly favourable bargaining position vis-à-vis its suppliers*” based on “*the structure of the market, the existence of entry barriers, the market share and the financial strength of the enterprise and its other resources, the size of its trading network, the size and location of its outlets and all of its trading and other activities*”. The Act on Trade prohibits, among others, the unjustified discrimination of the suppliers, the threatening of them with dissolution of contract in order to achieve one-sidedly favourable conditions, the unjustified restraint of the access of suppliers to sales opportunities, the unjustified alteration of the terms of contracting to the detriment of the suppliers or reserving such option for the retailer, charging fees one-sidedly to suppliers for services not demanded by them, or the forcing of them to avail themselves of designated third parties.

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<sup>1</sup> The Act of LVII of 1996 on Competition

<sup>2</sup> The Act of CLXIV of 2005 on Trade

<sup>3</sup> These factors were identified in case Vj-46/2001/13, *Magyar Posta Rt.* and *Matáv Rt.*, 13 August 2001.

<sup>4</sup> This argument came up in case Vj-50/2003/13, *GE*, 2 October 2003.

These descriptions are intended to catch practices – or certain types of them – like imposing various fees (e.g. slotting allowances, or fees covering nonexistent services), forfeit practices, exclusive discounting and other practices the suppliers often complain about publicly.

6. Although the act came into force in 2006, there has been only a few enforcement actions since. In a case<sup>5</sup> *OBI* (a DIY retailer) was claimed to abuse its SBP due to conditions in the general contract *vis-à-vis* suppliers with respect to forfeit, returning goods and discounting. In the end the case was terminated due to the lack of SBP (*OBI*'s turnover was under the HUF 100 billion limit), and no infringement was established. In the *TESCO* (an FMCG retailer) case<sup>6</sup> it was claimed that the retailer abused its buyer power and forced the suppliers to avail themselves of designated suppliers of merchandising. This case was ended with remedies by which *TESCO* undertook to choose its merchandising suppliers by means of a transparent tender. It is worth noting that none of the cases ended with imposing fine.

7. In summary, the Act on Trade specifies explicitly and almost completely what constitutes a SBP and an abuse of it; and the listed abusive behaviours fall basically under *per se* prohibition. As a consequence, there is no much room for the GVH to adopt a rule of reason approach such as identifying SBP or assessment of welfare effects of its exercise under the Act on Trade. Actually, the Act on Trade is not considered by the GVH as part of competition law, though the GVH is required to enforce the above-mentioned provisions of the Act. Thus, the remaining part of this submission focuses on the notion of buyer power as applied under the Competition Act.

## 2. Identifying buyer power

8. It is crucial to identify the factors that affect a firm's ability to use its buyer power. As mentioned above, the GVH takes into consideration supply-side and demand-side factors.

9. 1. With regard to demand-side substitutability the barriers to entry and/or expansion regarding the downstream market<sup>7</sup> or the ability to circumvent that market level<sup>8</sup> was considered. The latter refers to the case when a supplier has sufficient financial strength to establish its own downstream presence (in this case by setting up a wholesaler).

10. Assessing supply-side substitutability the dependence of the suppliers on the market of the product in question was considered. In other words: are they present in other product or geographical market(s)? Or in the extreme case is it possible for a supplier to exit the market?<sup>9</sup>

11. The possible existence of countervailing buyer power has been considered in the context of mergers on the supply side. In cement cases<sup>10</sup> a few large buyers was identified, nevertheless there were a

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<sup>5</sup> Case Vj-149/2007/58, *OBI*, 2 July 2008.

<sup>6</sup> Case Vj-92/2006/92, *TESCO*, 24 August 2007.

<sup>7</sup> In the case Vj-182/2001/22 (*Hungaropharma*, 13 June 2002.) it was found that a merger in the pharmaceutical wholesale market increases the buyer power, but it cannot be abused because there are no significant barriers to entry into the wholesale market.

<sup>8</sup> Case Vj-99/2002/33, *Phoenix Pharma* and *Bellis*, 19 November 2002.

<sup>9</sup> In the case Vj-41/2002/33 (*Nemzeti Autópálya Rt.* 2 June 2003.) it was found that the suppliers, large construction companies, have extensive business activities in other construction markets as well, so they can exit from the Hungarian motorway construction market, therefore they are not exposed to the abuse of buyer power of *Nemzeti Autópálya Rt.* (the national motorway operator monopoly and the buyer of motorway construction services).

lot of small buyers (representing a significant percentage of purchases together) as well, therefore the larger buyers' power was still not strong enough to countervail that of the merging parties. Taking into consideration other market attributes, such as the homogeneity of the product and the transparency of the market, the existence of large buyers could also motivate suppliers to defend themselves plausibly against any countervailing buyer power by price fixing.

12. 2. In a merger case<sup>11</sup> in the sugar industry it was pointed out that countervailing buyer power was mitigated by the price elasticity of end consumers: if the price elasticity was relatively low (and as a matter of fact due to the nature of the product, it was), then the buyer (a retailer) has less incentive to use its power against suppliers, as it can pass on the price increase to end consumers. Moreover, it was held that despite the existence of large buyers using industrial sugar, who have alternative sweetener supply sources (demand-side substitutability), they had weak incentive to use their bargaining power, as the importance of industrial sugar was insignificant in their cost structure.

### 3. Welfare Effects

13. 3. The GVH has not assessed the possible welfare effects of buyer power in any of its cases so far. However, the need of better understanding has arisen. Therefore, the chief economist conducted a research<sup>12</sup> devoted to the issue. The main results are summarized below.

14. 4. The assessment of welfare effects is rather complicated. Favourable effects can be the countervailing of upstream market power, the pass-through of the achieved cost reductions to the end consumers, the increasing of the price elasticity of demand due to stronger incentives to provide wider scope of products and to pursue intensive advertising by the buyer or the stronger incentives for suppliers and/or competitors to adopt more efficient methods.

15. 5. There can be negative effects as well, but these are not so straightforward and are harder to prove. First, if the buyer power raised the barriers to entry and/or to expansion, the incentives to improve quality and to innovate can be diminished. Second, the asymmetric distribution of downstream market power can weaken the above mentioned pass-through effect.

16. 6. Besides, in a case<sup>13</sup> it was stated that the negative effect of the abuse of buyer power could result in using less input (the firm can lower the price of the given input by decreasing its purchases) and in consequence producing less output in the downstream market in comparison to the outcome under effective competition.

17. 7. Thus the assessment of the pass-through effect is very important in such cases, but would be rather complicated to carry out. Moreover there is a certain possibility that the positive effects exceed the negative effects. As it has a considerable data and resource requirement, the GVH should consider to proceed with such evaluation only when it has a decisive role in a case.

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<sup>10</sup> Cases Vj-17/2001/89, *Holcim Rt., Breitenburger GmbH and CeBeKa Kft.*, 9 January 2002. and Vj-73/2001/65, *Holcim Hungária Rt., Duna-Dráva Cement Kft., BÉCEM Cement és Mészipari Rt. and Magyar Cementipari Szövetség*, 8 October 2002.

<sup>11</sup> Case Vj-127/2001/71, *Raffinerie Tirlementoise S.A. and Financiere-Franklin Roosevelt S.A.S.* 21 March 2002.

<sup>12</sup> The research is based mainly on the study of Rodrigues (2006): Buyer power and pass-through of large retailing groups in the Portuguese food sector.

<sup>13</sup> Case Vj-41/2002/33, *Nemzeti Autópálya Rt.* 2 June 2003.

#### 4. Buyer Power and Conduct

18. 8. Under competition law enforcement, as noted above, so far the GVH has had only a few cases involving buyer power issues. Regarding horizontal mergers, the issue did arise, but did not play a critical role. The subject was taken into consideration with respect to countervailing buyer power, for example in the sugar industry.

19. 9. Besides, in the *METSPA* case<sup>14</sup> it was found that, in spite of the fact that the parties (a buyer group) established a joint company to negotiate certain purchasing conditions with suppliers, the GVH established that the alleged conduct did not impede competition. The decisive argument was that the parties had small (less than 10 per cent) joint share on the upstream market and the fact that the parties negotiated the final conditions directly with the suppliers.

20. 10. Furthermore, although in the cement cartel case<sup>15</sup> and in the sugar merger case the assessment of countervailing buyer power did come up, the argument was not found decisive.

21. 11. Finally, the GVH has also encountered a rather odd argument in a proceeding<sup>16</sup>, requested by the *Lawyers' Chamber in the city of Debrecen* the applicant argued as an extenuating cause that the consumers' bargaining power was strengthened by knowing the Chamber's recommended fees. This innovative argument (perhaps relevant in a competition culture context rather than in a buyer power context) was rejected by the GVH.

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<sup>14</sup> Case Vj-176/2003/8, *Metro, Spar, Praktiker*, 7 April 2004.

<sup>15</sup> Case Vj-73/2001/65, *Holcim Hungária Rt., Duna-Dráva Cement Kft., BÉCEM Cement és Mészipari Rt. and Magyar Cementipari Szövetség*, 8 October 2002.

<sup>16</sup> Case Vj-56/2003/18 *Lawyers' Chamber Debrecen*, 9 September 2003.