

## APPENDIX I

**BUYING GROUPS: TEXT OF NOTES RELEASED ON JUNE 3, 1983  
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Perhaps it would be appropriate for me to start by explaining what I mean by a buying group, although I expect a number of you in this audience already belong to groups of your own. If you don't belong to one, you may still be familiar with some of the names -- for example Federated Cooperatives is one which operates in this part of the country.

Buying groups include any organization which can be said to do the purchasing for a group of otherwise more or less independent businessmen. They may do this in the real sense that they place orders, take delivery and perform other services for their members. Alternatively they may be a collection office which buys in name only, the purpose being to pool total volumes in order to get higher volume rebates.

Buying groups may have been in the news recently but there's really nothing new about them. They have been around for a long time. In fact you've got one of the originals here in town, Associated Grocers Ltd., incorporated in 1948. Back in 1935 a Royal Commission had expressed concern that large-scale buyers could exert unfair pressure on suppliers causing harm to small and medium-sized retailers. The law was changed to accommodate this view and to make sure that volume discounts are available to all buyers competing with each other and purchasing articles of like quantity and quality.

I believe this has made an important contribution to competition by allowing small buyers, through the establishment of legally distinct buying groups, to compete on the same basis for their supplies as their larger and more powerful rivals. It's not only fair that small buyers should have equal access to goods at the same prices as large buyers, it's also efficient. It ensures success for the fittest not the fattest in the market place.

In recent years there's been quite an expansion of buying groups. Groups have formed among retailers and wholesalers in all kinds of business -- groceries, hardware, auto supplies, paints, drugstores, furniture and appliances, food service, you name it. Some of these buying organizations are part and parcel of full-line franchise operations which provide members with additional and substantial services. Other primarily exist to take advantage of better rebates available through pooling their purchases.

### COMPETITIVE CONTRIBUTIONS

I think that those groups which provide substantial services deserve a special mention. Some businesses have found that they can improve the efficiency of their distribution and marketing by offering centralized services - delivery, inventory management, warehouses, advertising -- all sorts of services which are sometimes more effectively performed by a group than if they had to be undertaken separately by individual members. I'd say that this sort of group displays competitive initiative, finding and developing new and productive ways of doing business at lower costs, to the benefit of supplier, retailer and consumer alike. They are there for good reason - they provide valuable services to their members and do it well.

Associated Grocers is an example of such a group, based here in Calgary. Associated is a retailer-owned wholesaler that sponsors some 258 stores in Southern Alberta and South East British Columbia. The independents had been unable to obtain direct deliveries from manufacturers so they got together in 1929 to pool their warehousing and take delivery for the group. And it didn't stop there. Associated provides more than wholesaling and warehousing. It offers a whole range of services from trucking, to advertising, to store site locations, store planning, financing assistance, computerized reports, electronic ordering, all sorts of services sometimes more effectively performed on the larger scale of a group and perhaps beyond the capability or resources of the individual member stores.

Of course it's not only through groups that progress is made. I believe that the retail and wholesale industry in general has been particularly innovative and progressive, responding quickly and imaginatively to changes in the market. For example, the grocery business has responded to consumers' demands by providing bulk goods and developing house brands, neogenerics and no-name products. This gives consumers what they want at low cost at the same time as keeping suppliers and other retailers on their toes. One-stop shopping is another important example. This increases productivity in the retail industry.

But let's turn now to buying groups whose major and perhaps only function is to pool purchases to qualify for larger volume discounts. This is only a "paper" service but it may, all the same, have a positive effect on competition in a number of ways.

An important objective of any buying group is to keep purchase costs down. Members are able to pass some of the savings in purchase costs on to consumers in lower prices, and they will do this providing there's been no reduction in competition at the retail level. Again, keeping costs down is consistent with lively competition in the market place and of course we all welcome any move to keep consumers' prices down.

It may be good for consumers but what about the effect on competition among the retailers themselves? I have already mentioned this. Most important for competition is that buying groups allow small buyers to compete on the same basis for their supplies as their larger rivals. Success in the market place depends on efficiency not size and David gets a fighting chance against Goliath.

And what about competition at the level of the supplier? Again buying groups provide a David-and-Goliath solution, David the buyer, against Goliath the supplier. Groups help to improve an uneven balance of power between small buyers and big suppliers who may already have a degree of market power of their own.

Mind you, the supplier may also benefit from group buying if groups also provide a credit guarantee against the bankruptcy of their members. Those that do, notify the supplier when the member is in financial difficulty and, if needed, set up a fund to satisfy the supplier's claims. This can be a big help to a supplier, especially when he's dealing with a wholesaler or retailer whose financial situation is hard to investigate.

### STORMCLOUDS

No doubt you are beginning to wonder why I should have any worries at all about buying groups. I've said that they've been around for a long time and I've said that they make an important contribution to competition. So what's the problem?

The problem lies in the scale of the groups that are emerging now. Let's look at the grocery business, for example. Certainly small grocery retailers have taken advantage of buying groups. Indeed one such group of independent retailers, the Calgary based group United Grocery Wholesalers Limited, now buys on a larger scale than any of the individual major grocery chains. But, what's more, it's not just the small retailers who are forming buying groups. The big chains are doing it too. Most recently IGA and Safeway. And then there's Dominion and Steinberg, Lowlaws and Provigo. These are all big businesses and they too have combined to form their own buying groups. So what we are seeing now is the possibility of a dramatic increase in concentration in buying activities in the grocery retail business with the possibility too of a commensurate increase in buying power. And that's why buying groups have caught my attention.

I don't want you to think I'm picking on food retailers when I single them out. What I have to say applies to any area of business. It's simply that the food retail industry is so important to all consumers. The scale of its buying groups happens to be very visible. Suddenly it's all Goliaths and hardly any Davids.

So while buying groups have allowed small buyers to compete more effectively, they have also been responsible for a disquieting change in the potential concentration of buying power. And unfortunately a disproportionate degree of any market power can always lead to the danger of anti-competitive behaviour.

### COMPETITIVE CONCERNS

I'd now like to address the particular risks and concerns raised by this recent trend in concentration of buying activities through common buying offices.

The Combines Investigation Act has a number of provisions which protect the public interest from the abuse of market power whether in the hands of individuals or of groups of individuals, whether buyers or sellers. The major issues I am going to touch upon are arrangements which lessen competition.

### ANTICOMPETITIVE PRACTICES

#### Conspiracy (32)

First I would like to talk about conspiracy -- agreements among competitors to adversely affect competition at any point in the production and distribution chain. The Act's provisions against conspiracy are the cornerstone of competition legislation.

Section 32 makes it a criminal offence to make an agreement to lessen competition unduly. This applies to competition in the purchase of a product as well as in production, sale, supply or other activities. I want to emphasize that the offence is in the agreement itself. The only question is whether the lessening of competition likely to follow is undue.

When we look at buying groups, we see, by their very nature, that the members have entered into an agreement, the agreement to pool their purchases. This lessens competition in the purchase of a product and it does so by bringing two or more previously independent and competing purchasers together to act as one.

Now such an agreement may also increase competition among rival buyers in other areas of their business, say at the retail level -- but that's not what's at issue here. That would be competition in the sale or distribution of a product. What we're concerned with here is competition in the purchase of a product.

Of course, the critical question which follows is what constitutes an undue lessening of competition in the purchase of a product. Among other things that would depend on the group's leverage in the market as a purchaser -- the degree to which suppliers of products depend on the group's members to reach the final customer, the consumer. I might mention that previous judgements have found a share of a market as small as 54 per cent to be large enough to represent an undue lessening of competition.

We then have to decide on the relevant market. This would have to depend on the circumstances of the case. I can't give any fixed rules, but in many cases we'd probably be looking at a more local or regional market. We'd want to know what proportion of suppliers' products go through the buying group in order to reach the consumer.

A group need not be dominant in its dealings throughout the country to have leverage in its negotiations with suppliers. It could have market power as a purchaser either because it accounted for most the purchases of products produced in a particular region, or because its members were the major outlets in that region for products produced anywhere. If a group represents an important route of access for products to reach consumers in a particular region, this could give the group considerable market power even against national brand names.

These aren't my only concerns. It also matters how the buyers conduct their business. Various questionable practices in purchasing activities might also give me reason to believe that competition was lessened unduly. Let me give you an example.

A group might be tempted to abuse its market power by putting pressure on suppliers to give it lower prices, pressure which would not work if there were still lively competition among purchasers for the supply of goods: for example, blacklisting a manufacturer because he would not offer a volume incentive program. This would be an agreement to lessen competition in the purchase of a product.

While the very nature of a buying group constitutes an agreement that lessens competition in the purchase of a product, buying groups may also run a risk of conspiracy by reducing competition unduly in activities other than buying. Groups bring together buyers who compete with each other in retailing, wholesaling, or maybe even manufacturing. This could facilitate collusion in areas of business other than the actual purchasing of their supplies and that's a serious concern. Groups offer members the opportunity to exchange information about prices and market shares and the temptation to coordinate business to their mutual advantage in a way which could lessen competition unduly. Group members must be particularly careful to avoid this. Intimacy among rivals isn't to be encouraged, especially if they are already dominant in their market.

The harmonization of prices and promotional strategies, dividing up the market, tying up supplies, creating barriers to entry through pressure on suppliers -- agreements to participate in practices such as these might well constitute an undue lessening of competition at the horizontal level -- the retail level of whatever business the group's members are engaged in.

We've seen consumer groups express their own anxiety about the final outcome at the retail level. For example, I've seen statements in the newspapers which say that while consumers may benefit in the short term from lower prices, there are fears that group buying will inevitably lead to higher retail prices. Well, that fear might be realized if buying groups also manage to reduce competition at the wholesale or retail level. I'm telling you that you have to guard against any such arrangement to do this, to reduce competition at the next level of your business and, indeed, at the purchasing level too. I want to emphasize that the very idea of a continuing relationship between otherwise competing businessmen gives me cause for concern.

I have to admit that there is a fine distinction to be made between searching for the best available price, which is a feature of healthy competition, and channelling or controlling the price, which may be a feature of no competition at all. The point I want to stress is that members of bona fide buying groups should be careful to continue to act independently and competitively in their choice of products and their quest for best prices in their dealings with both suppliers and consumers.

#### Volume Rebates: When is a Group a Purchaser?

As I mentioned earlier, the Combines legislation requires sellers as a practice to charge competing purchasers the same price for like quantities of like quality goods. Historically, small buyers were given the chance by s.34 of the Act to form a buying group to purchase like quantities to those bought by the biggest chains and thus take advantage of volume rebates and discounts offered by their suppliers.

The issue here is whether a buying group is a legitimate "purchaser" eligible for volume rebates. If the group is not a legitimate purchaser then it may well be found to be a sham set up as a device to allow otherwise separate buyers to circumvent the law on price discrimination.

Some recent developments in the food retailing industry have given cause for concern in this connection. The emergence of very powerful buying groups composed of the largest food retailers suggests that the purchaser requirements of s.34 merit closer examination, an examination we are presently undertaking with respect to a number of buying groups. What factors support the argument that a particular buying group qualifies as a purchaser for volume rebate purposes under the legislation?

My first observation is that a buying group seeking the protection of the Act must be the purchaser in very strict, legal terms. This means the group must be a separate legal entity which buys goods from suppliers. The group is responsible to those suppliers for paying for the goods and acquires the property interest of the suppliers in making these purchases. This does not necessarily require the group to take delivery of the goods. But a prudent buying group will keep accurate purchase invoice records to substantiate its buying activities. As the purchaser of the goods, the buying group now sells the goods in a separate legal transaction to its members. This dual transaction feature is vital to the characterization of the group as a lawful intermediary engaged in purchasing activities on behalf of its members who, in turn, are thus able to benefit from volume rebate levels that they, in their individual capacities, would otherwise be unable to attain.

As the purchaser of first instance, the buying group will imperil its claimed 'purchaser' status if it seeks to limit, qualify, exempt or otherwise impair its responsibility to pay its suppliers for goods ordered in its name. Such efforts, in my view, would tend to support the interpretation that the member firms are the actual purchasers and that indirect price discrimination in their favour is being practised by the sellers involved in such schemes.

Similarly, questions will be raised if member firms in a group attempt to limit their liabilities to the cost of merchandise ordered on their behalf by the group. Any such efforts tend to support the view that the members are using the group as a sham to place their own orders to obtain rebate benefits to which they are not entitled.

I would like now to discuss the meaning of indirect price advantages under the Combines Act. S.34 states that sellers must charge competing purchasers the same price whenever like quantities of goods of like quality are involved. If you look at the whole provision, you will see that the meaning of "price" goes far beyond the idea of apparent selling price in the market. The definition is designed to catch any attempt to practise discrimination among competing buyers by any kind of price adjustments - the words are "any discount, rebate, allowance, price concession of other advantage." The operative purchase price for the purposes of the Act is the 'bottom line' or 'real net' price paid by the buying groups. On top of that, the provision prohibits both direct and indirect price discrimination.

This means that I would look very carefully at any evidence of a practice of direct or indirect payments made by suppliers to any purchaser. It doesn't matter whether the purchaser is an individual or a group. Any buyer with bargaining power might be able to extract discriminatory price concessions from a supplier. Insofar as buying groups are potentially powerful I would be especially alert to the danger that they might use their power to persuade suppliers to give them preferential treatment.

From my comments about the meaning of price advantages, it will be evident that proper and complete records ought to be maintained by suppliers to confirm the actual prices being charged buying groups. They will want to document their selling practices because section 34 is directed against pricing activities by suppliers. Whether buying groups and other buyers are also liable under section 34 has not yet been settled by our courts.

I hope that my remarks have alerted you to some of the serious legal risks that must be addressed by sellers, buying groups, and buyers contemplating the formation of buying groups. I would be pleased, in the context of our compliance advisory program, to respond to individual requests for further information and comments in this important area.

#### Other issues

I'd like to mention in passing some other provisions of the Act which might apply to buying groups. The sections I have in mind deal with monopoly and merger, and with price maintenance.

We're used to thinking of monopoly in terms of a selling monopoly -- control of the business of supplying a product. The relevant area of business here is not so much selling as buying. If a buying group substantially controls the market for the purchase of a product and operates in that market to the detriment of producers, then that buying group might be guilty of an offence under section 33 of the Act. Whether it has control in the selling market too is a different question. A buying group might have substantial control of the market for the purchase of a product and therefore be a monopoly but still have its members compete in the wholesale or retail market.

The section which prohibits a monopoly, s.33, also prohibits a merger. A merger means, among other things, the acquisition by one or more persons, of any control over or interest in the business of a competitor or a supplier whereby competition is likely to be lessened to the detriment of the public interest. This definition has a very broad sweep and could well include some buying groups.

The other provision I mentioned, price maintenance, comes under section 38. This section protects suppliers from pressures from powerful buyers to raise prices to other buyers or even to cut them off.

I'm not going to go into either of these matters, monopoly and merger or price maintenance, in any detail. I've taken enough of your time and will have to leave them for another occasion.

#### Concluding Remarks

I began my remarks with the historical reasons behind the formation of buying groups, groups which traditionally have been relatively small. Their

existence was stimulated by the need to compete more effectively with large buyers in the market place.

In recent years, we have seen the emergence of groups on an unprecedented scale, small buyers joining to make very large groups, and very larger buyers forming their own groups. The popular press continues to emphasize the advantages of buying through groups, whatever their size, but there is also a growing public awareness of the dangers of increasing concentration in the market place.

Buying groups with considerable potential market power necessarily give me cause for concern. This new development demands that we take a new look at buying groups and their relationship to the provisions of the Combines Act. The factors raised are complex -- I have talked about the major issues raised under sections 34 and 32, the sections dealing with price discrimination and conspiracy. Both the business community and its legal advisors will have to look carefully at these provisions. I will have more to say at a later date on these and other sections of the Act which may have particular relevance to buying groups.

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