RÉPUBLIQUE FRANÇAISE

Autorité de la concurrence

Opinion No 10-A-26 of 7 December 2010 on affiliation agreements of independent retailers and the terms for acquiring commercial land in the food retail sector

English version

of the *Avis n° 10-A-26 du 7 décembre 2010 relatif aux contrats d'affiliation de magasins indépendants et les modalités d'acquisition de foncier commercial dans le secteur de la distribution alimentaire*

The *Autorité de la concurrence* (section III),

Considering the decision no. 10-SOA-01 of 25 February 2010 starting a sector enquiry at its own initiative, relating to affiliation agreements of independent retailers and the terms for acquiring commercial land in the food retail sector, registered under no. 10/0017 A;

Considering Articles 101 and 102 of the Treaty on the Functioning of the European Union;

Considering Book IV of the Commercial Code concerning free prices and competition;

Considering the other documents of the file;

The Case Officers, the General Rapporteur and the Government Commissioner heard during the session held on 13 October 2010;

The representatives of *Groupe Casino, Groupe Carrefour, Système U, Groupe Auchan, E. Leclerc* and *Lidl* heard on the grounds of the provisions set forth in Article L. 463-7 of the Commercial Code;

Hereby adopts the following opinion:

Disclaimer

The *Autorité de la concurrence* provides the present translation into English of its ***Avis n° 10-A-26 du 7 décembre 2010 relatif aux contrats d'affiliation de magasins indépendants et les modalités d'acquisition de foncier commercial dans le secteur de la distribution alimentaire*** to enhance public access to information about its advisory and decision-making practices.

Only the French version is deemed authentic. The *Autorité de la concurrence* accepts no responsibility or liability whatsoever with regard to this translated document.

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I. Introduction

1. Article L. 462-4 of the Commercial Code provides as follows: "*The Autorité de la Concurrence may take the initiative of issuing an opinion on any question relating to competition. The said opinion is made public. It may also recommend that the Minister in charge of the economy or the Minister in charge of the relevant sector implement the required measures to improve markets' competitive operating*".

2. In its self-referral decision no. 10-SOA-01, the *Autorité de la Concurrence* stated that it wished to deal with the possible obstacles to competition, in the retail of daily consumer goods sector, posed by affiliation and franchise agreements on the one hand, and the terms for managing commercial land on the other. The self-referral decision states that the enquiry shall cover retailers of daily consumer goods (food and non-food products) and convenience shops. It emphasises that this analysis shall cover, in particular, local customer catchment areas.

3. Indeed, both the economic analysis and the statistical studies show the role played by the degree of market concentration in customer catchment areas on the level of retail prices. Several reports have moreover emphasised the high degree of market concentration in some customer catchment areas in the food retail sector. In its opinion no. 07-A-12, the *Autorité de la Concurrence* highlighted the role played by the specific regulation on retail planning introduced by the *Royer* and then *Raffarin* laws on the excessive concentration observed in some of these areas. By increasing the threshold for large supermarkets from 300 to 1,000m^2, above which administrative authorisation is necessary to open a new shop, the reform of retail planning introduced by the *loi de modernisation de l'économie* (law on the modernisation of the economy) has started to lower some of the regulatory barriers to the entry of new competitors in these concentrated customer catchment areas.

4. Nonetheless, the obstacles to entry can also arise from the conduct of operators. In particular, opinion no. 07-A-12 mentioned above had noted the significant role played by the management of commercial land in the operator entry process. In this case, some pointed out the strategies of "property freeze" implemented by competitors already established in customer catchment areas, consisting of holding unused property with the aim of preventing or making the establishment of competing shops less profitable. This opinion thus intends to deal in a more detailed manner with the frequency of such conduct, the various procedures involved and appropriate responses to it.

5. Moreover, given the major obstacles to the creation of new shops, one of the possible responses to the excessive concentration in customer catchment areas lies in the power competing operators may have to attract independent retail outlets affiliated to competing retail chains to their networks. In this way, a customer catchment area with, for example, five shops affiliated to two retail chains, could continue to accommodate five shops, but which are henceforth linked to three retail chains, thereby reducing the degree of market concentration in this customer catchment area and increasing competition for the benefit of the final consumer. Similarly, the mobility of independent retail outlets between retail chains could assist the entry of a foreign retail chain and could even intensify competition in the national market and reduce the concentration of central purchasing bodies. On the other hand, if the contracts binding independent retail outlets to retail chains are likely to restrict this mobility and if the market share of operators bound in this way is significant, the possibility of entry would be limited and the intensity of competition reduced. Only sufficiently high efficiency gains, in terms of the transfer of know-how or investment

incentives, for example, could then offset these restrictive competition effects. In this context, the purpose of this opinion is to assess the features of the various contracts binding independent retail outlets to their head of network, the restrictions to competition that are likely to result and how they should be dealt with.

6. On a preliminary basis, the *Autorité de la concurrence* reiterates that, in the framework of an enquiry started at its own initiative, it is not entitled to classify a conduct on a market according to Articles 101 and 102 of the TFEU and Articles L. 420-1 and L. 420-2 of the Commercial Code. Only the implementation of a fully adversarial procedure, as provided for in Article L. 463-1 of the Commercial Code, would allow the *Autorité* to make such an appreciation.

7. After presenting the main features of the French retail of daily consumer goods, particularly with respect to the organisation of its main operators, the concentration of customer catchment areas and barriers to entry observed (part II), the opinion shall list, respectively, practices observed in respect to commercial land management and the *Autorité de la concurrence*'s recommendations in this regard (parts III and IV). It shall then focus on an analysis of the practices observed in respect to the affiliation agreements of independent retailers with retail chains and the *Autorité de la Concurrence*'s recommendations in this regard (parts V and VI).

II. The French retail grocery sector

8. The main economic data about the retail of daily consumer goods sector (A), the main operators and their mode of operation (B), the degree of market concentration in the sector (C), the development prospects of operators (D) and barriers to entry (E) shall be presented below.

A. MAIN SECTOR ECONOMIC DATA

9. In 2008, large food retailers (including hypermarkets, supermarkets and discount retailers) supplied more than two thirds (67.3%) of the food product market (excluding tobacco), with specialist food shops and small retail businesses (bakeries, butchers, delicatessen shops) supplying around one sixth (16.6%). Small food retailers and frozen food shops represent 8.4% of the food product market. In 2006, 5,900 large food retailers made a turnover of 170.7 billion euros[1].

10. Large food retailers are divided into two main formats. Supermarkets, defined as primarily food retailers with a retail area of less than 2,500m^2 and greater than 400m^2, including discount retailers, which represent 41% of the sector's turnover. Hypermarkets, defined as primarily food retailers with a retail area greater than 2,500m^2 offering a wider range of non-food products than supermarkets, represent 56%[2]. With respect to the number of shops

[1] Source: INSEE, *Le commerce en France*, 2009 edition
[2] Source: INSEE, *Le commerce en France*, 2009 edition

and retail area, in 2009 France had 1,667 hypermarkets (17 of which were created between 2004 and 2009, an increase in numbers of 1% in this period) with a total retail area of 9.3 million m^2. There are furthermore 5,437 supermarkets (of which 345 were created between 2004 and 2009, i.e. an increase of 7%) with a total retail area of around 7 million m^2 and 4,531 discount retailers (of which 1,001 were created between 2004 and 2009, i.e. an increase of 28%) with a total retail area of 3.3 million m^2[3].

11. Local food retailers (grocery shops, minimarkets and frozen food shops) represent 17,600 companies with 19,400 points of sale. The turnover of grocery shops and minimarkets was 7.2 billion euros, i.e. 3.5% of the turnover of food retailers[4]. According to figures from *INSEE* (National Institute for Statistics and Economic Studies), the number of grocery shops has fallen six fold in just over thirty years, going from 87,000 companies in 1966 to 14,100 in 2006. Nonetheless, since 2000, the number of grocery shops (less than $120m^2$) and minimarkets (between 120 and $400m^2$) has risen by around one hundred each year, i.e. an increase of almost 1,000 units between 2000 and 2008 (+ 8.4%). This increase is essentially brought about by minimarkets, the number of which has grown by 25.5%[5] in this period. Since 2005, turnover has fallen by 1 to 2 points each year, largely due to competitive pressure from discount retailers and small town centre supermarkets (between 400 and $1,000m^2$ of retail area).

12. Until 2004, the hypermarket and supermarket formats were growing; their market share has since stabilised at 67%. This growth was essentially achieved at the expense of specialised food shops, whose market share fell from 22% to 16% between 1993 and 2008, and small food retailers, whose market share fell from 12 to 9%. The other major trend is the rise in the growth of hard discount retailers. According to the hard discount retailers who were interviewed, the rise in the notification threshold to open shops has significantly increased their ability to set up. Moreover, added to a new growth in the demand for local shops, this reform also boosted operators' interest in this format, described by several operators as a new vector of growth.

13. Paris is a case apart. The lack of hypermarkets, particularly for reasons of town planning in the city of Paris itself, the high cost of commercial land and the low density of food shops are the main characteristics of Paris. Nonetheless, the presence of hypermarkets at its immediate periphery meets, in a very limited manner, a particular consumer demand. It should also be mentioned that the competition occurs between relatively small distribution formats (minimarkets and small supermarkets, mainly) largely owned by two groups, *Casino*, operating in particular under the retail-brand *Monoprix* (owns 50% with the *Galeries Lafayette* group) and *Carrefour*.

14. The pricing policy of the retail of daily consumer goods (supermarkets and hypermarkets) shops has been subject to many criticisms. According to several works[6], the *Galland* Law encouraged a general rise in prices, detached from the price variations found in neighbouring countries and thus, largely, in the prices of commodities. However, it remains difficult to define the respective responsibilities of manufacturers and distributors in this price rise process. The repeal of the *Galland* Law (Law no. 2008-3 of 3 January 2008 on the development of competition for the benefit of consumers, called the

[3] Source: Xerfi, *Grandes surfaces alimentaires*, November 2009
[4] Source: INSEE, *Le commerce en France*, 2009 edition.
[5] Source: XERFI, *Epiceries et supérettes*, March 2010.
[6] In particular, listed by M.L. Allain, C. Chambolle and T. Vergé, *La Loi Galland sur les Relations Commerciales: Jusqu'où la Réformer?*, Cepremap, Editions ENS-Rue d'Ulm, 2008.

"*Châtel* Law"), then the removal of the prohibition of discrimination from suppliers (Law no. 2008-776 of 4 August 2008 modernising the economy, called "*LME*"), paved the way for a return to price competition between retail-brands[7], although it is still not possible to separate, in the process of price stabilisation, the current crisis in the global economy and the legislative reform started since 2007. In fact, while negotiations between manufacturers and distributors appear to have become tougher, the repercussion of possible purchase price reductions obtained by distributors would be, as in the past, unequal in extent depending on the type of product[8]. This could indeed depend on several factors, such as the ease of storing products, brand awareness, or the degree of competition in customer catchment areas. Moreover, the degree of competition observed in local customer catchment areas, where one finds the real competition between retailers, should also be a factor determining the extent of this repercussion[9].

B. THE MAIN OPERATORS AND THEIR MODE OF OPERATION

1. THE MARKET SHARE OF OPERATORS AND RETAIL-BRANDS

15. The food retail distribution sector is highly concentrated, similar to an oligopoly. In the first half of 2009, the six main groups, all French (*Auchan, Carrefour, Casino, E. Leclerc, ITM Entreprises* and *Système U*) held nearly 85% of the market share.

[7] According to several observers (see, for example, the report of the *Commission des Affaires économiques* (Economic Affairs Commission) of 8 July 2009), the LME allowed greater differentiation between the purchase price and thus the resale prices of major retail-brands. With a market share increase of 0.7 points between the first half of 2008 and the first half of 2009, the *Leclerc* co-operative group experienced the greatest increase in the sector. Other co-operative groups (*Intermarché* and *Système U*) both gained a 0.3 point market share. By being able to stabilise its market share, *Carrefour* had the best performance of the integrated groups, unlike *Casino*'s hypermarkets and discount formats (source: Xerfi, *Grandes surfaces alimentaires*, November 2009).

[8] See *Rapport sur la formation des prix alimentaires* by the State Secretariat for forecasting, and assessment of public policies and the development of the digital economy, 2008.

[9] "Quel est l'impact de la concurrence des surfaces de type discount sur les prix des hypermarchés à dominante alimentaire?", K. Berger, *Revue de la Concurrence et de la Consommation* no. 139, 2004.

GROUP	RETAIL-BRAND(S)	FORMAT	NUMBER OF SHOPS	MARKET SHARE (TNS estimate – December 2009)
Aldi (fully integrated family-run group)	Aldi	Discount	854	2.5 %
Auchan (integrated family-run group; development of the franchise using a supermarket format)	Auchan	Hypermarket	130	8.6 %
	Atac	Supermarket	5	2.5 %
	Simply Market	Supermarket	209	
Carrefour (listed group, integrated into the hypermarket format, "mixed" into the supermarket format and developing the franchise as local shops as well)	Carrefour	Hypermarket	231	13%
	Carrefour Market / Champion	Supermarket	987	8.4%
	Carrefour City / Carrefour Contact / Shopi / 8 à Huit / Marché Plus / Proxi	Grocery shop/ Minimarket	3 165	/
	Ed / Dia	Discount	928	2.5%
Casino (listed group, integrated into the hypermarket format, "mixed" into the supermarket format and developing the franchise as local shops as well with a very strong emphasis on the status of agent-manager)	Géant Casino	Hypermarket	122	3.2%
	Casino Supermarché	Supermarket	390	2.2%
	Petit Casino / Spar / Vival / Franprix	Grocery shop/ Minimarket	5 254	/
	Leader Price	Discount	559	2.7%
Cora (integrated group)	Cora	Hypermarket	59	2.5%
	Match	Supermarket	155	0.8%
E. Leclerc (co-operative group)	E. Leclerc	Hypermarket	540	16.9%
	E. Leclerc	Supermarket	78	
	Leclerc Express	Grocery shop/ Minimarket	57	/
ITM Entreprises (co-operative group)	Intermarché	Hypermarket/ Supermarket	1 488	12.1%
	Ecomarché	Supermarket	296	
	Netto	Discount	382	0.9 %
Lidl (integrated group)	Lidl	Discount	1 518	4.8%
Monoprix (50% *Casino*/ 50% *Galeries Lafayette)* (largely integrated group)	Monoprix	Supermarket/ Local shop	285	2.2%
Système U (co-operative group)	Hyper U	Hypermarket	59	9.1%
	Super U	Supermarket	727	
	Marché U	Supermarket	109	
	U Express	Grocery shop/ Minimarket	128	/
	Utile	Grocery shop/ Minimarket	241	/

Market shares of the main retail chains in 2009

Food retail chain	Market share (TNS Worldpanel estimate, 2009)
CARREFOUR	23.9%
LECLERC	16.9%
INTERMARCHE	13.6%
AUCHAN	11.1%
CASINO	10.3%
SYSTEME U	9.1%
PROVERA (CORA)	3.3%

16. As highlighted in the tables above, *Carrefour* and *Casino* occupy a dominant position within the three shop formats: hypermarkets, supermarkets, including discount retailers, and local retailers. The *Leclerc, Auchan and Système U* groups, major operators in the hypermarket and supermarket formats, are hardly present in the local shop market. Even more specialised, the *Cora* group is mainly present in the hypermarket format, whereas the *Intermarché* group is almost exclusively present in the supermarket format, including the discount sector (with the *Netto* brand). Finally, discount operators are exclusively present in these types of shops.

2. MODES OF OPERATION OF RETAIL CHAINS

17. Retail of daily consumer goods groups either operate as co-operatives or use the integrated (or "company with branches") model. The groups that have opted for integration are listed (*Casino, Carrefour*), family-run (*Auchan*) or foreign (*Lidl* and *Aldi*). The *E. Leclerc, ITM Entreprises and Système U* groups opted for the co-operative model. As part of their development, most integrated groups also rely on franchises, in particular *Carrefour* and *Casino* for the supermarket and local shop formats.

18. Given the variety of organisational and contractual models encountered in the scope of this sector enquiry, the generic terms "independent retail outlet" and "affiliated retail outlet" refer to all shops affiliated to a retail chain and operated by independent traders, responsible for the running of the shop(s) of which they are the managers. They are thus either independent retail outlets affiliated to a national or regional co-operative group or independent retail outlets affiliated to an integrated group through a franchise or similar agreement, and/or a lease management agreement.

19. Co-operative groups or, more specifically, groups of associated traders, are businesspersons' associations which are legally and financially independent of each other, with a specific legal status (in general, a public limited co-operative company of traders with variable capital - Articles L. 124-1 et seq. of the Commercial Code). Such a group is managed by shareholders who are members of the co-operative and also own the points of sale, under a system of democratic governance ("*one member, one vote*"), formalised by

articles of association and bylaws[10], under common rules of operation. These two documents provide the legal basis of any co-operative group. In some groups, they may be supplemented by other legal documents which allow the rights and obligations of each party to be legalised (retail-brand agreement or membership agreement, for example).

20. The purpose of the group is the pooling of resources (central buying body, retail-brands and sales concept, trade policies, financial resources, etc.) for the joint development of tools and activities that ensure that points of sale are competitive. One of the joint resources developed by the group members is the central purchasing body[11]. This body manages the purchases of its affiliates by offering them the following services: product study, supplier research, purchase negotiation and in some cases, distribution, organisation and documentation work. Based on the principle of "exclusive rights for cooperatives" provided by law, these services are reserved for the exclusive use of members of the central purchasing body, to which they are bound by contract. The horizontal structure of the group of distributors-retailers may thus be added to a vertical relation linking retailers and their central purchasing body. Other agreements may legalise a similar type of vertical relation, such as product sign, retail-brand, affiliation[12] or franchise agreements[13].

21. In the end, independent retail outlets are thus free to make decisions on their commercial policy (price, product mix, advertising) within the limits of the commercial policy decided by the group and specified in its articles of association and working rules. On the other hand, in an integrated retail chain, the shop is owned and managed by the retail chain which alone decides the shop's commercial policy and relies on an employee to carry it out. For some formats, nonetheless, it appears preferable to give greater freedom to the shop manager, in order simultaneously to increase his incentive to perform and to benefit from the best information he has about local market conditions. The retail chain must thus franchise shops, which will have been contributed by businesspersons or which it has contributed to setting up itself. In some cases, the retail chain owns the premises or the property on which the shop is opened. It may also be a partner in the operating company managing the franchise retailer.

22. Given the combination of retailers operating under the co-operative model and retailers using the franchise model, "independent" retailers, understood to be those operated by a company independent of a retail chain or only a member of one, represent the majority of retail-outlets in the three distribution formats. Thus, the main retail chains in the sector have declared that they operate a total of 1,376 hypermarkets of which 871, i.e. 63.3%, are affiliated retail outlets operating under the co-operative model. Very few hypermarkets are franchised. The place of "independent" retailers is even more marked in the supermarket (excluding discount shop) format: out of a total declared by the various operators

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[10] Thus, *ITM Entreprises*, a simplified joint stock company, is held in full by a non-trading partnership, *la société civile des Mousquetaires*. Members of the *société civile des Mousquetaires* are all members who operate a point of sale, each with the same voting right, according to the principle of "*one man, one vote*".

[11] Unlike central purchasing bodies, purchasing pools ("*centrales de référencement*") do not purchase products; they merely select products or suppliers from whom members of the network can purchase products at agreed prices.

[12] Some co-operative groups now accept "*allied members*", who have signed trademark license agreements, for example with the *E. Leclerc* group, under Articles 6 and 6a of its articles of associations, usually called "*affiliates*".

[13] By way of example, *ITM Entreprises* has the status of franchisor and makes, in this way, brand name agreements similar to franchise agreements with companies held by members to allow them to run shops under one or another of the retail-brands of the *Mousquetaires* group.

questioned during the enquiry of 4,599 supermarkets, 1,353, i.e. 29.4% are integrated retailers and 3,246, i.e. 70.6%, are affiliated or franchise retailers. Finally, with respect to local shops, the various retail-brands questioned run a total of 9,995 local retailers, of which 2,309, i.e. 23% are integrated retailers and 7,686, i.e. 77% are independent retail outlets. Lastly, only the discount sector is largely operated by integrated retailers: out of a total of 4,241 shops declared, 3,500, i.e. 82%, are integrated (*Aldi* and *Lidl* groups) and 741, i.e. 18%, are affiliated retail outlets, essentially under the *Ed* (*Carrefour* group), *Leader Price* (*Casino* group) and *Netto* (*Intermarché* group) retail-brands.

C. DEGREE OF MARKET CONCENTRATION IN THE SECTOR

23. Several methodological considerations shall first be presented concerning the definition of markets and the degree of competition likely to exist between independent retail outlets operating under the same retail-brand (1), and then the findings from the use of public databases or based on information provided by particular sector operators shall be presented (2). The statistical tables describing the structure of customer catchment areas, taken from databases produced during the enquiry, are provided in an appendix.

1. METHODOLOGICAL CONSIDERATIONS ON THE DEGREE OF MARKET CONCENTRATION IN CUSTOMER CATCHMENT AREAS, DEFINITION OF THE RELEVANT MARKETS AND COMPETITION BETWEEN INDEPENDENT RETAIL OUTLETS UNDER THE SAME RETAIL-BRAND

24. The methodological clarifications made below concern the reference index used to assess the degree of market concentration of a market (a), the definition of the relevant markets (b) and the degree of competition likely to exist between independent retail outlets operated under the same retail-brand (c).

a) The index frequently used by competition authorities to measure the degree of competition in a sector is the Herfindhal-Hirschman Index

25. To measure the degree of competition likely to exist in a relevant market, the competition authorities frequently rely, as a first estimate, on the calculation of the Herfindhal-Hirschman Index or HHI[14]. It is defined as the sum of the square of the market share of market operators: thus, the use of the data in the table in paragraph 15 leads to a HHI of 1,365 ($23.9^2 + 16.9^2$ + etc.).

[14] See *Horizontal Merger Guidelines (for public comment)*, Federal Trade Commission and US Department of Justice, 2010; Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentration between undertaking, European Commission, 2004/C 31/03; *Lignes directrices de l'Autorité de la concurrence relatives au contrôle des concentrations*, Autorité de la concurrence, 2009.

26. The HHI level thus depends on two factors: the number of operators, as the fewer there are, the higher their respective market shares will be and the imbalance in the market share between these operators, with the weight of a major operator being over-weighted by the multiplication of its market share by itself. Thus, the lower the number of active operators in a market and/or the more their market shares are unequal, the higher the HHI is.

27. By way of illustration, the new merger control guidelines by the American competition authorities offer a classification of markets into three types[15]: low-level concentration when the HHI is less than 1,500, concentration at an intermediate level when the HHI is between 1,500 and 2,500 and highly concentrated when the HHI is over 2,500. In a relatively similar manner, the *Autorité de la concurrence*, like the European Commission, considered, in its merger control guidelines, that "*it is unlikely that an operation will raise horizontal competition issues in a market where the HHI after the merger will be less than 1,000. These markets normally do not require an in-depth investigation. It is also unlikely that the Commission will determine the existence of horizontal competition issues, when the HHI at the end of the operation is between 1,000 and 2,000 and the delta is less than 250, or when the HHI at the end of the operation is higher than 2,000 and the delta is less than 150. For vertical or conglomerate mergers, it is unlikely that an operation will raise competition issues if the HHI after the operation is less than 2,000*".

28. Based on these various findings, a midway HHI of 2,200 was thus used in this opinion to identify concentrated customer catchment areas. In accordance with the decision-making practice of competition authorities in this sector, market share is measured on the basis of the sales area of shops and not their turnover.

b) Definition of relevant markets in the retail distribution sector

29. Thus, as has already been mentioned, the French retail of daily consumer goods sector is relatively concentrated: in the first half of 2009, the six main groups, all French (*Auchan, Carrefour, Casino, E. Leclerc, ITM Entreprises* and *Système U*) together held nearly 85% of the market share. Nonetheless, the Herfindhal-Hirschman Index calculated based on the market share data provided in the "Market shares of the main retail chains in 2009" table (see paragraph 15) is "only" 1,365, a value relatively remote from the thresholds beyond which the intensity of competition could, at first glance, be considered limited.

30. Nonetheless, the market share of retail chains, nationally and for all types of shops, is only useful to provide a summarised measure of the concentration of the sector and to measure the market share of "suppliers" of shops: the various central purchasing bodies and purchasing pools of retail chains. In this case, it may thus appear that in this "upstream" market, the intensity of competition amongst the various retail chains to supply independent retail outlets and/or make them their franchises is thus potentially significant, subject nonetheless to contracts linking independent retail outlets to their heads of network, allowing such competitiveness.

31. From the consumer's perspective, on the other hand, this measure of concentration may appear unsatisfactory as it does not take into consideration the distinction by the different

[15] See *Horizontal Merger Guidelines (for public comment)*, Federal Trade Commission and US Department of Justice, 2010, p.19.

types of shops and geographic areas of the relevant market where the demand of individual consumers is found.

32. Thus, while the "upstream" markets have a real national dimension, the downstream markets have a local dimension due to costs and transport times incurred by individual consumers when travelling to shops. In fact, the relation between price levels and intensity of competition in the customer catchment area has been the subject of several studies[16]. There are two types of conclusions. Firstly, the intensity of local competition effectively influences the price level noted in shops. Secondly, the entry into force of the *Galland* Law has reduced the strength of this relation: indeed, as negotiations thus essentially covered the level of back margins, the profit-loss threshold could not take their profits into consideration and shops thus only had a limited margin to manoeuvre to reduce their prices if competition in the customer catchment area was strong. On the contrary, by allowing the free negotiation of prices and by allowing the consequences of tariff benefits obtained by central purchasing bodies in the shops' resale prices, the reform of supplier-distributor relations brought in by the *loi de modernisation de l'économie* (law on the modernisation of the economy) should logically lead to a strong variation in sales prices according to the degree of competition observed in the customer catchment area.

33. In its recent decisions[17] on mergers concerning hypermarkets and supermarkets, the *Autorité de la concurrence* stated that, according to the type of retailer concerned, the conditions of competition should be assessed in two different areas: i) a first area in which consumer demand in an area and the offer by hypermarkets to which they have access in under 30 minutes by car are met and ii) a second area in which consumer demand and the offer by supermarkets and other equivalent types of retailers, situated at least 15 minutes away by car are met; other types of retailers may include, in addition to supermarkets, hypermarkets and discount retailers. Finally, in its decision no. 10-D-08 on practices implemented by *Carrefour* in the local food retail sector, the *Autorité de la concurrence* defined a relevant market for local food retail as including all retailers with a sales area of less than 1,000m^2 and hard discount retailers[18].

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[16] K. Berger (2004), "Quel est l'impact de la concurrence des surfaces de type *discount* sur les prix des hypermarchés à dominante alimentaire?" *Revue de la concurrence et de la consommation*, July, August, September 2004, no. 139. P. Biscourp, X. Boutin and T. Vergé, "The effects of retail regulations on prices: evidence from French data", working document, 2008. UFC-Que Choisir (2008), "Concurrence locale sur les zones de chalandise et niveaux de prix: quelle relation?" The role of local competition on price levels has also been demonstrated in the case of the British retail markets for food products at supermarkets: see *Competition Commission* (2009) *Grocery Report.*

[17] See, for example, decision no. 10-DCC-124 of 6 October 2010 on the exclusive takeover of *Chepar* by *ITM Alimentaire Sud Est*, paragraph 11.

[18] Other criteria may nonetheless be taken into account to assess the impact of concentration on the competition situation in the retail distribution market, which could lead to refining, in this case, the usual definitions provided above. In particular, the distinction between these three formats – hypermarket, supermarket and local retailer – is thus not always easily understood based only on sales area figures.

c) On the degree of competition likely to exist between independent retail outlets with the same retail-brand

34. In order to grasp the extent of the competition shops affiliated to the same retail-brand and established in the same customer catchment area will resort to, the *Autorité de la concurrence'*s merger control guidelines state (paragraph 594 et seq.): "*The notions of decisive influence and of market power do not take in one another. As such, even if the network head does not control the store operated by a member (franchisees, dealers, cooperating members...), the latter's sales can be included with those of the stores operated by the network head itself for the purposes of the competitive analysis, on the basis of the degree of autonomy of the commercial policy implemented by the network's independent members. On a case-by-case basis, the* Autorité *examines whether one must consider that, within a single trade area, the stores controlled by the network head, on the one hand, and those operated under the same trade name but not controlled by the network head, on the other hand, are likely to exert competitive pressure on one another.*".

35. In fact, while, theoretically, independent retail outlets operating under the same retail-brand also compete with each other by using their freedom to define their commercial policy, several factors are likely to limit the intensity of this competition. Firstly, a shop's commercial policy is not limited to pricing policy: they also include product mix, advertising, customer loyalty, retail-brand and image, etc. policies. Moreover, in these various aspects, the head of network is able to influence significantly, i.e. determine, the strategy followed by independent retail outlets. Thus, most often, the head of network defines a common product mix for all shops operated under the same retail-brand, which they are then obliged to use, in order to comply with the common image and identity of the retail-brand. In particular, the policy followed with respect to private label products must be uniform for all of independent retail outlets operating under the same retail-brand. These outlets cannot list products by competing brand-labels.

36. Secondly, the pricing freedom of independent retail outlets is reduced by at least two factors. On the one hand, since the law of 15 May 2001 on the new economic regulations (*"loi NRE"*), co-operative groups can apply common prices throughout the year *"through the implementation of promotion campaigns – which include, or not, advertising – that may include common prices"*. On the other hand, independent retail outlets, whether they are co-operative members *(membres d'un groupement cooperatif)* or a franchise of an integrated group, are mainly supplied (see below paragraphs 73 et seq.) by the central purchasing body or purchasing pool of the group. By controlling the purchase price of a very large number of products sold by independent retail outlets, the retail chain thus partly controls their commercial policy and the ability of independent retail outlets to compete with each other or with integrated retailers within the same group.

37. For these various reasons, the concentration of retail markets can be grasped at the level of the retail chain, given that independent retail outlets affiliated to the same group do not put the same competitive pressure on each other as do independent retail outlets or retailers which are part of competing retail chains. Furthermore, to these key reasons, a practical difficulty can be added: except hypermarkets, very few of which are operated as franchises, it has been impossible to identify, in each customer catchment area, the franchise retailers and integrated retailers and thus to calculate the concentration indices that distinguish independent retail outlets from integrated retailers.

2. ON THE DEGREE OF MARKET CONCENTRATION OBSERVED IN CUSTOMER CATCHMENT AREAS

38. Both the studies by *UFC-Que Choisir* (French consumers association) and *Asterop* (market research company) (a) and the statistics drawn up based on the *LSA Focus Alimentaire* (market research report) and data provided by operators (b) come to the conclusion that there is a high degree of market concentration in the food distribution sector.

a) A high degree of market concentration in customer catchment areas according to the *UFC-Que Choisir* and *Asterop* studies…

39. The concentration of customer catchment areas has already been the subject of two studies which both conclude that it is high. Thus, in 2008, the *Union Française des Consommateurs - UFC* (French consumers association) published a study which concluded that, out of 634 customer catchment areas studied, "*26.9% of areas are potentially competitive, 36.9% have medium levels of competition and 32.9% are not*"[19]. An area with medium levels of competition has, in addition to a hypermarket at the centre of the area, two hypermarkets in the primary area or four hypermarkets in the secondary area. Nonetheless, the definition of customer catchment areas used by the *UFC* does not correspond to that used in competition law[20] and it is probable that these are relatively more extensive[21]. Moreover, competitive intensity is measured by counting the number of hypermarkets without taking into account their sales area.

40. The same year, a study by the geo-location firm *Asterop*[22] also concluded that there was a poor degree of competition in customer catchment areas in the retail of daily consumer goods. This study defined customer catchment areas as a living area organised around a "centre of local attraction"[23]. France is thus divided into 629 living areas in which four competitive situations were distinguished: "*leadership*", "*two-way*", "*three-way*" *and* "*four-*

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[19] UFC-Que Choisir (2008), "Concurrence locale sur les zones de chalandise et niveaux de prix: quelle relation?"

[20] In practical terms, the customer catchment area covered by the *UFC-Que Choisir* study is supposed to consist of a "primary" area and a "secondary" area. "*The primary area is defined as the area which allows the theoretic potential of the hypermarket to be met, of 2.71 households per square metre. To be more specific, in the primary area, there is an average of 2.71 households per square metre, which provides the standard to be met by a hypermarket as this is representative of what is observed nationally. Indeed, this figure is obtained by comparing, for the whole of France, the total number of m^2 in hypermarkets and the number of households covered, i.e. 80% of the total population. The primary area is the most important, the closest and it provides the main part of turnover. Consequently, competition is most harmful to the latter. The secondary area is defined as the area which allows, in total, a possible 50% extra households than those only in the primary area. Retailers situated in the secondary area are thus going to compete at the point of sale but will not have the same impact on its profits*".

[21] Indeed, the report states that it hardly takes into account hypermarkets situated more than ten minutes away from the hypermarket situated at the centre of the area (p. 8) even though, in the case of hypermarkets, the radius of a customer catchment area in competition law is around a 30-minute car journey, thus, based on a driving speed of 50km/h, it is a radius of around 25 km.

[22] *Local Enseignes GMS* study, March 2008.

[23] "*A "centre of local attraction" is distinguished by a large number of jobs, shops and services available (including sovereign services). A living area is thus considered an independent area from the perspective of all daily-life activities (work, study, shopping, leisure, etc.). The concept of a living area was created following work by INSEE (National Institute for Statistics and Economic Studies) on residential catchment areas which aim to organise rural areas around local centres that have an attracting power over the communes around them. ASTEROP has extended this approach to urban areas and all retail activities*".

way" *situations*[24]. 58% of areas had a "*leader*" situation, 30% a "*two-way*" situation, 9% a "*three-way*" situation and 2% a "*four-way*" situation. Nonetheless, the classification of market structures used may appear to be excessively restrictive, as an operator would be considered a "leader" once its market share exceeded 25% and that of its closest competitor is lower by more than 10 or 15%: it is thus an extremely flexible definition of market power or dominant position.

41. The *Autorité* has thus sought to refine, in different ways, this measure of the degree of market concentration in customer catchment areas in order to make the measurement methods more consistent with those used in competition law and more comprehensive, in particular integrating the local retailers and supermarket formats.

b) …confirmed by data gathered while preparing the opinion

The databases used

42. Several databases were used to assess the degree of market concentration of customer catchment areas, which differ, in particular, according to the format studied and how it was created.

43. Thus, for hypermarkets, two databases were used.

44. The first is taken from *Focus Alimentaire LSA* (market research study). This describes 629 living areas defined according to *Asterop's* "centre of attraction" method (see above, paragraph 40), by mentioning, in particular, the main retail outlets in the area, their size and retail-brand, as well as an estimate of the potential demand in the area. However, *Focus Alimentaire LSA* only offers a survey of the hypermarkets found in 208 of these areas. In practice, this survey is possible when their number is limited; in the other case, only the largest hypermarkets are described, making it impossible to calculate the market share by retail area in the area.

45. The second is taken from the statements made by operators. Four of the main retail of daily consumer goods (supermarkets and hypermarkets) operators thus described the customer catchment areas in which one of their hypermarkets has a market share, by sales area and by adding the market share of different shops in the retail chain in the area, of more than 30%. The definition offered of customer catchment areas is that adopted by the *Conseil* and then the *Autorité de la concurrence* and summarised above, however with customer catchment areas being delimited around the hypermarkets and supermarkets considered[25].

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[24] A "leader" situation is that in which the main operator in the area has a market share of over 25%, and more than 15 points more than that of the next competitor immediately following it if its market share is more than or equal to 40% or 10 points if its market share is less than 40%. A "two-way" situation is one in which, without an identifiable leader, two actors share the main part of the market. A "three-way" or "four-way" situation is one in which, without a leader or a "two-way" split, 3, 4 or more actors are present.

[25] The economically most relevant definition of customer catchment areas centred on residential catchment areas was dismissed by operators insofar as the identification of the main residential catchment areas for each hypermarket or supermarket would have led to far higher delays in responses.

46. A similar database was used for the description of customer catchment areas corresponding to the supermarket format, whose degree of market concentration has never yet been the subject of assessment. Nonetheless, only data transmitted by two retail chains could be used.

47. Lastly, the local food retailer format was also studied, based on statements by operators. The request for information sent to them was considered a sample of French cities with more than 25,000 inhabitants. More specifically, on the one hand, it listed cities with more than 100,000 inhabitants (37 cities) and on the other hand randomly selected 130 cities with populations of between 25,000 and 100,000 inhabitants. Relying on the definition of the market concerned by the *Autorité de la concurrence* in its decision no. 10-D-08, the request for information aimed to identify market share by the sales area of shops of the respondent retailers and their competitors in the retail of daily consumer goods market for shops with an area of between 0 and 1,000m^2, accessible on foot. The resulting database thus provides the number and market share by sales area of shops established in these communes[26].

The limitations of their use

48. None of the databases used is free of limitations and this should be borne in mind when interpreting the results. In particular, the common limitation of the databases used to assess the degree of market concentration was to only use a sample of customer catchment areas.

49. In the case of hypermarkets and supermarkets, the sample is biased and is likely to increase the degree of market concentration as only areas with a limited number of hypermarkets (case of the *LSA-Focus alimentaire* database) or in which a retail chain straightaway has a market share greater than 30% (case of databases on hypermarkets and supermarkets taken from statements by retail chains) were studied. To make up for this bias, the number of concentrated customer catchment areas identified is considered with respect to the total number of shops or areas in France. Thus, the figures provided must be considered as reducing the real degree of market concentration in customer catchment areas.

[26] Due to the statistical availability of data, shops with an area of less than 100m^2 were not considered in the database. On the other hand, all the shops established in a commune, both town centre shops and those on the outskirts, were included. As a consequence, the database thus includes many discount retailers. Lastly, *Monoprix* shops, whose area is usually larger than 1,000m^2, were only included up to an area of 1,000m^2, roughly reflecting the share of food products in their turnover, and entered in the accounts of the *Casino* group, in accordance with the letter of the Minister of Economy, Finance and Industry of 2 October 2000 to the board of *Casino* concerning the acquisition by this group of holdings in *Monoprix*'s capital. Taking the entire sales of *Monoprix* shops or the distinction between *Monoprix* shops and other retail-brands in the *Casino* group into consideration leads, respectively, to increasing and decreasing the level of concentration of the markets studied.

50. With respect to local shops, the sample used does not necessarily reflect the population structure and demand in French cities. In particular, the largest cities are naturally overrepresented. Once more, as the degree of market concentration tends to reduce with demand, the proportion of cities identified as having a concentrated local retail grocery market is reduced with respect to the actual level.

The degree of market concentration observed in customer catchment areas

51. Three parameters describing the competitive structure of the customer catchment areas included in the databases have been calculated.

- Firstly, the tables provided in the appendix to this opinion show the proportion of customer catchment areas in which a retail chain (among those who responded to the request for information) is likely to be dominant. These customer catchment areas likely to be dominated are defined restrictively as those in which the respondent retail chain owns more than 60% of the sales area in the customer catchment area, those in which they own more than 50% of these sales areas and in which no competing retail chain has more than 15% of this area, and finally, those in which the respondent retail chain owns more than 40% of the sales area in the area and in which none of the competing retail chains owns more than 10% of the area.
- Secondly, these tables also present the proportion of customer catchment areas whose market structure can be classified as duopolistic (the two main operators in the area own a market share of over 90 in the area studied) or oligopolistic (three or four of the main operators in the area own a market share in shop floor of more than 90% of the area studied).
- The tables also show the median concentration index calculated for the sample areas and the proportion of areas (calculated for all the shops in the respondent retail chains) for which the concentration index is higher than 2,200.

52. With respect to hypermarkets, between at least 4 and 9% of the customer catchment areas included in the databases are likely to be dominated by a single retail chain. At least 30% of the customer catchment areas described deal with fewer than four operators. Finally, at least 43% of the customer catchment areas have a HHI higher than 2,200 (see Appendices 1 and 2).

53. The degree of market concentration is lower for supermarkets. Indeed, in this format, taking into consideration discount retailers and hypermarkets more than makes up for the 15 minutes to the customer catchment area restriction. More specifically, the proportion of customer catchment areas in which two operators having responded to our request for information are likely to hold a dominant position is, at least, 3.7%. At least 14% of these areas only have four retail chains or less. Finally, at least 20% of customer catchment areas have two retail chains which responded to the request for information for this format with a HHI greater than 2,200 (see Appendix 3).

54. Finally, concerning the local retailer format, the proportion of communes in our sample in which a retail chain is likely to hold a dominant position is 14%. 21% of the communes studied have a triopoly market structure and 34% of them have a small oligopolistic structure with four operators. Finally, around 70% of the communes studied have a local food retailer sector in which four operators dominate more than 90% of sales area and 87%

of the communes sampled have a HHI higher than 2,200. Although not as high as in cities with more than 100,000 inhabitants, the degree of market concentration of local food shops remains significant: an operator thus holds a position that is likely to be classified as dominant in three of these cities, i.e. 8% of the sample, and four operators hold more than 90% of the market share in 40% of the 37 cities studied. The HHI is higher than 2,200 for 25 of these 37 communes with more than 100,000 inhabitants (see Appendix 4).

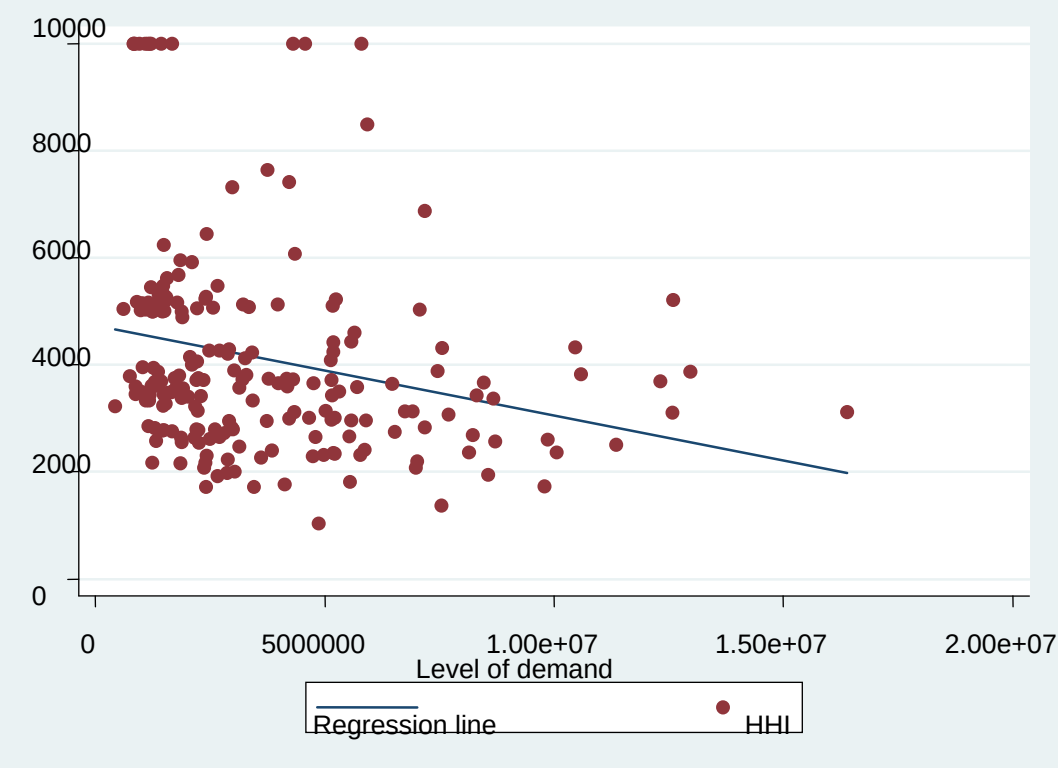
55. In this respect, Paris provides a particularly striking case. The main operator in local food shops in the capital, the *Casino* group, effectively holds a market share in sales area of more than 60%, whereas its closest competitor, the *Carrefour* group, has a market share of less than 20%. Thus, as there are at least eight retail chains in the capital, the Herfindhal-Hirschman Index almost reaches the exceptionally high threshold of 5,000. This market structure is partly based on the *Casino* group's (more than 40% of market share in sales area) acquisition of a stake in *Monoprix* (more than 20% of the market share in sales area) and the obstacle to new operators still posed by the high cost of commercial land in the capital, emphasised by almost all of the operators questioned.

The determining factors of the degree of market concentration observed

56. Demand, measured by the number of households in the customer catchment area multiplied by average income, has a considerable influence on the degree of market concentration in customer catchment areas.

57. By way of illustration, the diagram below shows, according to the level identified on the x-axis, the HHI by customer catchment area included in the database taken from the *LSA-Focus alimentaire* catalogue. A negative correlation can clearly be identified between the level of demand and degree of market concentration. Concurrently, nonetheless, it may also be noted that an identical level of demand may co-exist with highly differentiated degrees of concentration. Although the relationship between the level of demand and concentration may be less in particular cases, a similar observation may be made for each of the other formats: by attracting new operators, the size of demand tends to reduce the level of concentration observed in an area, but considerable inequalities may nonetheless be identified. Demand is thus not the only factor which explains the concentration of customer catchment areas.

Diagram: Level of demand and level of concentration of customer catchment areas in the database taken from the *LSA-Focus Alimentaire* catalogue



58. The databases produced based on statements by operators or the *LSA Focus alimentaire* catalogue also show the influence of retail chains on the degree of market concentration in customer catchment areas. Indeed, by way of illustration, if the *LSA Focus alimentaire* database is considered, it may also be noted that the average number of retail chains found in the 208 areas studied is 3.13, compared to the 7 retail chains (*Leclerc, Système U, Intermarché, Auchan, Carrefour, Casino* and *Cora*) which operate hypermarkets (i.e. with an area of over 2,500m^2). In particular, the number of shops in these areas is, on average, higher than one unit (4.3 shops per area on average). In other words, the degree of market concentration in customer catchment areas measured at the level of retail chains arises in part from the fact that a retail chain may hold or have affiliates in several shops in the same customer catchment area. In fact, the share of shops affiliated to the same retail chain established in the same customer catchment area is very high. By way of illustration, the *Leclerc* group has two or more shops in around a quarter of the 208 customer catchment areas taken from the *LSA Focus alimentaire* catalogue. The accumulated median market share of these shops is thus greater than 32%. Similarly, it may also be observed that the HHI median calculated in the customer catchment areas taken from statements by operators (Appendix 2) goes from 3,500 when the concentration rate is calculated for retail chains to 2,800 when it is calculated for shops. In other terms, if independent retail outlets were transferred to retail chains not already present in the area, the HHI median would decrease by around 20%. This observation is clearly all the more relevant in the case of local shops in which the large majority of shops are franchises.

Conclusion

59. The earlier studies by *UFC-Que Choisir* (French consumer association) and *Asterop* (market research company) reached the conclusion that there is a very high level of concentration in customer catchment areas, but rely on definitions of the market and concentration indices which are far removed from those used in competition law and which are likely to overestimate the degree of market concentration.

60. The databases produced during the enquiry support the observation of a high degree of market concentration in customer catchment areas while making it consistent with the methods used in competition law and extending it to the local retailer and supermarket formats. More specifically, the opinion observes that the proportion of customer catchment areas likely to be dominated by a single operator is probably less than 10%, or 5% for supermarkets. On the other hand, the high degree of market concentration of a very high number of customer catchment areas is established, particularly in the case of hypermarkets and local retailers. In the first case, at least 40% of customer catchment areas in which distributors responding to our request operate can be considered concentrated. In the second, more than 85% of the communes sampled have a concentrated local retailer market and 65% in communes with more than 100,000 inhabitants. The case of Paris appears to be particularly striking in this regard as one operator (the *Casino* group) holds, either through integrated retailers or affiliated retail outlets, more than 60% of the market share in sales area, with its nearest competitor holding less than 20% (the *Carrefour* group).

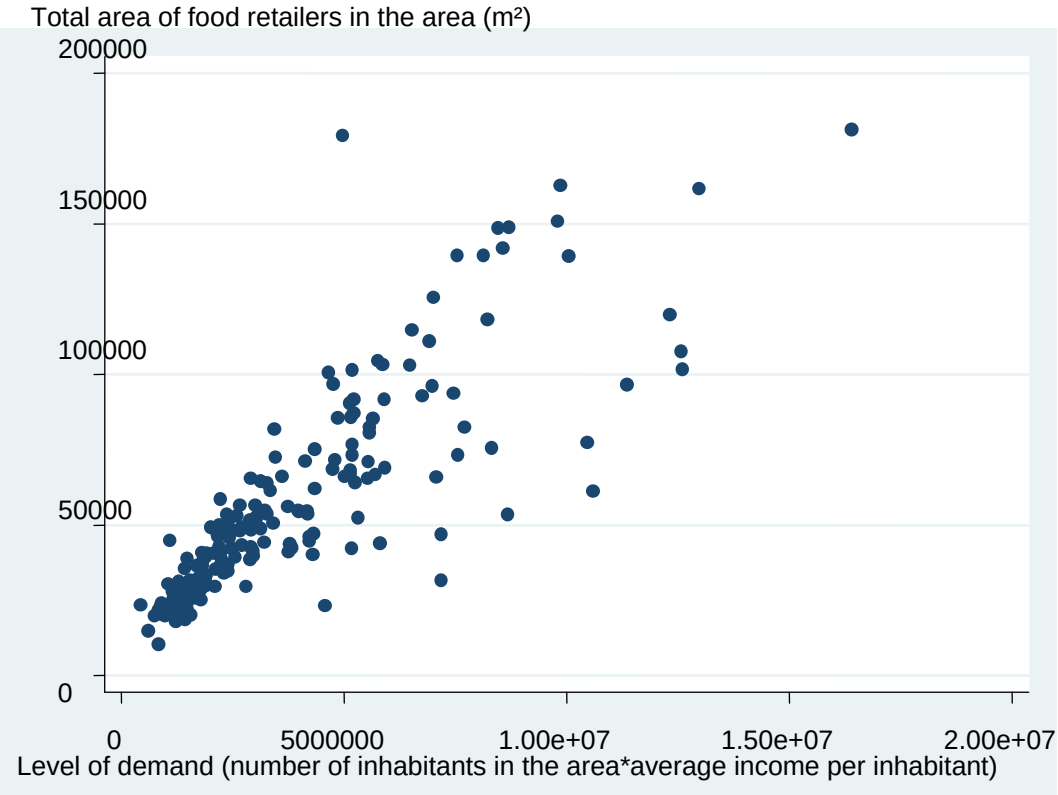
61. The high degree of market concentration in some customer catchment areas arises in part from the slightest demand which may, frequently, be noted, but not this alone. It also arises from the fact that, in a very high proportion of customer catchment areas, retail chains have one or more shops or affiliated retail outlets.

D. DEVELOPMENT PROSPECTS OF OPERATORS

62. The retail of daily consumer goods (supermarkets and hypermarkets) sector thus has a high degree of market concentration locally, particularly in hypermarkets and local shops. This arises in particular due to the absence or near-absence of some retail chains in particular areas or retail formats. Thus, local shops remain largely concentrated around the operators *Casino* and *Carrefour*. For hypermarkets and, to a lesser degree, supermarkets, very frequently a retail chain only faces competition from two or three operators.

63. The very large majority of operators confirmed that there are still areas likely to accommodate new retailers, including hypermarkets. To illustrate the possible prospects for growth, the following diagram, taken from *Focus Alimentaire LSA*, compares the level of demand in each of the customer catchment areas defined by *Asterop* with the total number of m^2 of grocery retail area developed. For the same level of demand, very different total sales areas co-exist, showing large room for improvement regarding retail facilities.

Diagram: Level of demand observed in 208 customer catchment areas taken from the *LSA-Focus alimentaire* catalogue and total area of food retailers in the area



64. More generally, as each operator tends to be relatively specialised by geographic area, each of them seeks to increase the presence of his network in areas where it is not yet established. Moreover, the network of daily consumer goods retail outlets must adapt to population flows and areas experiencing population growth are thus able to accommodate new shops. Similarly, the discount retailer model could maintain a considerable development potential. Nationally, this format still only has 14% of the market share, after being present in the market for more than twenty years, and the number of shops in France (4,241 in 2010) remains much lower than that observed in Germany, even after taking into consideration the lower population level. Regionally, while there is a very high density of shops in the North and East, the Île-de-France, Paca, Rhône-Alpes, Corsica and Ouest regions may have a significant potential for development[27]. Finally, the growth of the local retailer format is also of interest to several retail chains.

E. BARRIERS TO ENTRY IN THE FOOD RETAIL SECTOR

65. During interviews, operators stated that they came up against several barriers to entry in their plans to develop shops, regardless of the format chosen to be opened in a given customer catchment area. These result mainly and always from regulations surrounding the

[27] *Linéaires*, 260, July-August 2010.

business of running retail outlets selling groceries (1), difficulties associated with the purchase of commercial land (2) and rigidity of the various distribution networks (3). Other more residual barriers, such as awareness of the retail-brand and logistical costs are also worth mentioning (4).

1. ADMINISTRATIVE AND REGULATORY BARRIERS

66. Administrative and regulatory barriers are the obstacle to entry most frequently mentioned and on which most operators place the greatest importance. Depending on the format, these are of different types.

67. For hypermarkets and large supermarkets (with an area larger than 1,000m^2), operators continue to come up against administrative barriers through applications for establishment permits from the *Commissions Départementales d'Aménagement Commercial (CDAC)* (Departmental commissions for retail planning). Furthermore, operators state that these permits are the subject of many appeals which significantly increase the cost, length and uncertainty linked to these authorisation procedures. According to operators, appeals are brought before administrative courts and then, where applicable, before the administrative appeal courts, resulting in relatively long litigation, which can last several years.

68. Independent of the barriers posed by establishment permit procedures, building permits are also increasingly the subject of appeal, both by, in particular environmental, associations and the company's competitors seeking to establish themselves. While these appeals are not necessarily unreasonable and the costs are not actually a deterrent, they delay and add an element of uncertainty to the completion of the establishment process and the opening of new shops.

69. These various uncertainties lead operators automatically to make deeds for the purchase of commercial land contingent on conditions precedent linked to obtaining various establishment and building permits. The term of these suspension clauses is generally 18 months and can only exceptionally exceed 36 months. Overall, the time taken for the set-up of a hypermarket, from finding suitable commercial land to finalising plans, is between seven and ten years, as opposed to three to five years in the case of a supermarket. In fact, some plans may thus be abandoned when the time limits linked to the various administrative procedures exceed the time limits permitted by the conditions precedent.

2. BARRIERS TO ENTRY LINKED TO COMMERCIAL LAND

70. Commercial land to be used as a food or daily consumer goods shop must meet several criteria, in terms of area (on the outskirts, the area of the property required to set up is four to six times larger than the sales area), location (so that it is easily accessible, situated near to the main living areas and transport), layout of the premises (for local shops, for example, it is preferable that premises are single-storey) and compliance with local urban plans, territorial cohesion plans and land use plans. On this final point, several operators have stated that particular communes would deliberately choose to limit the development of particular distribution formats by setting up highly restrictive local urban plans, particularly on the outskirts of towns.

71. In town centres, administrative, operational and economic constraints come together to make new establishments difficult, particularly those larger than 400m^2. On the one hand, property allowing the establishment of a retail area sufficiently large to be attractive remains relatively rare. On the other hand, in order to obtain these premises, food distribution operators are in competition with companies in other sectors whose larger margins allow them frequently to outbid the offers made by food retail chains. Distributors may again suffer administrative restrictions as, on the one hand, some mayors frequently use the purchase option available to town halls against food retail groups and, on the other hand, residents associations are frequently opposed to the set-up of food shops near their homes, due to the nuisance, in particular sound pollution, they can create.

3. THE RIGIDITY OF THE VARIOUS FOOD RETAIL CHAINS

72. The enquiry has led to the observation that there is considerable rigidity between the various food retail chains, arising from the almost-exclusive relation between retail chains and their affiliates, on the one hand (a) and the poor mobility of independent retail outlets between competing retail-brands, on the other (b).

a) The existence of an almost-exclusive relationship between retail chains and their affiliated retail outlets

73. Most of the contractual documents which were able to be analysed as part of the enquiry impose on signatory companies a non-competition obligation throughout the entire duration of the relation, forbidding them to carry out any food retail business other than in the shop in question and to affiliate to a competing retailer.

74. Moreover, while relatively few networks demand that their affiliated retail outlets agree to be exclusively supplied by their central purchasing body, the loyalty rate of shops (i.e. the proportion of purchases made by an independent retail outlet affiliated to a group from the central purchasing body of this group) is particularly high, most often equal to or higher than 80%, with other purchases mainly covering products of local origin, meat products and fresh produce (vegetables, fruit).

75. Several characteristics, both legal and economic, of the terms of supply to retailers provide an explanation for these high loyalty rates. Firstly, nearly all operators require that their independent retail outlets are supplied exclusively with respect to the sale of private label products. These tend to cover 30 to 40% of the product mix defined by retail chains. Shops are thus obliged to have the main part of their purchases supplied by their central purchasing body. Secondly, some contracts also contain minimum or priority supply clauses which further increase the supply rate to independent retail outlets from the central purchasing body of their group. Thirdly, logistical costs linked to varied supply, the right of particular franchisors to inspect the free purchases of their franchisees, quantity discounts included in some supply agreements, the exclusive rights of co-operatives[28], and

[28] According to the principle of exclusive rights of co-operatives, any co-operative group is prohibited from supplying persons or companies who are not members of the group. This principle is provided by Article 3 of Law no. 47-1775 of 18 September 1947 concerning the status of co-operatives in the following terms, "*co-operatives may not allow third party non-members to benefit from their services, unless the particular laws which govern them permit this*". This authorisation was not given by the special law governing retail traders'

more generally, the unwillingness of most central purchasing bodies to hand over affiliated retail outlets to a competing network lead independent retail outlets to give priority to their network's central purchasing body for their supplies.

76. This almost exclusive supply of independent retail outlets from the central purchasing bodies of their heads of network constitutes an obstacle to upstream market entry for supply to a new operator, who is then compelled to open its own shops to sell its products.

b) The poor mobility of independent retail outlets between competing retail networks

77. While independent retail outlets are supplied almost exclusively by the central purchasing bodies of their affiliated group and the obstacles to establishment prevent shops being set up by new operators, they nonetheless have the possibility of attracting shops already affiliated to other retail chains. This reasoning, which is valid both at the national level and in customer catchment areas, nevertheless contrasts with the observation that there is very little mobility for shops.

The observation of very poor mobility of independent retail outlets

78. In view of the information gathered from operators during the enquiry, it appears that since 2005, the rate of rotation of independent retail outlets, understood as shops managed by companies independent of retail chains or associated with the latter, is relatively small. Indeed, according to retailers, the initial rates (number of independent retail outlets having left the network between 2005 and 2009/number of independent retail outlets in 2005) are between 0 and 1% for hypermarkets, between 4 and 15% for supermarkets, between 2 and 4% for local shops and between 4 and 5% for hard discount retailers. By way of comparison, a time period indicative of the contractual relation between the shop and its head of network of five years potentially allows a complete renewal of the number of affiliated retail outlets every five years, i.e. a potential initial rate of 100% greater than the rates actually observed for the various distribution formats.

Various explanations for the limited mobility of independent retail outlets

79. The relative inertia of independent retail outlets seems to be able to provide an explanation of different sorts for the main part.

80. This situation may, firstly, be explained by a lack of will and/or capacity of integrated groups to develop the franchise or any other form of affiliation. Indeed, the large integrated retail chains have not really developed franchises in the hypermarket and hard discount retail formats. As a result, their ability to accommodate shops under these formats would be limited. Nonetheless, there are three limits to this explanation. On the one hand, integrated groups are able to buy back franchise shops in order to operate them themselves, particularly when the managers of affiliated retail outlets retire. On the other hand, several integrated operators have stated that the obstacles to the creation of new shops has largely led them to develop their franchise networks, in the retail formats or geographic areas they

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co-operatives. On the contrary, Article 2 of the Law of 11 July 1972, codified under Article L. 124-2 of the Commercial Code confirms that "*retail traders' co-operative societies may not admit third party non-members to benefit from their services*".

have not yet had much of a presence in. The poor mobility of shops has also been observed within co-operative groups or in retail formats in which a large number of shops are operated as franchises, such as local retailers, for example. Consequently, the lack of mobility of independent retail outlets between competing networks does not result from the reluctance of retail chains to welcome independent retail outlets, but from a lack of will or difficulties independent retail outlets face in changing networks.

81. Secondly, the lack of mobility of independent retail outlets may also be explained by the attachment affiliated retail outlets have to their retail-brand. This attachment may in particular be due to the economic satisfaction independent retail outlets draw from the affiliation to a head of network and thus they have no desire to change network. It may also be due to the common values and human links developed within networks and particularly within co-operative groups (regional or national collective work days, the sponsorship system set up the *Leclerc* group, etc.).

82. Thirdly, any change of retailer has a particular commercial risk, which deters, in some cases, affiliated retail outlets from changing network. Indeed, the level of awareness by consumers differs considerably depending on the retail-brand. The manager of a shop is thus never absolutely certain that his customers will remain loyal to his shop rather than his retail-brand. Moreover, any change of retail-brand implies a change in the management method (terms of supply, information technology systems, etc.) and the physical layout of the shop, as well as the product mix and prices, both for the purchase and sale, of goods.

83. The lack of mobility of independent retail outlets seems to have mainly found its explanation in both the contractual and corporate relations that food retail chains have with their affiliated retail outlets. Firstly, the enquiry showed that there is a particular lack of clarity in these relations, in particular due to the large number of contractual documents formalising the relation and the lack of information the affiliate has about the extent of the commitments it has agreed to. This lack of transparency prevents potential affiliates or an affiliate whose contract has expired from making the various retailers compete and thus hinders the mobility of affiliated retail outlets between different networks. In addition to this, some contractual and corporate mechanisms set up by the retail chains in their relations with their affiliates, such as relatively long terms of commitment, deferred subscription fees, post-contractual non-reaffiliation and non-competition clauses and priority rights, have the purpose or effect of deterring the affiliate from leaving the network. These various mechanisms are analysed below (see below paragraph 113 et seq.).

4. OTHER BARRIERS TO ENTRY

84. The awareness of the retail-brand seems to be a major barrier to the entry of foreign retail-brands, who are unknown to consumers. This obstacle also plays against small retail networks that are relatively unknown outside of the regions they are from. Franchises can in part make up for this lack of awareness, as the franchisee is sometimes known to consumers and local politicians and has greater incentive to develop his business.

85. Logistical costs are another barrier to entry and explain in part the development "in clusters" of large-scale distributors. The transport of goods from regional or national central purchasing bodies to areas where a retail chain only has a few shops is in fact rather expensive and difficult to make profitable. It is thus preferable that, when an operator seeks to penetrate a region in which it still does not have much of a presence, it can rely simultaneously on several shops.

86. In spite of these obstacles to the creation of new shops, nearly all integrated operators have stated that they continue to prefer creating shops rather than taking over independent retail outlets operated under a competing retail-brand.

87. Nonetheless, the change of retail-brand of independent retail outlets can be beneficial to the consumer. Indeed, the independent retail outlet is able to choose a retail-brand, which, if it must satisfy its profitability expectations above all, must be able to offer a layout plan for the point of sale, a higher level of customer service, more products offered, private-label products and price positioning likely to meet consumer expectations better. In particular, the profit made by the independent retail outlet by improving its purchasing capacity and using a more effective retail-brand, particularly in the case of a high level of competition in the customer catchment area, must logically be reflected in the prices.

88. Having presented the main barriers to entry in the food distribution sector, the two types of practices which are the subject of the sector enquiry – started by the *Autorité* at its own initiative – should be studied, i.e. those concerning the management of commercial land, on the one hand, and those concerning affiliation relations on the other. For each of these two types of practices, a report shall be drawn up before a competitive analysis is carried out and the *Autorité*'s recommendations provided.

III. Practices observed with respect to the management of commercial land

89. Concerning practices in the management of commercial land, the enquiry was particularly focused on the holding of unused property (A) and on the use of exclusive rights clauses in contracts for the sale and purchase of commercial land (B)[29].

[29] Several operators have also emphasised the role played by the retail chains' property companies and the saturation conduct in customer catchment areas. The enquiry did not go beyond simply descriptive elements. They shall not be discussed in the scope of this opinion.

A. HOLDING UNUSED LAND

90. During their interviews, several operators stated that they had been prevented from entering particular commercial areas due to practices consisting of competitors already present there holding unused property. Nonetheless, these same operators recognise that this "property freeze" practice is frequently performed with a view to the future opening of a shop by the retail chain holding the plot of land. Many of them also stated that this practice does not constitute a definite entry barrier, and that, most often it only slows down the entry process or reduces profitability by preventing the competitor from setting up its shop on the most attractive plots of land. For some operators, no group has ever prevented them from setting up in a customer catchment area due to the practice of property freezing.

91. In order to understand the issue more specifically, albeit in a declarative manner, of the extent of property held but not used by operators, questionnaires were sent to the main operators asking them to identify unused commercial and non-commercial land areas. Several operators thus declared that they hold plots of commercial land which is as yet unused and, in some cases, these unused plots are held even though the shop has a very large market share in the area.

92. Nonetheless, the number of these plots of lands would be relatively limited with respect to the number of shops in these groups. Moreover, in some cases, the plots held would have a limited area making it unlikely that a major competitor would set up a shop there or there was no alternative to holding this property. In particular, reasonable justifications have been put forward, such as the wait for a building or establishment permit, the necessary time for the sale of land or the shop when it is not profitable or when the land initially purchased is too large.

93. In some cases, the purchase of unused property is part of a long-term strategy to develop the shop, encouraged simultaneously by the rarity of property and the notification threshold to open shops: operators may thus start by opening a small shop in order to obtain the approval of the administrative authorities more easily, then enlarge it once their chances of receiving the consent of these same authorities are sufficiently large. In some cases, the term of holding may be long as the resale follows an authorisation refusal by a CDAC: it may then be relatively long finding a potential buyer.

B. EXCLUSIVE RIGHTS CLAUSES IN CONTRACTS FOR THE SALE AND PURCHASE OF COMMERCIAL LAND

94. The retail chains were also asked about non-competition clauses likely to be provided in their contracts for the sale and purchase of commercial land. These clauses prohibit the retail chain’s co-contracting parties from operating a food retail business on the land sold and/or the land near the land sold of which it remains the owner.

95. An examination of the contracts for the sale and purchase of property shows that such clauses appear relatively frequently, mainly in the case of contracts of sale. The term of these clauses shows wide variations, with a large number of them being for a term of 30 to 50 years. Some contracts furthermore incorporate priority rights for the retail chain in the case of the possible resale of the land.

96. In the case of contracts for the purchase of commercial land, such clauses are rarer and mainly relate to cases in which the vendor of land is also the owner of an adjoining piece of land.

97. Crosschecking the sales and purchases of commercial land, including non-competition clauses, with the market shares of operators in the customer catchment areas concerned tends to show that these clauses are present even when the operators have large market shares in their customer catchment area.

98. According to operators, there are three main reasons for these non-competition clauses. The first relates to cases of land immediately bordering that on which the shops are located: this type of clause would allow the profitability of the shop already established to be maintained and prevent another food shop being set up alongside the first (instead of a clothes, DIY, etc. shop), thereby reducing the retail diversity and attractiveness of the area for customers.

99. The second reason deals with the concern about capitalising on the invigorating role the food retailer plays in the dynamism of a retail area: often the first shop set up in a retail area, the food retailer, through its advertising, number of customers, competitiveness, generates flows of customers and thus spills over for other shops in the area. The non-competition clauses inserted into contracts for the sale and purchase of property thus have the purpose of preventing competing shops from setting up which are likely to act as freeloaders in such retail areas.

100. A third reason relates to cases of relocation-expansion: either following the request of a municipality or another authority or through the desire to set up at a more attractive site, an operator may close a shop and re-establish itself elsewhere close by. As such operations involve major costs, operators are thus careful to maintain the profitability of their new shop. In these situations, operators state that the use of such clauses is void as the purchaser of the land is most often a local authority or a developer wishing to build housing on it.

101. The relevance of these arguments appears to be limited nonetheless. In particular, the argument about protecting investments is not convincing. On the one hand, investments made in this sector are not particularly risky, in the words of operators themselves. On the other hand, a large proportion of investments made are not of specific assets so that the arrival of a competitor in an area does not cause irreparable damage to competitors already established there, who can, if they wish, resell their developed and undeveloped land. Similarly, the spill-over of demand created by the establishment of a food shop in a customer catchment area (which results in traffic flows of people and increases the profitability of neighbouring shops) can be monetised (by increasing rents or the sale price of property available in the area after a food supermarket sets up there, for example) by the owner of neighbouring lands and thus reconveyed to the food shop, which would pay less than for its first set up of a shop, as the vendor of the land still has commercial land near the land sold (which would logically be the case if non-competition clauses are negotiated). The use of exclusive rights clauses to guarantee a far greater range of shops in an area is not convincing either: on the one hand, major obstacles, particularly administrative, already exist to the arrival of food shops, and on the other hand, through their purchases, it is up to consumers to determine the desired level of retail diversity: in particular, they may prefer a little retail diversity if this increases competition and lowers prices.

IV. Competitive analysis of the practices observed concerning the terms of managing commercial land and recommendations

102. The competitive analysis of the practices observed is presented first (A), followed by recommendations drawn up by the *Autorité de la concurrence* concerning the necessary regulatory framework for these practices (B).

A. COMPETITIVE ANALYSIS OF THE PRACTICES OBSERVED CONCERNING THE TERMS OF MANAGING COMMERCIAL LAND

103. As has been demonstrated, several customer catchment areas remain excessively concentrated, due, in particular, to the significant barriers to entry. The rarity of commercial land constitutes a barrier to entry mentioned by nearly all sector operators. In this context, any strategy set up by an operator already established in an area and aimed at further limiting the access of distributors to commercial land may constitute an additional barrier to entry.

104. The documents gathered during the enquiry and operator interviews have more specifically led to the identification of three types of practice likely to constitute, through their purpose or effects, a barrier to the entry of new operators: the holding of unused property on the one hand, non-competition clauses inserted in contracts for the transfer and purchase of commercial land on the other hand, and the saturation of customer catchment areas through the establishment of several shops within the same customer catchment area, with respect to shops selling the same type of product or belonging to clearly separate sectors.

105. Nonetheless, the practices of "commercial land freezing" are frequently justified by the prospects of enlarging shops, the necessary time periods to obtain administrative permits and transition periods following the bankruptcy or closure of a shop. Moreover, for an operator wishing to hinder the establishment of a competitor, strategies consisting of the resale of a site accompanied by a non-competition or preference clause, or a lease of the site to non-competitor operators can be less costly than a property freeze.

106. Similarly, to be classified as anti-competitive, the establishment of several shops with the same retail-brand or different retail-brands belonging to the same retail chain must have as its sole or main reason the purpose of excluding possible entrants. Such a classification would require not only the demonstration of the existence of a dominant position in the area, but also for it to be established that many shops lead to a loss of market share so that the fixed costs arising from the establishment of a new shop would lead to a reduction in the group's operating profits, so that this could only be explained by the wish to exclude competitors. Moreover, the reduction in logistical costs allowed by the agglomeration of shops from the same group (when they sell the same products) and the over-spill of demand arising from the establishment of different shops in a given customer catchment area should be taken into account. In order to be carried out, such an analysis would require a detailed investigation of the cases of pre-emption mentioned, often evasively, by some operators.

107. On the other hand, practices consisting of, for a distributor, accompanying the resale of developed or undeveloped land with non-competition clauses for a term which can run from ten to fifty years (for those of these clauses which include a term limitation) and which are transmitted during later resale, contribute to increasing the barriers to entry to the retail grocery market, as has been stated by several operators. Moreover, these clauses do not seem to be able to be justified validly (see above, paragraphs 94 et seq.).

B. THE *AUTORITÉ DE LA CONCURRENCE*'S RECOMMENDATIONS: THE REMOVAL OF NON-COMPETITION CLAUSES AND PRIORITY RIGHTS IN CONTRACTS FOR THE SALE AND PURCHASE OF COMMERCIAL LAND

108. In the food retail sector, the excessive concentration of particular customer catchment areas is in part a result of the existence of high barriers to entry. These obstacles to the arrival of new retailers mainly arise from administrative procedures prior to the establishment of a new shop. On these different aspects, the *Autorité de la concurrence* refers in particular to its opinion no. 07-A-12 on the *Royer* and *Raffarin* Laws, which at the time noted the failure of these laws to protect local shops and their role in the excessive degree of market concentration in customer catchment areas. In this case, the *Conseil de la concurrence* had recommended limiting the regulation on retail planning to town planning rights only and not to add supplementary administrative procedures. In the context of the observations made in this opinion, the *Autorité de la concurrence* can only repeat this recommendation that the specific administrative uncertainties of the retail of daily consumer goods sector face make their search for commercial land even harder.

109. Nonetheless, it was noted during the enquiry that the regulatory obstacles to entry are made worse by the conduct of existing operators, and particularly their use of non-competition clauses in a large number of contracts for the sale and purchase of commercial land. In contracts for the sale of commercial land, these clauses have the purpose of prohibiting the purchase of land or a retail premises from running a food business for a period which can run for up to 50 years. Included more rarely in contracts for the purchase of commercial land, they then have the purpose of prohibiting the establishment of companies that could operate a food business on other land held by the vendor (most often neighbouring the land which is the subject of the contract); the terms of these clauses can also spread out over several decades. The enquiry also showed that there are priority rights in favour of retail chains in some contracts for the sale of commercial land; the term of these contracts can run for up to 50 years as of the date the contract is signed. These clauses give a significant competitive advantage to the beneficiary by allowing it to know about offers made by potential purchasers and thus to anticipate the arrival of a competitor or to prevent it by using their priority right.

110. Several operators stated that such clauses had posed an obstacle delaying their entry in a customer catchment area or had reduced its impact. It has furthermore been observed that such clauses are also used by operators who are likely to have, in their customer catchment area, high market shares and which could affect local markets which are already relatively concentrated. Moreover, the justifications given by operators for these clauses in contracts are unconvincing; they do not appear necessary to promote investment in this sector or to guarantee a better service to consumers.

111. The removal of these non-competition clauses, both from future and current contracts, thus appear necessary as they create a limitation on competition and obstruct the establishment of new retailers. Several alternative solutions to a complete prohibition of these clauses have been considered. It should theoretically be possible only to prohibit these clauses and priority rights in areas where the degree of market concentration passes a particular threshold. Such a condition would nonetheless require the local market to be demarcated, its degree of market concentration assessed and areas deemed concentrated to be adjusted gradually as they develop (with the opening and closure of shops). Given the lack of efficiency gains associated with these clauses, the legal uncertainty which could arise from delimiting customer catchment areas and measuring the degree of market concentration makes it clearly more preferable to prohibit them outright. Similarly, the authorisation of time-limited non-competition clauses for commercial land that is unlikely to host a new operator would constitute a remedy that is difficult to monitor even though the effects produced by these clauses can be significant.

112. These recommendations are similar to those drawn up by the Competition Commission in the United Kingdom. They raised, in particular, the issue of restrictive use clauses through which a retail chain selling a piece of land prohibits the purchaser from using it to operate a distribution business or to resell it to another retail chain ("*restrictive covenant*") and also limited the term of particular territorial exclusive rights through which a distributor was protected against the establishment of competing distributors in the same geographic area (see Competition Commission, *The supply of groceries in the UK market investigation*, 2008).

V. Practices observed in affiliation relations between affiliated traders and retail chains

113. The *Autorité de la concurrence*'s decision no. 10-SOA-01 of 25 February 2010 starting a sector enquiry at its own initiative states: "*For affiliation agreements of independent retailers, the referral shall examine the various contracts in use, particularly franchise agreements or members agreements for an independent retailers' co-operative as well as other contracts binding a retailer to a legal person representing the network (supply, lease-management, lease or shareholders' agreement, etc.). The investigation shall thus have to assess the strength of the link between heads of network and affiliated retailers and the actual degree of independence the latter have. The impact of these vertical relations on inter-network mobility must be assessed for each of the main sales formats (hypermarkets, supermarkets, local shops, specialist shops) according to the nature and regulatory framework of the links between members of the network. Thus, the following must be taken into account: the term of contracts linking the independent retailer and his network, obstacles to changing the retail-brand of a shop and barriers to entry thus created against new operators. The characteristics of these relations between the independent retail outlet and its affiliation network must thus be assessed with respect to their possible competitive effects, which are due to the rarity of retail sites in the customer catchment areas and the influence of operators bound by these contracts to the relevant markets identified. The pro-competitive reasons given for these clauses, in terms of transferring know-how and reducing the risk borne by the independent retail outlet in particular, must also be taken into account in this assessment*" (paragraph 6).

114. Firstly, the enquiry allowed the size of the number of independent retail outlets affiliated to daily consumer goods retail chains to be observed. According to the main operators, in France this represents around 63% of the total number of hypermarkets, 70% of the number of supermarkets (excluding hard discount shops) and 77% of the number of local shops, with the share of the remaining shops representing integrated retailers operated directly by retail chains.

115. The enquiry secondly emphasised the variety of organisational and contractual forms of affiliation. Indeed, the forms of affiliation of an independent retail outlet to an integrated group are varied. By way of illustration, the *Carrefour* group thus has five separate organisation models for its shops: "*Case no. 1: integrated shops directly operated by Carrefour; case no. 2: shops operated by franchisees (natural or legal persons without Carrefour's capital holding), owners of the business; case no. 3: shops operated by franchisees (natural or legal persons), Carrefour's lessee-managers; case no. 4: shops operated by franchisee companies, with Carrefour's share in capital, Carrefour's lessee-managers; case no. 5: shops operated by franchisee companies, with Carrefour's share in capital, owners*".

116. As stated above (paragraph 72 et seq.), the enquiry was finally led to emphasise the poor mobility of independent retail outlets between competing networks. Taking into consideration the many obstacles to the creation of new shops, this poor mobility constitutes a considerable barrier to entry in the food distribution sector. For a large part, this inertia by affiliated retail outlets is due to particular measures set up by retail chains, the purpose and/or effect of which is to prevent their affiliated retail outlets from leaving the network. These measures are contractual on the one hand (A) and corporate on the other (B).

A. CONTRACTUAL MEASURES CONSTITUTING OBSTACLES TO THE MOBILITY OF INDEPENDENT RETAIL OUTLETS

117. Relations between affiliates and retail chains are often formalised through various contractual documents (franchise agreement, brand name agreement, supply agreement, trademark license agreement, lease management agreement, articles of association, by laws, etc.). For the main part, these relations include several provisions which have the purpose and/or effect of deterring affiliates from leaving the network; these are relatively long terms of commitment (1), different expiry dates of the various contracts binding the shop to its head of network (2), deferred subscription fees (3), post-contractual non-reaffiliation and non-competition clauses borne by the affiliate (4) and priority rights in favour of heads of network (5).

1. RELATIVELY LONG TERM OF COMMITMENTS

118. The enquiry was able to observe relatively long terms of commitment (a) for which operators gave unconvincing justifications (b). The legal analysis of these clauses allows questions to be raised about the excessive nature of most of the terms of commitment observed (c).

a) Relatively long and disparate terms of commitment depending on the retail-brand

119. In general, it is the co-operative groups which have the longest contractual terms with membership periods which can run for up to 30 years.

120. Nonetheless, one of the big French co-operative groups does not provide a minimum membership term for its members: they are free to withdraw from the group at the end of the financial year in return for compliance with a six-month notice period[30].

121. Franchise agreements used by integrated group are usually for a shorter term than those of membership agreements for co-operative networks. Their term is between 3 and 9 years. They are most often renewable automatically for a term equivalent to the initial term. Terms for the notice of termination of contract are usually between six months and one year. A lack of regularity in terms for the types of retail formats between the retail-brands of different groups as well as between the different retail-brands within the same group has also been observed.

122. To ensure compliance with the term of contracts by independent retail outlets, most retailers also use penalty compensation clauses in the case of the early termination of the

[30] The rules of this group nonetheless provide that when a member benefits from specific individual assistance, the central purchasing body to which it is affiliated can ask it to remain a member of the co-operative for a term of up to 10 years. Situations that actually give rise to payment are nonetheless negligible.

contract. The amount provided for this compensation generally corresponds to the amount of contributions which are outstanding up until the contract's expiration date or a specific percentage (which can be up to 10%) of the affiliate's turnover. By way of comparison, it should be noted that according to the *Fédération des entreprises du commerce et de la distribution (la FCD*) (Federation of Trade and Distribution Businesses), the average net margin rate of the three main integrated distributors (*Auchan, Carrefour* and *Casino*) was 2% in 2009[31]. The early termination of the contract also gives rise to costly litigation procedures, particularly when there is an arbitration clause.

b) Justifications provided by operators for relatively long terms of commitment

123. According to operators, a long contractual term could provide better incentives for investment and greater stability for the network.

The case for investment incentives

124. According to most operators, long-term contracts are necessary to motivate the two parties, the retail chain and independent retail outlet, to make investments in the shop, including investments made to open the shop and those made regularly for the purpose of renovating the shop, carried out on average every five to seven years. The affiliate, in order to reinvest in his shop, would need to have a term of commitment sufficiently long to have the time to make the investment made profitable, which could explain why contracts, at the end of the first collaboration term of five to seven years, are extended for an equivalent term. Moreover, a long-term relation would also be a guarantee of security for banking establishments lending their financial assistance to the independent business. During their interviews, market actors thus stated several times that the redemption period of a goodwill is between five and ten years according to the format and net margins made.

125. Nonetheless, this accounting depreciation does not correspond to the reasoning given in competition law, which only takes into account the specific nature of assets, the risk of freeloading and, where applicable, the uncertainty linked to investments. Moreover, according to operators, the risk associated with the establishment of a shop would be relatively small once the necessary administrative authorisations have been obtained. The risk of freeloading is also limited: investments made by an affiliate hardly run the risk of benefiting another competing affiliate. Finally, the specific nature of assets acquired by the affiliate is mainly limited to investments made to lay out the shop[32], amounting to around 300 euros per m^2 according to an operator. Using this as a basis for its reasoning, estimates of turnover per m^2 and the net margin provided in the file, the redemption period of this specific investment would thus be between two and five years[33].

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[31] *Casas et associés* study, April 2010.

[32] Indeed, franchised traders generally recover the main part of their initial investment during the resale of their business.

[33] Turnover per m^2 varies in a non-linear manner with retail area, but would normally be between €6,000 and €7,000 for a supermarket, around €8,000/m^2 for a hypermarket, and around €4,500 to €6,000/m^2 for a local shop with a relatively large retail area. As net margins are between 1% (in the case of a large food retailer with competitors) and 5% (for a reasonably-sized local shop) according to sector studies by *Xerfi*, the net profit per m^2 made by these shops is thus between 80 and 225 euros. Based on an interest rate of 5%, the initial investment is thus redeemed in less than 5 years for hypermarkets and less than two years for local shops.

126. The highly unequal nature of investments made by the parties must also be taken into consideration to assess the appropriate term of contractual relations between the head of network and independent retail outlet. With the exception of cases where affiliates operate through a joint venture company with the head of network, investments made by the latter to accompany its affiliate remain, without exception, very limited. Thus, according to an integrated operator who was questioned, the latter may pay 70,000 to 120,000 euros for "*casual associated products*" for a period of 7 years, most often when the shop is renovated. Other investments are also made by retail chains, like "*spaces on platforms, the codification of shops and their product mixes in the system, integration in advertising promotions, set up of support teams (mainly for goods), training of shop teams, configuration of IT tools, and where necessary, the installation of new tools, connection to the loyalty system, updates of all company reference systems…in brief, broad integration management*", but they could not be assessed and in any case are not specific at all to a given affiliate.

127. Very different contractual terms (from 0 to 30 years) observed in the sector also tend to put into perspective the scope of justifications based on investment incentives: indeed, at no time did the operators with the longest terms provided in the contracts they execute claim that the investments made by their group or affiliated retail outlets were higher than those made by competitors with shorter terms of commitment. In particular, the example of the co-operative group that does not require any term of commitment in this respect is quite striking.

128. Moreover, on a more theoretic level, the greater the competition between operators and the greater the investment incentives, the stronger both retail chains and independent retail outlets are. Indeed, independent retail outlets able to use the competition between distribution networks could thus urge them to invest. Similarly, retail chains able to extend the density of their networks by accepting shops operated under a competing retail-brand could increase the investment incentives of independent retail outlets in order for them to remain affiliated to the network. Long-term contractual relations can appear to be disadvantageous for independent retail outlets affected by worsening commercial terms offered by their head of network: in this case, both the specific nature of the investments agreed and the term of the commitment made pose obstacles to any desire to change retail-brand.

The case for maintaining the network's stability

129. Secondly, a long-term contractual relation could also be, for the retail chain, a method of ensuring the stability of its network and its volumes of purchases and thus the competitiveness of its supply.

130. The argument for maintaining the network and its competitiveness is also limited. According to operators, in particular co-operative groups, a smaller contract term could result in less stability in the network, with a large number of shops being likely to leave it each year to join a competing retail chain. Nonetheless, this argument does not take into consideration the shops that each network, depending on its performance, would be able to accept each year as the term of their commitments with competing groups would also be shorter.

131. A more convincing variation on this rationale is that integrated groups, for fear that their independent retail outlets may leave the network, decide to acquire them totally or partially if the term of the contracts binding them to their affiliated retail outlets is shortened. With smaller financial capacities, co-operative groups cannot effectively copy this strategy. In

the end, the reduction in the number of independent retail outlets could lead to a weakening of co-operative groups and thus a reduction in their competitiveness. Nonetheless, the examination of the transfers of shops shows that integrated groups are not necessarily the operators towards which shops wishing to change their distribution network would turn. Moreover, such buyout operations, if they focus on sufficiently large shops, must be notified to merger control at the *Autorité de la concurrence*, which will assess its impact on competition. It should be noted that both co-operative groups and integrated retail chains rely on corporate measures (share in capital of operating companies) to prevent the departure of some of their shops to competing retailers.

c) Legal analysis of relatively long terms of commitment

132. In a ruling of 22 February 2000, the *Cour de cassation* (French Supreme Court) held that the clause in the articles of association obliging each co-operative member to join a group for a term of at least 30 years was not contrary to co-operative law insofar as this clause "*had the purpose of maintaining, for a reasonable term, the cohesion of co-operative members in view of covering risks decided on jointly and completing the redemption which the departing or dismissed members had temporarily profited from*" (Cass. com., 22 February 2000, no. 97-17-020).

133. On the other hand, in the scope of decision no. 05-D-49 of 28 July 2005 concerning practices in the sector for the rental and maintenance of mail franking machines, the *Conseil de la concurrence* had the opportunity to consider that "*the inclusion of a long-term clause in a contract, possibly extended by tacit renewal, could itself have restrictive effects on competition if it is not justified by the need to redeem investments or by a counterparty granted to the co-contracting party. The addition of constraints to early termination increases the restrictive effect on competition*". In this decision, the *Conseil de la concurrence* held that an initial contractual term of four years, doubled by an automatic renewal clause for a term of four years and the limitation of the possibility of terminating the contract on its anniversary date subject to compliance with a three-month notice prior to the expiration date of the contract, had restrictive effects on competition in the rental and maintenance market for mail franking machines, as it could not be justified by the need to redeem an initial investment and the market structure (90% of market bound by contracts for a term of 5 or more years) was such that these long-term contracts prevent any effective admission of a competing operator.

134. Moreover, as has been seen, the reasons put forward by retail chains to justify the relatively long term of the commitments made, particularly those relating to the redemption period of investments, are unconvincing (see paragraph 123 et seq.). Moreover, most of the retail-brands have relatively long terms of commitment, of more than 5 years: only five retail-brands belonging to integrated groups and a co-operative group offer membership terms of less than or equal to 5 years. In addition, the analysis of these clauses must be made taking into consideration the almost exclusive relationship between retail chains and their affiliated retail outlets. Thus, as stated in paragraphs 73 et seq., in spite of the lack of an exclusive supply clause, affiliated retail outlets are almost exclusively supplied by central purchasing bodies and their head of network. The creation of new shops remains hindered by several obstacles, as shown in the contrast between the relative stability of the number of shops open and the development potential still noted in many customer catchment areas. Consequently, excessively long terms of commitment between the two partners are likely to limit the competition central purchasing bodies practice to sell their products to independent retail outlets. In this respect, Article 5 (1) (a) of

Commission Regulation no. 330/2010 on vertical restrictions provides that any non-competition obligation, including exclusive supply obligations, in vertical agreements and whose term is unspecified or exceeds five years cannot be exempt. Article 5 (1) of the Regulation also states that a non-competition obligation automatically renewable beyond a period of five years is considered to have been made for an open-ended term.

135. In view of the analysis table provided by the *Conseil de la concurrence* on this matter, on the provisions of Commission Regulation no. 330/2010, the accumulated market share held by the retail-brands binding their affiliates to long terms of commitment, and the weak scope of their justifications, term clauses which exceed five years thus raise legitimate competition concerns.

2. MULTIPLE CONTRACTS AND DISCREPANCIES IN THEIR EXPIRY DATES

136. The enquiry observed that relations between retail chains and their affiliated retail outlets are mainly formalised by several separate contractual documents (franchise agreement, co-operative membership agreement, supply agreement, lease agreement, shareholders' agreement, articles of association of independent retail outlets, etc.). When such contracts are of a different term and the expiry date of one of them does not automatically lead to the termination of the other – which is frequently accompanied by the payment of compensation and/or the entry into force of non-competition or non-reaffiliation clauses (see below), the term of the contractual relation can then be extended artificially. Moreover, the large number of contractual documents creates uncertainty and legal insecurity which are likely to deter the owner of an independent retail outlet from leaving the network to which it is affiliated.

137. In its decision no. 98-D-52 of 7 July 1998, the *Conseil de la concurrence* held that "*the accumulated use of the abovementioned clauses proposed by J.C. Decaux, including the automatic renewal of contracts with termination terms that make it difficult for groups to exercise this right, the signing of additional clauses for a term equal to the initial term in the case of the replacement of movable property during the contract, sometimes accompanied by automatic renewal clauses, and preference clauses under the terms of the initial contract for companies in the Decaux group in the case of the installation of movable property at new sites, has the purpose of artificially extending the term of the contractual relation between Decaux and the groups and allows companies in this group to avoid, for very long periods, sometimes several decades, any open competition*".

138. Moreover, in the scope of the referral on *Carrefour's* practices in the local food retail sector which resulted in decision no. 10-D-08 of 3 March 2010, the *Syndicat de l'Épicerie Française et de l'Alimentation Générale (SEFAG)* (French Grocers and Food Retailers Union) criticised the gap in the expiry date between the various contracts made between the *Carrefour* group's subsidiaries and franchises, which according to it had the effect of artificially extending their term. In its decision, the *Autorité de la concurrence*, having noted this difficulty, noted the *Carrefour* group's commitment to putting an end to this situation by setting the expiry dates of current franchise and supply agreements with different terms to one date (paragraph 33 of this decision).

3. DEFERRED SUBSCRIPTION FEES

139. Several retail-brands provide a subscription fee for the network which corresponds to a percentage of forecast turnover whose payment is deferred to the date the affiliation agreement ends.

140. Clauses providing deferred subscription fees are not illegal clauses per se. They may nonetheless have the effect of deterring the affiliate from leaving the network on the expiry date of the contractual relation or if there is a serious contractual breach attributable to the head of network. Indeed, deferred subscription fees oblige the affiliate who decides to leave the network to pay an actual "redemption fee" whereas a staggering of divided payments as the contract runs would be more sustainable for the affiliate.

141. In this respect, the www.pme.gouv.fr website published by the Ministry of the Economy, Industry and Employment to help SMEs recommends not adopting such clauses and limiting over time the staggering of the payment of the subscription fees when this procedure is applied.

4. POST-CONTRACTUAL NON-REAFFILIATION AND NON-COMPETITION CLAUSES

142. Most of the affiliation agreements analysed provide post-contractual non-reaffiliation or non-competition clauses (a) which are necessary, according to operators, to protect the know-how transmitted to affiliates (b). A legal analysis of these clauses should be carried out to determine whether they satisfy the conditions for necessity and proportionality with respect to the objectives of competition law (c).

a) The variety of post-contractual non-reaffiliation and non-competition clauses noted

143. Several retail-brands also include post-contractual non-reaffiliation or non-competition clauses in one or more of the contracts binding them to an independent retail outlet or its owner. Most of the non-reaffiliation clauses noted are only intended to apply in the case of early termination of the contract, for a term of one to two years as of the termination of the contract. Other non-reaffiliation clauses in the contracts analysed are intended to apply either when the contract reaches its expiry date or is terminated early. Some retail-brands use more general non-competition clauses at times applicable only in the case of the early termination of the contract and at others applicable at the anticipated expiry date. These non-competition clauses are all for a post-contractual term of one year. Several retailers do not use either post-contractual non-reaffiliation clause or non-competition clauses.

144. Moreover, the geographic range of these clauses varies according to the retail chain: it may thus be a granted area, with a radius of 30km (in rural areas), 20km, 15m, 10km (in urban areas) or 5km around the shop. Some post-contractual non-reaffiliation and non-competition clauses are not geographically limited on the other hand.

b) Justifications given by operators for post-contractual non-reaffiliation and non-competition clauses

145. Operators justify such clauses by the need to protect the know-how transmitted to affiliated retail outlets which have decided to leave the network.

146. In the food distribution sector, the know-how groups undertake to transmit to their affiliates generally consists of:

- Advice about the general organisation of the shop's activity, and more particularly the commercial policy and physical layout of the shop, budget, desirable investments and operating accounts, promotional actions to take, commercial, administrative and financial management, including recommended consumer sales prices, product mix and layout plans;
- Staff training programmes;
- A communication policy and publicity for the retail-brand;
- Assistance in finding sites for new shops;
- Organisation of meetings on the prospects for the development of the retail-brand, etc.

c) Legal analysis of post-contractual non-reaffiliation and non-competition clauses

147. In the retail grocery sector, it appears to be possible to assimilate post-contractual non-reaffiliation and non-competition clauses. Moreover, these clauses meet a requirement of necessity and proportionality which it is not clear will be complied with in relations between independent retail outlets and affiliation groups.

Assimilation of a non-reaffiliation clause with a post-contractual non-competition clause

148. Case law distinguishes non-reaffiliation clauses from post-contractual non-competition clauses, on the ground that the former impose a restriction on the trader's exercise of his activity and not a prohibition. This principle was restated by the *Cour de cassation* (French Supreme Court) in a recent ruling: "(…) *the non-competition clause has the purpose of limiting the franchisee's ability to carry out a similar or analogous business to that of the network it is leaving, while the non-reaffiliation clause restricts its freedom to affiliate to another network*". (Cass. Com. 28 September 2010, appeal no.: 09-13888). The *Cour de cassation* has nonetheless several times had the opportunity to subject non-reaffiliation clauses to the same validity terms as post-contractual non-competition clauses (Cass. Com. 17 January 2006, appeal no.: 03-12382; Cass. civ. 2ème 10 January 2008, appeal no.: 07-13558).

149. Indeed, as the prohibition on reaffilation makes it not impossible but very difficult to operate a business and its profitability uncertain, the non-reaffiliation clause may validly be assimilated into a non-competition clause. This may also be the case if a non-affiliated retail outlet is unable to put real competitive pressure on affiliated retail outlets.

150. In fact, in the retail of daily consumer goods (supermarkets and hypermarkets) sector, the distinction between non-reaffiliation clauses and non-competition clauses appears to be particularly delicate. Indeed, more and more general food shops choose to affiliate to a retail-brand in order to benefit from an attractive commercial policy and brand image, including in the local food shop market. According to the *IFLS* (French retailer association)[34], nearly all local supermarkets (97.8% of shops and 97.9% of sales area) of more than 400m^2 are thus bound to large French retail chains and the role of retail chains in the smaller-sized formats also appears to be growing as 34% of local shops with an area of between 120 and 400m^2, i.e. 43.5% of total sales area of shops of this size, are already affiliated to a retail-brand. Thus, the larger a shop is, the more necessary affiliation to a network may be for its operation. The qualitative elements gathered from operators themselves also tend to confirm this assumption: by way of example, describing the factors for the success of local shops, the executive director of a retail chain mentioned the extent of the stock offered, the level of price acceptability, the new advertising system set up and the use of inter-format and inter-shop loyalty cards.

151. It thus appears that in the retail grocery sector, the fact of being affiliated to a retail chain constitutes, for independent retail outlets, a necessary element of the conduct of their business or, at least, a necessary condition to put competitive pressure on affiliated retail outlets. Thus, in this business sector, non-reaffiliation clauses may validly be assimilated with non-competition clauses.

Clauses which must be necessary and proportional to their purpose

152. In accordance with established Community and domestic case law, the *Conseil de la concurrence* allowed the presence of non-competition and non-reaffilation clauses in franchise agreements, subject to them meeting particular conditions of necessity and proportionality. In its decisions no. 96-D-36 of 28 May 1996 and no. 97-D-48 of 18 June 1997, the Council specified these terms: "*Given that non-affiliation and non-competition clauses can be considered an inherent part of the franchise insofar as they allow the know-how transmitted, which must only be of benefit to members of the network, to be protected and give the franchisor time to re-establish a franchisee in the exclusive rights area; these clauses must nonetheless remain proportionate to the purpose they seek; given that EEC Regulation no. 4087/88 provides that a non-competition obligation may only be imposed on franchisees after the expiration of the contract for a reasonable term which may not exceed one year and only insofar as such an obligation is necessary to protect the franchisor's industrial or intellectual property rights or to maintain the common identity and reputation of the network*".

153. In particular, Article 5.3 of EC Regulation no. 330/2010 of 20 April 2010 concerning the application of Article 101, paragraph 3, of the TFEU to categories of vertical agreements and concerted practices provides that the exemption by category does not apply to vertical agreements which contain any direct or indirect obligation prohibiting the purchasers, at the end of the agreement, from manufacturing, purchasing, selling or reselling goods or services, unless all the following conditions are cumulatively met: *a) the obligation concerns goods and services which are in competition with contractual goods or services; b) the obligation is limited to premises and lands from which the purchaser carried out its business during the term of the contract; c) the obligation is necessary to protect the know-*

[34] *Le commerce d'alimentation générale de proximité*, IFLS, 2007

how transferred by the supplier to the purchaser, d) the term of the obligation is limited to one year as of the termination of the agreement".

154. In this respect, in a ruling of 9 June 2009 the *Cour de cassation* (French Supreme Court), based on the requirements laid down by EC Regulation 2790/1999 (since replaced by Regulation no. 330/2010 mentioned above) overturned a court of appeal ruling which declared valid a post-contractual non-competition clause with a term of one year and applicable within a radius of 30km around the point of sale, provided in a franchise agreement made between *Distribution Casino France* (franchisor) and *Perrosdis* (franchisee): "*Whereas in ruling thus, although the benefit of the exemption provided in Article 5(b) of Regulation 2790/1999 in favour of post-contractual non-competition clauses is reserved uniquely for those, of a term of one year, which are limited to the premises or lands from which the contracting party has operated during the term of the contract and which is necessary to protect the know-how transferred to it by its co-contracting party, the court of appeal violated the abovementioned text*". (Cass. com. 9 June 2009, no. 08-14301).

Validity of clauses found in affiliation agreements with respect to the rules provided

155. The extent to which post-contractual non-reaffiliation and non-competition clauses provided in affiliation agreements are really necessary for the protection of know-how and the common identity and reputation of the network shall be examined and then the proportional nature of these clauses shall be considered with respect to their purpose.

The necessary feature of protecting know-how

156. With respect to the affiliation agreements transmitted to the investigation services and hearings held with operators, the know-how transmitted by retail-brands to their affiliates and members have three characteristics:

- Firstly, a part of this know-how is noticeable in the shop, particularly that relating to the physical layout of the shop, its product mix and plans for the placement of products. This therefore does not have to be protected by non-competition or non-reaffiliation clauses.
- Secondly, another part of this know-how is made up of unnoticeable but elements common to all retailers and essential for traders to carry out their business. In particular, these include the skills of the independent trader in the financial management or establishment of shops. Common to all shops, this know-how thus does not need to be protected either, as the profitability of its transfer is ensured by the long-term affiliation agreements made between independent retail outlets and their heads of network. This know-how integrates the experience and professional skills of the shop manager and thus it is not possible to prevent him from using it at the end of the contract.
- Thirdly, a final part of the know-how is made up of elements specific to the retail-brand and which are difficult to use by competitors, such as the know-how relating to the retail-brand promotion policy. This component of know-how may justify the presence of post-contractual non-reaffiliation/non-competition clauses even if, in most cases, this component of know-how can be protected perfectly by a confidentiality clause. Moreover, most affiliation agreements include such confidentiality clauses which, unlike post-contractual non-reaffiliation/non-competition clauses which prohibit the affiliate from

carrying out its business for a particular period of time at the end of the contract, are limited to prohibiting the affiliate from directly or indirectly re-using the know-how transmitted or disclosing it to a third party, subject to prosecution. Moreover, it should be noted that the independent retail outlet is often not the decision-maker of strategies likely to be relied on in this type of know-how as each retail-brand has its own guidelines on the matter. By changing retail-brand, the affiliate in fact abandons most of the know-how, specific and general, transmitted by the group it was affiliated to in order to adopt that transmitted by the new group it will be affiliated to. Thus, the possible transfer of know-how from one retail-brand to another by its independent retail outlets appears limited.

157. The know-how required or which could effectively be the subject of protection through non-competition or non-reaffiliation clauses seems relatively limited. In addition, post-contractual non-reaffiliation/non-competition clauses mentioned in the contracts of some retail-brands are only exercised if the contractual relation is terminated early, which tends to indicate that these are not linked to the fear of a "leakage" of know-how to competing retail chains; if this was the case, they would apply independently of the circumstance, termination or anticipated expiry date provided in the contract, leading to the termination of the contract.

The necessary and proportional character with respect to the purpose of protecting the common identity and reputation of the network

158. The inclusion of a post-contractual non-competition or non-reaffiliation clause in shareholders' agreements and lease management agreements also allow the identity and reputation of a retail-brand to be maintained by marking a disruption in the operation of the business, to make sure that the former affiliate does not take away with it an important element of the business by re-establishing it for itself. Similarly, a non-competition or non-reaffiliation clause appears necessary, when the affiliate owns its business and the business premises, or intends to carry out its business at another premises situated in the same customer catchment area, to mark a disruption in operation, so that the affiliate does not continue to benefit from the reputation and image acquired from its clients through its affiliation to a retail-brand.

159. Nonetheless, given the rapidity with which sales concepts evolve, the need to mark a disruption in the operation of a premises or a business by including a relatively long post-contractual non-reaffiliation and non-competition clause may be questioned. Moreover, given the relative weakness of the differences which exist between the different local food retailers, it does not thus appear necessary to impose long post-contractual non-reaffiliation and non-competition clauses on affiliates to maintain the network's image.

160. It should be noted that in accordance with Article 5.3 of Regulation no. 330/2010 mentioned above (see paragraph 153), post-contractual non-competition clauses must, to be able to benefit from the exemption, be simultaneously necessary to protect the know-how and limited to the premises from which the affiliate carried out its activities during the term of the contract on the one hand and limited to a term of one year as of the expiration of the agreement, on the other.

161. It appears that most post-contractual non-reaffiliation and non-competition clauses provided in the affiliation agreements studied do not meet the terms for necessity and proportionality with respect to the objectives sought and established by competition law.

5. PRIORITY RIGHTS FOR RETAIL CHAINS

162. Most of the contracts analysed include priority rights for retail chains on the sale of the shops of their affiliates which are valid for the whole duration of the relation and for several years afterwards (a), for which operators do not provide convincing justifications (b). Given the poor mobility of independent retail outlets between retail chains, the legal analysis of this type of clause raises questions about their anti-competition characteristics (c).

a) The inclusion, in most contracts, of priority rights valid throughout the entire term of the contract and for several years after the expiration date thereof

163. Most of the contracts analysed provide priority rights for retail chains on the sale of the shops of their affiliates. Generally, two types of priority right are used alternatively. The right of first refusal gives the original network the privilege of making the first offer of sale. If there is disagreement between the parties on the terms of the sale, the latter are determined by an expert. Purchase options allow the original network to bring itself into line with the offer made by a competing group.

164. The term of validity of these clauses varies according to the retail-brand. For some of them, the priority right granted by the affiliate to its head of network is only valid during the contractual relation. Nonetheless, in most cases, the priority right survives the term of the contract for terms which can run from one to fifteen years and sometimes even for an unlimited period.

165. All the priority rights provided are accompanied by a right of approval for the benefit of the retail chain: if the head of network waives its priority right, the buyer must nonetheless be approved by the latter to comply with the contract in force. The contract is otherwise considered to be terminated at the initiative of the affiliate.

b) Justifications provided by operators for the presence of these priority rights

166. Operators give two main justifications for the inclusion of priority rights in affiliation agreements. Firstly, these clauses may aim to ensure their affiliated retail outlets stay in the network, thereby sustaining the number of shops and consequently their purchase volumes and competitiveness. The survival of these clauses at the end of the contract may aim to counter the risk of the measure being worked around by an affiliate who, wishing to sell its shop to a competitor with a better offer waits for the expiration date of its contract to sell its shop to this competitor. Similarly, the relatively long term of priority rights may aim to prevent the measure being worked around, for example by an integrated operator who is satisfied to hand over the independent retail outlet in order to buy it back once the priority right has expired.

167. Secondly, co-operative groups justify the presence of such clauses as being a means of countering "predatory" practices in integrated networks which, with greater financial resources, would be able to outbid them to purchase shops and commercial premises, and thus improve their purchase power and competitiveness.

168. The relevance of these arguments remains highly relative nonetheless. Firstly, while these priority rights aim to complete the measure intended to prevent independent retail outlets from leaving one retail chain for another, they then add long terms of commitment and the

non-competition clauses already noted, intended to allow retail chains to make a profit on know-how and, in some cases, the business transmitted.

169. Secondly, it is not up to the distribution network to determine the optimal method of organising the (integrated or affiliated) distribution sector and to prevent their members from choosing one or the other of these two methods. In this case, the competition between these various formats to increase the size of their networks must be arbitrated by consumer choices, which place greater importance on the method of organisation which provides them with the best value for money and not by discriminatory clauses included in affiliation or franchise agreements. When the acquisition is likely to restrain consumer choice excessively, the assessment of its effects remain the sole means for the competition authorities, who, according to the level of competition in the customer catchment area, authorise the planned acquisition or not. The lowering of notification thresholds for mergers made in the retail trade sector specifically allow an assessment of the repurchase of independent retail outlets as the amounts in question (15 million euros annual turnover) are sufficiently large for financial restrictions to be able to prevent some groups from participating in this competition.

c) Legal analysis of priority rights provided in affiliation agreements

170. The French competition authorities have already had to deal with priority rights of the type employed in franchise or affiliation agreements. In its decision no. 95-D-39 of 30 May 1995 on practices in the rental of large-format advertising space sector, the *Conseil de la concurrence* held that "*the end of lease preference clause creates an imbalance in the negotiation of the lease of spaces by allowing the current bill poster artificially to limit the risk of losing the space; indeed, by using this clause, the lessor of a space at the end of the lease knows at all times the identity and amount of the offers made by its competitors and has the guarantee of always keeping its space without having to outbid on a competing offer; on the other hand, a competitor wishing to obtain the lease of a space previously rented by another company can never be ensured, even if it outbids, that it will be able to obtain the desired space; the companies concerned recognised the effectiveness of the end of lease preference clause in limiting the mobility of billboards; thus, this clause, which cannot be considered necessary to protect the quality of products, has the effect of artificially restricting the play of competition in the large-format advertising space market by limiting the variability of advertising spaces between bill posters beyond the six year period set as the maximum term of space rental agreements by the Law of 29 December 1979*".

171. Similarly, in its opinion no. 09-A-21 of 24 June 2009, the *Autorité de la concurrence* recommended to the government, with respect to independent service stations, that it "*prohibits preference clauses which provide that the supplier has a priority right to buy back the business if the independent retailer retires*" (paragraph 240); this is in order to avoid the "*consolidation* [of integrated networks] *by buying back independent retail outlets and making management through lease-management widespread*" (paragraph 230).

172. Purchase options which provide the possibility for the head of network to come into line with the conditions of the best buyer, and thus to conclude the sale, creates for the beneficiary retail chain an imbalance in the negotiation of the buyback of its affiliated retail outlets by allowing it to limit artificially its risk of seeing these shops being bought back by competitors. Indeed, by using this clause, the beneficiary retail chain, at all times, knows the identity and amount of the offers by its competitors and is practically guaranteed, unless it cannot or does not want to pay, of always being able to keep its

affiliated retail outlets in its network without having to outbid on a competing offer. On the other hand, this type of clause deters competing retail chains from entering into negotiations with the owner of the shop wishing to sell his shop. Indeed, their buyback offers, whose composition may appear relatively costly given the various expert reports and assessments they require, have little chance of succeeding, as the retail chain benefiting from a priority right can provide equivalent terms and conditions in the contract of sale. The lack of incentive for competing groups to draw up purchase offers reduces the negotiating power of the shop owner and thus increases that of the head of network, which can ensure the sustainability of its network at a lower cost.

173. The right of first refusal which obliges the affiliate to offer, as a priority, the sale of its shop to a head of network also raises concerns for competition. Indeed, in this hypothetical case, the shop owner does not have the possibility of seeking offers from competing groups before first offering its shop for sale to its head of network. The fact that the shop offered for sale is not subject to market rules and that its sale price is thus set by an assessment method provided in the contract or by an expert reduces the value of the shop, thereby allowing the head of network beneficiary of the shop to keep shops within its network at a lower price.

174. It appears that both purchase options and the right of first refusal granted to retail chains have the effect of artificially restricting the play of competition by limiting the possibility of the buyback of independent retail outlets by competing retail chains.

175. Moreover, these measures deter competing retail chains from accepting in their network an affiliated retail outlet encumbered by a priority right in favour of its former head of network, for a particular number of years or an unlimited period.

176. These clauses constitute real barriers to entry as they prevent any new entrant accessing the network of independent retail outlets. Indeed, the presence of this type of clause in most affiliation agreements is likely to create an artificial territorial division of retail chains: the fact that each operator has the possibility of reserving the vacant premises of its former affiliates results in perpetually fixing the geographic location of retail chains.

177. These measures consequently contribute to the poor mobility of shops between retail-brands and the competition concerns this raises.

B. CAPITAL LINKS THAT CONSTITUTE OBSTACLES TO THE MOBILITY OF INDEPENDENT RETAIL OUTLETS BETWEEN FOOD RETAIL CHAINS

178. More and more frequently, retail chains, both integrated and co-operatives, acquire minority interests in the capital of the operating companies of their affiliates giving them a blocking minority.

179. Some integrated retail chains, but not all, have developed a very active policy of acquiring an interest in their franchise shops.

180. These acquisitions of holdings generally vary between 26% and 50% of the capital of the company operating the affiliate, frequently giving retail chains a blocking minority. Moreover, by using brand name clauses and majority rules provided in articles of associations and/or shareholders' agreements, retail chains have an actual right of veto concerning the change of the retail-brand of the shop. Furthermore, shareholders' agreements often provide a mutual priority right between shareholders to the company's securities, through which shareholders mutually agree, if they sell their securities, to give

preference to other shareholders at a determinable price based on an investment ratio and valuation rules provided in the agreement. Shareholders' agreements generally have a non-competition clause forbidding natural person affiliates (unlike non-competition clauses in franchise agreements which bind operating companies) who have transferred all of their securities, from carrying out a competing activity for several years, in particular by being a shareholder in a company operating a food shop.

181. Co-operative groups also contribute to the capital of member companies. Indeed, Article L. 124-1, 7, of the Commercial Code allows co-operatives to "*acquire holdings, including majority holdings, in direct or indirect members' companies running a business*". This is an increasingly frequent practice.

182. The *Autorité* has analysed some of these acquisitions of holdings as part of merger control. By way of example, as part of decision no. 10-DCC-88 of 4 August 2010 on joint takeover of *Nico* by *Marchal*, it stated that the articles of association of the operating company of the *Intermarché* member (in this case, *Nico*) gave *ITM Entreprises*, through its preference action for a period of 25 years, the chance to block any change of retail-brand, to oppose any transfer of shares and oblige majority shareholders to assign the business as soon as they operate a similar business under a competing retail-brand. Moreover, the articles of association provide that beyond this period, *ITM Entreprises* maintain a priority right, in the case of transfer, for a period of 5 years. These elements allowed the *Autorité de la concurrence* to hold that *ITM Entreprises* had joint control over this company.

183. In addition to "vertical" acquisitions of holdings, i.e. by the head of network in the member's operating company, the enquiry also observed the existence of "horizontal" acquisitions of holdings, i.e. by one or more members in the operating company of another member. In this hypothetical case too, some statutory provisions and shareholders' agreements guarantee that the operating company and the shop may stay in the network of this group.

184. If necessary, acquisitions of holdings by retail chains in the capital of the operating companies of the affiliated retail outlets may be the subject of notification to the *Autorité de la concurrence*, for merger control (see below, paragraph 198). Nonetheless, it should be noted that unlike vertical acquisitions of holdings, horizontal acquisitions within co-operative groups have thus far never given rise to notification for the purpose of merger control, as the turnover taken into consideration is that of members who are parties to the merger and not that of the co-operative group overall.

VI. Competitive analysis of practices observed with respect to affiliation and recommendations

185. The poor mobility of affiliated retail outlets between competing distribution networks, in part due to the contractual and corporate practices implemented by the various retail chains (A), produces anti-competition effects both on the upstream supply market and the downstream retail sales market (B). The practices observed are likely to be stopped by competition law but, to date, the *Autorité de la concurrence* prefers to draft recommendations that it intends to see followed up by operators and the relevant professional bodies (C).

A. OBSERVATIONS

186. The contractual and corporate practices observed, which have the purpose and/or effect of obstructing the mobility of affiliated retail outlets between competing networks (1), produces anti-competition effects both on the upstream market and the downstream market of the food distribution sector (2).

1. SUMMARY OF VARIOUS OBSTACLES TO MOBILITY OBSERVED

187. The enquiry shows the contractual and corporate practices implemented by retail chains and explained above which limit the mobility of shops between competing retail-brands, which have already been obstructed by the economic risks inherent in any change of retail-brand.

188. The long length of contracts and their automatic renewal constitutes a first obstacle to the mobility of independent retail outlets between retail chains. In some cases, this obstacle is reinforced by the de facto interdependence which exists between the various contracts binding the affiliate and the retail chain, by the high compensation rates provided in the case of early termination and by the payment of deferred subscription fees by the affiliate, i.e. on the date of the termination of the contract. The arbitration clauses included in some contracts also contribute to making any action to settle disputes between groups and their affiliates costly.

189. Secondly, even when the contract has been terminated, some former affiliates remain bound to their head of network by post-contractual non-reaffiliation and non-competition clauses. Consequently, after leaving the network, they are unable to manage a shop within a competing network.

190. A third difficulty is linked to provisions which limit the chances affiliates may have to transfer their business to a third party in the network. The priority rights mentioned in contractual documents apply for a generally long period, during which groups have a right of first refusal or purchase option on the sale and/or lease-management of the shop and/or the shares of the operating company. The difficulty of transferring a business to a third party in the network seems, moreover, reinforced, for a large and growing number of affiliates, by the existence of acquisitions of holdings with a blocking minority by the various retail chains in the business of affiliates, allowing them to monitor the identity of potential purchasers.

191. All of these practices create many disputes, often brought by retail chains when one of their affiliated retail outlets leaves for a competing network. Most often, these conflicts give rise to long and costly legal or arbitral actions and thus constitute an additional deterrent to independent retail outlets wishing to leave their network.

2. IMPACT OF THE POOR MOBILITY OF INDEPENDENT RETAIL OUTLETS ON THE PLAY OF COMPETITION

192. The contractual and corporate obstacles to changing retail-brand and the resulting poor mobility of independent retail outlets between distribution networks must be analysed in view of the structure of the retail of daily consumer goods (supermarkets and hypermarkets) sector. The enquiry showed that many customer catchment areas remain

excessively concentrated, due to major barriers to establishment in this sector. It also showed that in spite of the lack of exclusive supply clauses in contracts binding them to their head of network and its central purchasing body, independent retail outlets tend to be supplied, for the main part of their needs, by the retail chain to which they are linked. For this reason, an operator who wishes to enter a customer catchment area or distribution circuit it is not yet present in and to allow consumers to benefit from a more competitive commercial policy must have a number of integrated or affiliated retail outlets: it cannot in practice sell its goods to independent retail outlets affiliated to competing groups.

193. In this sectorial context, any obstacle to the greater mobility of independent retail outlets between networks is thus damaging to the efficiency of the food retail sector and the benefits consumers could draw from it. Indeed, given the obstacles to creating new shops, the entry of a new operator on the upstream supply market can probably only take place by relying on independent retail outlets from the existing distribution networks. The legal obstacles to changing retail-brand make it nonetheless almost impossible to implement such an entry strategy, as has been shown elsewhere in the growth strategies of existing operators, who, in spite of their limits, give preference to the creation of shops rather than affiliation, franchise or the buyback of competing shops. On the other hand, affiliation agreements allowing real mobility for independent retail outlets could encourage the entry of a new operator.

194. Moreover, the obstacles to entry resulting from the lock-in of affiliation and franchise agreements also produce their effects on local markets. As stated previously, many customer catchment areas show a particularly high level of concentration, particularly due to the limited number of retail chains in these areas (rather than the number of shops actually established). A greater mobility of independent retail outlets between retail-brands could thus allow the entry of retail chains in customer catchment areas in which they are not yet present and this is all the more so as the shop ratio in some customer catchment areas is already high, which makes the arrival of an external competitor all the more difficult. Currently, nonetheless, contractual and corporate obstacles to the mobility of independent retail outlets between retail-brands deter the implementation of such strategies: operators thus give preference to the creation of shops, which is more costly and slow.

195. More open affiliation agreements would also allow independent retail outlets to compete more frequently with retail chains and thus benefit from better services on their part, such as lower purchase prices, a better quality of supply and better communication from the retail-brand. This competition with retail chains by independent retail outlets would essentially benefit consumers, who would have part of the benefits thus acquired by independent retail outlets transferred to them. It would also allow consumers to benefit fully from the competition which is likely to exist between operators active in the national retail of daily consumer goods market, which is often greater than that they can exercise in local retail markets which are clearly more concentrated than the national market. More open affiliation agreements are thus all the more necessary as the obstacles to the creation of new shops; the number and size of new independent retail outlets likely to join retail chains are too limited to restrict them to making their terms of affiliation more flexible.

B. PRACTICES LIKELY TO BE STOPPED BY COMPETITION LAW AT THE EXPENSE OF LONG LEAD TIMES AND SIGNIFICANT UNCERTAINTY

196. In the preamble, the *Autorité de la concurrence* states that, within the scope of an opinion, describing the behaviour in a market with respect to Articles 101 and 102 of the TFEU and Articles L. 420-1 and L. 420-2 of the Commercial Code does not fall within its power. It may only conduct such an assessment by carrying out inter partes proceedings, such as provided by Article L. 463-1 of the Commercial Code. In this section, the legal tools which the *Autorité de la concurrence* has to monitor and, where necessary, correct the conduct observed with respect to affiliation agreements in the retail of daily consumer goods sector will be mentioned here in a non-exhaustive manner.

197. Practices that consist, for a retail chain, of taking control of its affiliates through distribution agreements or the acquisition of holdings may fall within the scope of merger law in very specific circumstances and subject to the turnover of the shops involved meeting the notification thresholds (1). Litigation may also be brought against retail chains which bind their independent retail outlets excessively. These proceedings are nonetheless lengthy and uncertain. A solution in concert with operators would hence offer efficiency advantages (2).

1. UNDER MERGER CONTROL LAW

198. Paragraphs 581 et seq. of the *Autorité de la concurrence* guidelines on merger control show the application made by the competition authorities of the ordinary law of mergers to relations within distribution networks. While it does not exclude that the conclusion of a distribution agreement can confer on a head of network a decisive influence on the activity of a shop (a), it is essentially through minority acquisitions of holdings that merger law is able to control the organisation of distribution networks (b).

a) Control by the head of network of its members by concluding a distribution agreement

199. The guidelines state that the conclusion alone of a distribution agreement is likely to confer decisive influence in the meaning of Article L.430-1 of the Commercial Code only in very specific cases. In particular, the typical provisions included in brand name and franchise agreements (compliance with sales standards, for example) do not give the head of network a decisive influence over its franchisees as they continue to bear the commercial risks inherent in their activity (stock management, pricing policy).

200. Nonetheless, taken jointly with other de facto and de jure elements, distribution agreements are likely to confer on the head of network a decisive influence over its members. The *Autorité de la concurrence* can thus hold that distribution agreements accompanied by a transfer of assets (stocks, premises, business, share in capital - see point b below) are likely to give the head of network control over the assets of its affiliates, subject to it being possible to attribute to these assets a set turnover and that the merger notification thresholds are met. Similarly, distribution agreements limiting the autonomy of affiliated retail

outlets, both in their commercial policy and their chances of changing network, can grant the head of network a decisive influence over the affiliated retail outlet[35].

b) The head of network's control of its members by a minority acquisition of holdings granting it a blocking minority on strategic decisions

201. The acquisition of a minority holding by the head of network may also, in some cases, constitute a merger, particularly when it is accompanied by a modification of the articles of association of the company in question. The *Autorité de la concurrence*, in this case, will assess to what extent some clauses in these articles of association are likely to confer on the minority shareholder a decisive influence on the members. In particular, while these articles of association specify the retail-brand under which the member must carry out its activity and which may only be modified with the agreement of the minority shareholder, the head of the distribution network is able to prevent the member leaving the network and, along with the distribution agreement, the minority holding confers a decisive influence on the head of network. It is the same when the stipulations of the articles of association set a very long time period during which the member cannot leave the network, or the member is prevented de facto from leaving the network for a very long period. Such provisions may be the consideration for holdings equal to a small blocking minority (34% in a public limited company, 26% in a limited liability company), even by holding a single preferred share. In this respect, the guidelines refer in particular to the *Autorité*'s decisions no. 09-DCC-06 of 20 May 2009, *ITM/Evolis* and no. 09-DCC-064 of 17 November 2009 *ITM/Mikery*.

c) Limits of the sole recourse to merger law to review the contractual provisions binding independent retail outlets and their heads of network

202. With the exception of cases in which the contract binding the independent retail outlet to its head of network is accompanied by a minority holding, the re-classification of some affiliation agreements through mergers remains rare. This reclassification has a certain legal uncertainty which is damaging to operators, and particularly to independent retail outlets, and its wider use would significantly increase the cost of merger proceedings, both for companies and the authorities. More generally, merger law only applies when the operation meets the notification thresholds, regardless of its type: majority holding, minority holding resulting in decisive influence, contract resulting in decisive influence. For the record, the *Loi de modernisation de l'économie* (law on the modernisation of the economy) of 4 August 2008 lowered the merger notification thresholds for shops in the retail sector, from 150 to 75 million euros for the "comprehensive" threshold and from 50 to 15 million euros for individual thresholds. This being the case, merger control must henceforth apply to operations concerning hypermarkets and large supermarkets, but not those concerning local food shops, or medium-sized supermarkets (up to approximately 2,000m^2). In

[35] By way of example, the Minister of Economy, decided that an almost-exclusive supply agreement granted the supplier a decisive influence over the actual management and commercial policy of its distribution network (Min. Eco. 5 March 2009, Inbev/Pédanadel). It held that the decisive influence was established as the exclusive supply agreement between the supplier and members of the network, for a considerably long term (10-15 years), in particular provided the application of very strict penalties for the non-performance of annual progress objectives, the existence of a purchase option and the impossibility of renegotiating purchase volumes, payment amounts and penalties.

particular, the acquisitions of holdings made before the reduction in thresholds remain acquired. The acquisitions of holdings by some co-operative groups evade merger control by being carried out not by the head of network but by some shops which are members of the group.

2. UNDER ANTITRUST LAW

203. In this opinion, the *Autorité de la concurrence* holds that the characteristics identified in franchise and affiliation agreements have restrictive effects on competition in the various retail of daily consumer goods markets. These practices may thus be the subject of litigation, through inter partes proceedings, in application of Art. 420-1 of the Commercial Code and Article 101 of the Treaty on the Functioning of the European Union (a). They may also be, under several conditions, prosecuted under the prohibition of the abuse of economic dependence (b).

a) In application of the legislative provisions on vertical agreements

204. None of the retail chains, considered suppliers of products via their central purchasing bodies, holds a market share greater than 30%. Similarly, none of the shops represents more than 30% of sales made in this market. The thresholds below which an exemption by category may be granted, in the absence of hardcore restrictions, thus do not appear to have been crossed.

205. In practice, the restrictive effects on competition of the affiliation agreements described above arise in part from the spread of clauses hindering the mobility of independent retail outlets throughout the sector and on the other hand, the market power of the shops or retail chains implementing them in some customer catchment areas. An analysis carried out in customer catchment areas would naturally be a source of disputes due to their high number and the uncertainties that may remain as to their delimitation in terms of products and geographic borders. The difficulties of such an investigative method appear to have been implicitly recognised by the European Commission when publishing new guidelines on vertical restrictions (2010/C 130/01), which do not refer to the retail sale or resale of products or services market but to the "upstream" market in which suppliers possibly implicated sell their contractual products to the purchaser and to the market in which the distributor purchases contractual products.

206. On the other hand, the practices observed may be reviewed through the application of the "cumulative effects" theory. In practice, Article 6 of the exemption regulation effectively authorises the Commission or a Member State to remove the benefit of the exemption on vertical agreements when access to the market in question or competition therein are significantly restricted by the *cumulative effect* of parallel networks with similar vertical restriction applied by competing suppliers, i.e. when these restrictions produce similar effects on the market and the operators resorting to them cover more than 50% of the market in question. In this case, both co-operative groups and integrated networks developing the franchise for particular sales formats have set up contractual systems contributing to protecting their respective networks and avoiding the loss of points of sale insofar as is possible, so that the 50% threshold thus defined appears to have been clearly crossed. Similarly, while the particular characteristics of contracts binding shops to retail chains can differ (term of commitment, post-contractual clauses and rights, presence or otherwise of deferred entry fees, supply rates from the central purchasing body, etc.), they

appear nonetheless to be of a kind that produce similar effects of barriers to entry to a market. If the existence of cumulative effects was, where applicable, demonstrated, the *Autorité de la concurrence*, in view of Article 7 of the exemption regulation, could have the chance of withdrawing the benefit of the exemption from the affiliation agreements of the main food retail chains, which would allow these agreements to be described as anticompetitive practices in view of Articles L. 420-1 of the Commercial Code and 101 (1) TFEU.

207. However, possible litigation could result in considerable time taken and greater legal insecurity for operators, given the investigative methods (analysis of market share in customer catchment areas, assessment of the cumulative effect caused by a series of similar contracts) which could have been used. In these conditions, alternative methods of improving the flexibility of distribution networks appear, firstly, to have been sought. Insofar as, given the limited number of new shops likely to make the heads of network compete, there are few incentives for retail chains to reduce the lock-in effects in their contractual and corporate measures, legislative proposals appear to be a remedy suited to the failures observed in relations between retail chains and independent retail outlets.

b) In application of the legislative provisions on the abuses of economic dependence

208. The practices observed may also, where applicable, contribute to defining the abuse of economic dependence of some conduct. Indeed in its *SEFAG* decision no. 10-D-08 of 3 March 2010, the *Autorité de la concurrence* stated that the emphasis on a situation of economic dependence of franchisees with respect to a franchisor may result from the accumulated use of a series of contractual clauses imposed by the latter, the purpose of which is to limit the chances for franchisees to leave the network and restrict their contractual freedom to proportions that go beyond the inherent purposes of a franchise, without the circumstances in which these clauses had been intentionally agreed to being binding on them (paragraph 163 of the decision). In this case, concerning the case in question in the above decision, the state of economic dependence in relations between *Carrefour* and its distribution network could not be emphasised due to the lack of elements in the individual situation of each franchisee with respect to a subsidiary of the *Carrefour* group and in the absence of consistency in the position of franchisees within the *Carrefour* network (paragraph 166 et seq. of the decision).

209. Thus, it appears that the contractual and corporate practices identified in the scope of this opinion could, if applicable, allow the existence of a state of economic dependence between a retail chain and its affiliates to be established. Nonetheless, for the definition of an abuse of dependence to be held, after having reported the existence of a state of economic dependence between the retail chain and each of its affiliates concerned, the abusive behaviour of the retail chain towards its affiliates must be demonstrated, which may in particular consist of the implementation of one or more practices which restrict competition provided in I of Article L. 442-6 of Commercial Code, and that this affects the state of competition, for example, if it occurs in a concentrated customer catchment area. The demonstration of such an anti-competitive practice appears, clearly, to be less easy as it would have to be carried out in each case in a particular way. Given the widespread nature of the contractual and corporate measures observed in the retail of daily consumer goods sector, such a method hardly appears effective to remedy the competition concerns described in this opinion.

C. THE AUTORITE DE LA CONCURRENCE'S RECOMMENDATIONS

210. Several measures could allow the flexibility of distribution networks to improve. These aim, on the one hand, to allow independent retail outlets to choose freely and clearly the retail chain they decided to become an affiliate of (1), and on the other hand, to limit the term of commitments made and to facilitate the terms for leaving networks in order to increase the mobility of shops between competing networks (2). These recommendations could, firstly, be implemented with the assistance of professional organisations in the sector. Otherwise, to make operators follow the recommendations provided, the involvement of the legislator may be necessary (3).

1. THE NEED TO ALLOW INDEPENDENT RETAIL OUTLETS TO MAKE A FREE AND CLEAR CHOICE ON THE RETAIL CHAIN THEY DECIDE TO AFFILIATE TO

211. An independent retail outlet seeking affiliation must be able to compare the terms of affiliation offered by different groups. A network offering shorter terms of commitment and/or exit terms which are more beneficial could thus be able to attract a larger number of candidates. Nonetheless, the representatives of the independent retail outlets interviewed during the enquiry repeatedly emphasised that they measure the implications of their commitment poorly and in particular, the restrictive terms for leaving the network to which they are often subject.

212. It thus appears necessary to make the terms of affiliation more transparent in order to allow candidates for affiliation to make their choice freely and clearly. In this respect, it is recommended that operators formalise all the terms of the relationship with the affiliate in a single framework agreement (a), communicate this single framework agreement as early as possible for negotiations (b) and to emphasise pre-contractual information for the attention of the affiliation candidate (c). Indeed, once the retail chain is chosen, the affiliation candidate enters into negotiations with the head of network, which, both financially and in human terms, reduces the chance for the candidate to later go back on its choices even though no contract has as yet been signed.

a) Formalisation of the relation between the affiliated retail outlet and its head of network in a single framework agreement

213. The large number of contractual documents to formalise one and the same contractual relation is a source of confusion and legal insecurity, as the risk of contradictory clauses in different documents is increased. Consequently, following the example of the single framework agreement aimed at governing relations between the supplier and distributor provided in Article L. 441-7 of the Commercial Code, the *Autorité de la concurrence* recommends that operators formalise the terms of the relation between the affiliate and their head of network through a single framework agreement supplemented, where necessary, by one or more implementation contracts. The drafting of such a framework document would have the advantage of making the terms of the relation more transparent and where applicable, would facilitate the work of the control authorities. Moreover, this single framework agreement, which must in particular mention the common provisions on the various "aspects" of the relation such as the term clause, terms for termination, terms for dispute resolution or even the jurisdiction clause, would limit the presence of contradictory clauses and the related legal insecurity.

b) Communication of the draft single framework agreement and implementation agreements must be completed sufficiently far ahead of the negotiations

214. Several representatives of independent retail outlets emphasised the length of the affiliation process to a retail-brand. Indeed, between the time that the first contact is made and when the parties sign the contractual documents, a certain amount of time passes during which the parties assess their incentive and the relevance of their joint project. In particular, it is during this period that the affiliation candidate seeks financing and sponsorship. During this period, the affiliation candidate also carries out the training provided by the retail chain and/or person paid to do so by the group. By the time of the last stage of negotiations and the signing of the contract, the affiliation candidate has thus already invested a considerable amount of time and personal effort in the proposed affiliation and is thus unable to challenge or attempt to negotiate the affiliation conditions which are then sent to it. Moreover, at this stage, it is too late to compare the terms of affiliation with those of competing groups as it can only give up its affiliation plans with difficulty, unless it also waives the investments it has already made and starts a new, long and difficult, affiliation process with another retail chain. In these conditions, it thus appears necessary that the affiliation candidate has, as early as is possible, communicated to it the draft single framework agreement and its possible implementation agreements.

c) Reinforcement of pre-contractual information for the attention of the affiliation candidate

215. Law no. 89-1008 of 31 December 1989, the "*Doubin Law*" introduced a pre-contractual obligation on the head of network to provide information to the affiliate. In this respect, Article L. 330-3 of the Commercial Code provides that: "*Any person who makes available to another person a retail name, trademark or retail-brand, by demanding from it an exclusive or almost-exclusive rights commitment for the performance of its activity, must, prior to signing any contract made in the common interest of the two parties, provide the other party with a document giving honest information, which allows it to commit knowingly*". This document must in particular mention the term, terms of renewal, termination and transfer of contract as well as the scope of exclusive rights (Art. L. 330-3 (3) and R. 330-1, 6 of the Commercial Code).

216. In this respect, the *Autorité de la concurrence* recommends to operators that the information given concerning the term, the terms of renewal, termination and transfer do not relate only to the franchise agreement (or equivalent) strictly speaking but to the whole contractual relation which, as has been seen, may be formalised through various documents (franchise agreement, supply agreement, lease agreement, lease-management agreement, articles of association of the operating company, shareholders' agreement, etc.). In addition, it is recommended that operators mention, among the information given at this stage, the presence of clauses restricting the freedom to affiliate during the termination or expiry of the contractual relation, including possible priority rights in favour of the head of network, post-contractual non-reaffiliation and non-competition clauses, etc.

2. THE TERM OF COMMITMENT MUST BE LIMITED AND THE TERMS TO LEAVE NETWORKS FACILITATED

217. Transparency increased by the terms of affiliation offered by the various retail chains should reinforce the competitiveness of distribution networks for the independent retail

outlets seeking to affiliate. Nonetheless, given the size of the existing number and difficulties of opening new shops, these measures may only have a moderate impact as they can only produce effects on new independent retail outlets. The mobility of independent retail outlets already affiliated to a retail chain should thus also be facilitated by reducing the term of commitment made (a) on the one hand and by reducing the terms for leaving the networks they are subject to. This reduction must be based on standardising the term and method of termination of the different contracts that make up the contractual relation (b), a prohibition on priority rights for heads of network (c), a framework for post-contractual non-reaffiliation and non-competition clauses (d), a staggering of the payment of subscription fees instead of their deferred payment (e), and a framework for capital holdings by retail chains in the capital of the companies operating their affiliated retail outlets (f).

a) Reduction in the term of commitments made

218. The enquiry has shed light on the relatively long terms of some contracts made between affiliates and their heads of network, some of which can run from 3 to 30 years and are most often automatically renewable for equivalent terms.

219. It also appears that the terms of contracts noted are far higher than necessary for the redemption of specific investments made by the parties, which are moreover not risky or for which the danger of free riding is limited.

220. In a sector marked by major obstacles to the creation of new shops, a high degree of market concentration in the retail market, almost-exclusive relations between retail chains and their affiliated retail outlets and in which the alignment of independent retail outlets to a retail-brand represents for the latter a major factor for development, very long terms of commitment result in effects that restrict competition both on the upstream market supplying shops and the downstream market of the resale of these goods to consumers. A shortening of the term of contracts could facilitate the mobility of independent retail outlets between retail-brands, reduce barriers to entry and reinforce the competition between retail chains.

221. Nonetheless, a sufficiently long term of commitment may also produce a particular efficiency. It may thus allow the affiliate to secure the investments made in assets specific to its retail chain even if these are relatively limited, as has been seen. Moreover, it may constitute a guarantee with respect to banking institutions which grant loans to affiliates necessary to set up shops. The terms of commitments made by the retail chain should thus not be too short, at the risk of depriving the affiliation candidate of an element securing their plans. As has been mentioned above (paragraph 73), there is a de facto almost-exclusive supply agreement between independent retail outlets and the retail chains they are affiliated to. In this respect, Article 5 (1) (a) of Commission Regulation no. 330/2010 on vertical restrictions provides that any non-competition obligation, including exclusive supply obligations, found in vertical agreements and whose term is unspecified or exceeds five years may not be exempt. Article 5 (1), *in fine* of the Regulation specifies, moreover, that a non-competition obligation automatically renewable beyond a period of five years is considered to have been made for an unspecified term.

222. Consequently, the *Autorité* requests operators to limit the term of contractual commitments made with their affiliated retail outlets to a maximum term of five years and to modify, in this way, contracts currently being performed. Moreover, the parties should avoid having

the chance to renew their contract automatically upon its expiry, to encourage the parties to enter into negotiations on the terms of a possible new contract.

223. Nonetheless, on its own, a reduction in the term of commitments would not be enough to meet the competition concerns raised by the contractual provisions binding independent retail outlets and retail chains. On the one hand, the term of commitments is frequently extended by various contractual provisions which survive the term of the main contract. On the other hand, a reduction in the term of commitments risks damaging independent retail outlets if those wishing to change network are unable to enter a contract rapidly with another retail chain at the end of their affiliation agreement.

b) Standardisation of the term and method of terminating the various contracts constituting the contractual relation

224. The enquiry noted that in some cases, the various contracts binding the affiliated retail outlet to its head of network could have had different terms or different expiry dates and termination conditions. In addition to creating a certain legal uncertainty, these discrepancies and differences between the various contracts have the effect of artificially extending the term of the commitments made. The *Autorité de la concurrence* thus asks operators to standardise the term and method of termination of all the contracts which make up the current and future commercial relation. The conclusion of a single framework agreement, such as is recommended by the *Autorité* (see above, paragraph 213) should also allow operators to standardise the term and method of termination of commitments made by parties in the future.

c) The prohibition of priority rights in favour of heads of network

225. Most of the contracts studied during the enquiry provide a priority right (right of first refusal or purchase option) in favour of the retail chain, which is usually valid during the term provided for the contract as well as several years after it has expired. The wish of retail chains to secure their investments and ensure the continuity of their network does not justify the presence of such clauses in contracts.

226. This type of clause, moreover, creates an imbalance in the negotiation of the sale of the shop, with the beneficiary retail chain being guaranteed to be able to keep the shop against possible competing offers. This imbalance is likely to deter competing retail chains from eliciting independent retail outlets from other retail-brands and thus freezing the retail markets and play of competition.

227. Consequently, the *Autorité de la concurrence* asks operators not to include in contracts priority rights or similar provisions for the benefit of the head of network and not to implement those relating to contracts being performed, at the very least when the retail chain is not the owner of the premises of the shop and does not have any financial holding in the operating company. Indeed, from this view, reopening the retail-brand to competition with other competing retail-brands is facilitated by the real freedom to act the operating company has to make a new partnership with another more effective retail chain. It is clear that in the case that the retail chain actually is a partner in the development of the independent retail outlet (holding of capital corresponding to actual financial assistance from the retail chain, owning the premises or business), the existence of a priority right or a similar provision appears fair.

d) Regulating post-contractual non-reaffiliation and non-competition clauses

228. According to the elements gathered during the enquiry, the post-contractual non-reaffiliation and non-competition clauses mentioned in the contracts made between retail chains and their affiliates may, in some cases, be necessary to protect the know-how and maintain the common identity and reputation of the network but are not always proportional to this objective (see above, paragraphs 142 et seq.). With respect to the provisions of Regulation no. 330/2010, a term of one year and only for the shop which is the subject of the contract in question could be considered to limit the post-contractual non-reaffiliation and non-competition clauses found in affiliation agreements, and should apply to new contracts as well as those currently being performed.

e) Staggering the payment of subscription fees instead of their deferred payment

229. Deferred subscription fees allow the affiliate to pay subscription fees only upon expiry of the contract. While it allows independent operators thus to reduce the financial restrictions on their accounts during the first years of business, this provision carries the risk of limiting their commercial freedom by deterring them from leaving the network. In accordance with the recommendations made on the www.pme.gouv.fr website, it is thus recommended that such deferred fees are removed, including in contracts currently being performed and that they are replaced with the possibility of staggering the payment of subscription fees over a sufficiently short term.

f) Regulating capital holdings by retail chains in their affiliated retail outlets' operating companies

230. Most retail chains, both co-operative and integrated groups, more and more frequently acquire minority holdings in the capital of the operating companies of their affiliated retail outlets.

231. These holdings grant them a power to control the management of their affiliates' operating companies. In particular, they most often have a right of veto which in particular allows them to oppose any change to the shop's retail-brand. Moreover, the articles of association of these operating companies or the related shareholders' agreements frequently contain priority rights for the benefit of the retail chain and post-contractual non-competition clauses borne by the affiliate. Consequently, these holdings create a serious obstacle to the mobility of independent retail outlets between different retail-brands.

232. These holdings most often constitute mergers but as they do not go beyond the notification thresholds applicable to retail sales (L. 430-2-II of the Commercial Code) or which were carried out before the entry into force of the *loi de modernisation de l'économie* (law on the modernisation of the economy) and the reduction of notification thresholds applied to retail trade, they do not have to be controlled by competition law. Nonetheless, these practices have a lock-in effect on shops and thus need to be regulated. Regulating holdings could in particular consist of prohibiting brand name clauses in the articles of association and shareholders' agreements of operating companies. Indeed, these clauses which grant a right of veto to the retail chain against any decision concerning a change of retail-brand of the shop in question, prevents the affiliate from changing network at the end of the contract, where applicable.

3. TERMS FOR THE IMPLEMENTATION OF THESE RECOMMENDATIONS

233. The implementation of these recommendations requires the legislator's involvement. It is indeed through its involvement that clear and rapid responses to the competition restrictions highlighted through the enquiry may be provided.

CONCLUSION

234. At the end of its analysis, the *Autorité de la concurrence* believes that the level of concentration in some customer catchment areas is excessively high, particularly for hypermarkets and local shops. For this latter retail format, the case of Paris, in which only two retail chains, active under several different retail-brands, are actually in competition, needs to be highlighted. This concentration of customer catchment areas is all the more worrying as the food retail sector has major barriers to entry which result, in particular, from regulations governing the establishment of new shops and the relative scarcity of commercial land.

235. In this context, any conduct likely to increase the obstacles to entry reinforces the concentration of customer catchment areas, reducing the intensity of competition between shops and worsens the situation for consumers. It is thus the same as the non-competition clauses included in contracts for the sale of commercial land. Similarly, contractual or corporate provisions aimed at limiting the mobility of shops between retail chains also prevents the arrival of new retail-brands in some customer catchment areas or new retail chains in some retail formats. In the end, it is really the consumer who is negatively affected by this conduct, which reinforces barriers to entry and thus reduces competition in the customer catchment areas and thus the justifications provided by operators appear all the more inadequate to explain the extent of the restrictions set up in this way. The establishment of such barriers to entry appears all the more damaging as in the French food retail sector, there are a large number of independent retail outlets and they could thus represent a viable means of entry for a new competitor. Several actors in the sector have furthermore stated that affiliation to their network by competing shops could constitute a vector of their development in geographic areas or retail formats in which they do not yet have a presence once, nonetheless, the contractual and corporate measures which currently hinder the mobility of independent retail outlets between networks is lifted.

236. Having started an enquiry at its own initiative, the *Autorité* cannot, within the framework of its consultative role, describe the practices observed with respect to competition law. Only the setup of inter partes proceedings, such as is provided in Article L. 463-1 of the Commercial Code, could allow it to make such an assessment. The following recommendations, summarised briefly in the table below, are nonetheless able to facilitate the establishment of new shops and the mobility of independent retail outlets between competing retail-brands. The implementation of these recommendations is in the hands of the economic operators concerned, particularly retail chains, who have the power to modify their contracts in the way recommended in this opinion, the application of which will be monitored by the *Autorité de la concurrence*. The involvement of the legislator would otherwise be necessary to remove these obstacles to competition.

Practices observed	The *Autorité*'s recommendations
Concerning commercial land	
Presence of non-competition and priority right clauses in contracts for the sale and purchase of commercial land	Removal of non-competition and priority right clauses in contracts for the sale and purchase of commercial land

Concerning relations between retail chains and their affiliates	
Lack of transparency in terms of affiliation particularly due to the large number of contractual documents and their staggering over time	-The conclusion of a single framework agreement supplemented, where necessary, by implementation agreements -Communication of a draft single framework agreement as early as possible for negotiations -Reinforcement of pre-contractual information provided to the affiliation candidate
Terms of commitment too long	-Limitation of the term of affiliation agreements to 5 years maximum -Standardisation of the term and terms of termination of all contracts making up the same relation
Presence of priority rights for the benefit of retail chains in affiliation agreements, joint articles of association and/or shareholders' agreements	Prohibition of priority rights for the benefit of retail chains in affiliation agreements
Presence of post-contractual non-reaffiliation and non-competition clauses in affiliation agreements, joint articles of association and/or shareholders' agreements	Limitation of post-contractual non-reaffiliation and non-competition clauses in affiliation agreements, joint articles of association and/or shareholders' agreements to a term of one year and for the shop which is the subject of the contract
Presence of deferred subscription fees in affiliation agreements	Staggering the payment of subscription fees instead of their deferred payment
Multiple capital holdings by retail chains in their affiliated retail outlets' operating companies giving them a blocking minority	Regulating capital holdings by retail chains in their affiliated retail outlets' operating companies

Deliberations on the debriefing of Ms Juliette Herzele and Mr Etienne Pfister and the statement of Ms Virginie Beaumeunier, General Rapporteur, by Ms Anne Perrot, Vice-President, Chair, Ms Laurence Idot and Mr Yves Brissy, Members.

The Meeting Officer,

Véronique Letrado

The Chair,

Anne Perrot

APPENDICES

Appendix 1: Table covering the 208 living areas taken from the *LSA Focus Alimentaire* catalogue

Study of the living areas described in the *LSA Focus Alimentaire* catalogue		"Group approach"			"Shop approach"		
		No.	%	Demand	No.	%	Demand
Number of areas identified in the *LSA focus Alimentaire* catalogue		629	100	NA	629	100	NA
Number of areas studied		208	33.07%	2,658,052	208	33.07%	2,658,082
Dominant position	Number of areas in which i) an operator has a market share of over 60%, ii) an operator has a market share of over 50% and all operators have less than 15%, iii) an operator has a market share of over 40% and all competing operators have a market share of less than 10%	55	8.74%	1,904,199	48	7.63%	2,248,346
Duopoly	The two biggest groups have a cumulative market share of more than 90% and neither of these operators has a dominant position	24	3.82%	1,479,294	24	3.82%	1,363,225
"Triopoly"	The three biggest groups have a cumulative market share of more than 90% and none of these operators has a dominant position	79	12.56%	2,800,851	60	9.54%	2,415,942
Oligopoly	The four largest groups have a cumulative market share of more than 90% and none of these operators has a dominant position	42	6.68%	4,075,697	40	6.36%	2,627,002
Summary	Number of areas in which an operator is in a dominant position or in which the market structure is similar to a duopoly, "triopoly" or oligopoly of 4 companies	200	31.80%	2,528,289	172	27.34%	2,251,211
Concentration	HHI median	3,797.48			3,665.178		
	HHI>2,200	205	32.59%	2,600,896	192	30.52%	2,528,289

Customer catchment area: Defined according to the method used by *Asterop* and based on residential catchment areas.

"**Group approach**"**:** Market share calculated for the retail chain.

"**Shop approach**"**:** Market share calculated for the retail chain's integrated shops and shops for co-operative groups.

Demand: Number of inhabitants in the area multiplied by their average income (in 1,000s of euros, source: Asterop)

Appendix 2: Table describing the customer catchment areas of hypermarkets (source: Data provided by the four respondent retail chains)

Study of customer catchment areas centred around hypermarkets – only areas in which a group has a market share of over 30% are considered		Total calculations made for four retail chains			
		"Group approach"		"Shop approach"	
		No.	%	No.	%
Total number of hypermarkets of the four respondent retail chains		740	100%	740	100%
Number of hypermarkets with a market share in retail area of over 30% for the four respondent retail chains		329	44%	282	38%
Dominant position	Number of areas in which i) an operator has a market share of over 60%, ii) an operator has a market share of over 50% and all operators have less than 15%, iii) an operator has a market share of over 40% and all competing operators have a market share of less than 10%	40	5%	33	4%
Duopoly	The two biggest groups have a cumulative market share of more than 90% and neither of these operators has a dominant position	34	5%	27	4%
"triopoly"	The three biggest groups have a cumulative market share of more than 90% and none of these operators has a dominant position	74	10%	35	5%
Oligopoly	The four largest groups have a cumulative market share of more than 90% and none of these operators has a dominant position	100	14%	38	5%
Summary	Number of areas in which an operator is in a dominant position or in which the market structure is similar to a duopoly, "triopoly" or oligopoly of 4 companies	248	34%	133	18%
Concentration	HHI median of the areas studied	3,495		2,767	
	HHI>2,200	318	43%	227	31%

Customer catchment area: Defined around hypermarkets with a market share of more than 30%.

"**Group approach**"**:** Market share calculated for the retail chain.

"**Shop approach**"**:** Market share calculated for the retail chain's integrated shops and shops for co-operative groups.

<u>Appendix 3:</u> Table describing the customer catchment areas of supermarkets (source: Data provided by the two respondent retail chains)

Study of customer catchment areas centred around supermarkets – only areas in which a group has a market share of over 30% are considered		Total calculations made for two retail chains	
		"Group approach"	
		No.	%
Total number of supermarkets held or affiliated to the two respondent retail chains		2,864	100%
Number of supermarkets with a market share in retail area of over 30%		652	22.77%
Dominant position	Number of areas in which i) an operator has a market share of over 60%, ii) an operator has a market share of over 50% and all operators have less than 15%, iii) an operator has a market share of over 40% and all competing operators have a market share of less than 10%	105	3.67%
Duopoly	The two biggest groups have a cumulative market share of more than 90% and neither of these operators has a dominant position	51	1.78%
"Triopoly"	The three biggest groups have a cumulative market share of more than 90% and none of these operators has a dominant position	106	3.70%
Oligopoly	The four largest groups have a cumulative market share of more than 90% and none of these operators has a dominant position	130	4.54%
Summary	Number of areas in which an operator is in a dominant position or in which the market structure is similar to a duopoly, "triopoly" or oligopoly of 4 companies	392	13.69%
Concentration	HHI median of the areas studied	3,060.759	
	HHI>2,200	562	19.62%

Customer catchment area: Defined around hypermarkets with a market share of more than 30%.

"**Group approach**"**:** Market share calculated for the retail chain. A shop approach could not be considered as the franchise shops in integrated groups could not be identified.

<u>Appendix 4:</u> Table describing the local food retail market in the 167 *communes* sampled and in the 37 *communes* with more than 100,000 inhabitants studied

Structure of the local daily consumer goods retail market in 167 towns – market share calculated for retail chains		Total sample (167 communes)			Communes with more than 100,000 inhabitants (no. = 37)		
Number of towns studied		"Group approach"			"Group approach"		
		No.	%	Demand	No.	%	Demand
Dominant position	Number of areas in which i) an operator has a market share of over 60%, ii) an operator has a market share of over 50% and all operators have less than 15%, iii) an operator has a market share of over 40% and all competing operators have a market share of less than 10%	23	13.77%	1,101,704	3	8.11%	4,320,521
Duopoly	The two biggest groups have a cumulative market share of more than 90% and neither of these operators has a dominant position	4	2.40%	715,613	0	0.00%	
"Triopoly"	The three biggest groups have a cumulative market share of more than 90% and none of these operators has a dominant position	35	20.96%	765,583	1	2.70%	2,581,988
Oligopoly	The four largest groups have a cumulative market share of more than 90% and none of these operators has a dominant position	57	34.13%	943,337	11	29.73%	2,983,421
Summary	Number of areas in which an operator is in a dominant position or in which the market structure is similar to a duopoly, "triopoly" or oligopoly of 4 companies	119	71.26%	915,364	15	40.54%	2,983,421
Concentration	HHI median	2,900.305			2,441.463		
	HHI>2,200	145	86.83%	954,421	25	67.57%	2,999,594

Customer catchment area: comprising a *commune*'s territory

"**Group approach**"**:** Market share calculated for the retail chain. A shop approach could not be considered as the franchise shops in integrated groups could not be identified.

Demand: Number of inhabitants in the area multiplied by their average income (in 1,000s of euros, source: respondent retail chain).