

**TAKING FORWARD THE
ESTABLISHMENT OF A BODY TO
MONITOR AND ENFORCE
COMPLIANCE WITH THE
GROCERIES SUPPLY CODE OF
PRACTICE (GSCOP): THE
GROCERIES CODE ADJUDICATOR**

**The Government's policy for a
Groceries Code Adjudicator**

MAY 2012

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Foreword from Norman Lamb MP

I am very pleased to announce that the Groceries Code Adjudicator (GCA) Bill has been published today, following its introduction yesterday into the House of Lords. The Bill will establish an independent Adjudicator to enforce the Groceries Code and ensure that large supermarkets treat their suppliers fairly and lawfully. This document sets out how and where the Adjudicator is to be established, the office's role, duties and functions, and how the office is to be funded.



The establishment of an Adjudicator was first recommended by the Competition Commission in 2008, following its inquiry into the Supply of Groceries. The inquiry found that although the groceries market was generally working well, in some circumstances large supermarkets were using their buying power to pass on excessive risk and unexpected costs to suppliers. This could act against the long-term interest of consumers, by discouraging suppliers from investing and innovating in new product lines or production processes.

It's important to bear in mind that the Competition Commission found that overall the retailers were providing a good deal for their customers. Retailers should not be prevented from securing the best deals, and passing on benefits to consumers.

But equally, retailers should be required to treat their suppliers fairly and lawfully. Free and fair competition is the key to a healthy market and it is right that a Groceries Code Adjudicator should be established to strengthen the groceries supply chain and make sure the market is working in the best long-term interest of consumers.

Introduction

This paper accompanies the Groceries Code Adjudicator Bill which was introduced into the House of Lords on 10th May 2012. It sets out why the Government proposes to set up the Groceries Code Adjudicator and explains what the Bill is seeking to achieve. The Explanatory Notes give more detailed commentary on the clauses in the Bill. The Government response to the consultation on the Groceries Code Adjudicator announced Government's policy on most aspects of the Adjudicator¹, as did its response to the Business, Innovation and Skills Select Committee's Ninth Report of Session 2010-12². The remaining aspects on how the Adjudicator will be set up and funding arrangements are covered in this paper.

¹ "Taking forward the establishment of a body to monitor and enforce compliance with the groceries supply code of practice (GSCOP): The Groceries Code Adjudicator - Government response to the consultation". <http://www.bis.gov.uk/assets/biscore/business-law/docs/competition-matters/10-1011-groceries-supply-code-practice-government-response.pdf>)

² Time to bring on the referee? The Government's Proposed Adjudicator for the Groceries Code: Government Response to the Committee's Ninth Report of Session 2010-12
<http://www.publications.parliament.uk/pa/cm201012/cmselect/cmbis/1546/154602.htm>

1. A statutory basis for the Groceries Code Adjudicator

1.1 In its final report on the supply of groceries in the UK³ the Competition Commission found that, while the exercise of buyer power by grocery retailers is likely to have positive implications for consumers, it could raise concerns in certain, limited circumstances. The Commission found that when, in the hope of gaining competitive advantage, retailers transferred excessive risks or unexpected costs to their suppliers, this was likely to lessen suppliers' incentives to invest in new capacity, products and production processes, with the potential for detriment to the long term interest of consumers.

1.2 As a result, the Competition Commission made the Groceries (Supply Chain Practices) Market Investigation Order 2009 ("the Order")⁴. The Order requires large retailers to incorporate the Groceries Supply Code of Practice ("the Code") into agreements for the supply of groceries for resale in the United Kingdom and to supply a written copy of the agreement and certain other information to the supplier. This means that if a large retailer breaches the Code it will be in breach of its contract with the relevant supplier, who may then have contractual remedies against the retailer such as a claim for damages.

1.3 Large retailers are required by the Order to train their buying teams about the Order and the Code. They must also appoint a compliance officer to act as a point of contact with suppliers and to prepare an annual compliance report for the Office of Fair Trading.

1.4 The Order also includes a dispute resolution scheme. A supplier who believes that a large retailer has breached the Code may notify the retailer's compliance officer. If the dispute is not resolved within 21 days then, at any time within four months of the dispute arising, the supplier may refer the dispute to arbitration. The Order protects direct suppliers, based anywhere in the world, to the large retailers.

1.5 The Competition Commission considered that the Code would be more effective with an adjudicator in place to enforce it – in effect, to act as a referee and police the new rules. After failing to gain sufficient agreement from the retailers to establish such an enforcer

³ "The supply of groceries in the UK market investigation" dated 30 April 2008
http://www.competition-commission.org.uk/rep_pub/reports/2008/fulltext/538.pdf

⁴ http://www.competition-commission.org.uk/inquiries/ref2006/grocery/pdf/revised_gscop_order.pdf

voluntarily, the CC recommended that the Government take the necessary steps to establish an Adjudicator as soon as is practicably possible.

1.6 Following public consultation, the Government announced in August 2010⁵ its intention to establish the Groceries Code Adjudicator (“the Adjudicator”) with statutory powers to enforce the Code. The Government considers that the arbitration scheme created by the Order should be carried out by the Adjudicator or another person appointed by him or her.

1.7 On 24 May 2011 the Government published a draft Bill for pre-legislative scrutiny. In its 9th Report of Session 2010-2012⁶, the Business, Innovation and Skills Select Committee endorsed the need for an Adjudicator and made a number of recommendations, to which the Government responded⁷. Principal changes to the Bill following pre-legislative scrutiny include the removal of restrictions on sources of evidence the Adjudicator can consider when deciding whether to begin an investigation; the establishment of a method of escalation in cases of repeated non-compliance with the Groceries Code; to have the first review of the Adjudicator after two rather than three years; and to extend the source of secondments to the Adjudicator from the current provision of BIS and the OFT, to the entire public sector.

1.8 Supermarkets play an important role in the economy. The Government recognises that creation of an Adjudicator should not stifle the consumer benefits delivered by the supermarkets but needs to ensure fair dealings between suppliers and large retailers which will ultimately benefit consumers in the long run.

4 <http://www.bis.gov.uk/assets/biscore/business-law/docs/competition-matters/10-1011-groceries-supply-code-practice-government-response.pdf>

⁶ Time to bring on the referee? The Government's proposed Adjudicator for the Groceries Code
<http://www.publications.parliament.uk/pa/cm201012/cmselect/cmbis/1224/122402.htm>

⁷ The supply of groceries in the UK market investigation” dated 30 April 2008
http://www.competition-commission.org.uk/rep_pub/reports/2008/fulltext/538.pdf

2. The Groceries Supply Code of Practice

2.1 As of 4th February 2010, all retailers with groceries turnover in excess of £1 billion per year are now parties to the Code. The Code's provisions are now included in each of these retailers' contracts with their suppliers. The Code has an overarching fair dealing provision. It prohibits retailers from imposing retrospective changes to terms and conditions of supply unless reasonable notice is given to the supplier in writing. It limits the extent to which suppliers are required to pay for listings, promotions, inaccurate forecasts by retailers or customer complaints. It also sets out the requirement for retailers to provide reasonable notice and commercial justification before a supplier is de-listed.

2.2. The following paragraphs summarise the functions and powers of the Adjudicator, the role of Ministers, funding and review arrangements.

3. Functions and powers of the GCA

3.1 The sole purpose of the Adjudicator will be to oversee and enforce the Code as set out in the legislation.

3.2 The Government proposes that, in carrying out this duty, the Adjudicator should have the following statutory functions and powers:

Arbitration: to act as arbitrator, if a supplier refers a dispute to arbitration under the Code, or to appoint another person to act as arbitrator

Investigation: to carry out investigations of suspected breaches of the Code by a retailer. The Government proposes that in deciding whether to initiate an investigation, the Adjudicator must be satisfied that there are reasonable grounds to suspect a breach of the Code or that a retailer has not followed a previous recommendation. Both before and during an investigation, the Adjudicator may consider information from any source; however, he or she will only have powers to require information – other than for the purpose of monitoring whether a retailer has complied with a previous investigation – once an investigation has been initiated. The Government's rationale for this policy is explained further in paragraphs 4.1 – 4.2 below.

Enforcement: the Adjudicator must publish a report of any investigation and, if the retailer is mentioned in it, give them the opportunity to comment on it before publication. If the Adjudicator is satisfied there has been a breach of the Code, he or she can:

- recommend steps be taken by the retailer to improve compliance with the Code;
- require the retailer to publish information about the investigation and the breach; and
- subject to paragraph 5.2 below, impose financial penalties on the retailer for breach of the Code.

Advice and guidance: The Adjudicator must publish guidance on investigations. He or she will also be able to publish guidance on other aspects of the Code and how he or she intends to fulfil his or her functions and must publish an annual report on his or her work. More generally, the Adjudicator may choose to advise suppliers and retailers on any matter relating to the Code.

3.3 The Adjudicator will not monitor the obligations which the Order places on retailers regarding training on the Code and the Order and the appointment of compliance officers to act as a point of contact with suppliers⁸.

⁸ Under S 162 Enterprise Act 2002 the OFT is responsible for keeping this enforcement order under review.

4. Confidentiality and information which can start an investigation

4.1 Investigations are intended to be broad ranging and to be based upon general patterns of behaviour by the retailers. It would be rare for an investigation to be based upon a particular complaint. One of the fundamental principles of the Adjudicator will be his or her ability to investigate complaints and maintain the confidentiality of the identity of complainants. The Competition Commission found that many suppliers were afraid to make complaints as they were concerned that it would lead to retaliatory treatment by the retailer, for example that the retailer might stop trading with them. Protecting the identity of suppliers should help them feel safer in raising concerns about retailers who may have breached the Code. With limited exceptions, the Government therefore proposes that the Bill should prohibit the Adjudicator from disclosing any information that may lead to disclosure of the fact that a particular person has complained about a retailer failing to comply with the Code.

4.2 The Government proposes that the Adjudicator may consider information from any source when deciding whether to initiate an investigation: he or she must simply be satisfied that there are reasonable grounds to suspect a breach of the Code or a failure to follow an earlier recommendation. Although, as these are contractual matters, it is most likely that a direct supplier would have the information required to make an appropriate complaint, it is also possible that other information, for example that provided by indirect suppliers, third parties such as trade associations, whistleblowers or information in the public domain may also be of value.

4.3 The Government recognises that if trade associations do not act responsibly then the Adjudicator could be burdened with dealing with larger numbers of less direct and lower quality complaints. The Bill therefore provides that, at each triennial review of the Adjudicator, the Secretary of State will be required to assess whether the involvement of third parties is helping or hindering the Adjudicator, and if the latter applies then he or she will be able to restrict the sources of information.

5. A power to impose financial penalties

5.1 The Government's view is that a requirement for a retailer to publish information about an investigation which finds it in breach of the Code will be an effective deterrent. That information could be taken into account by those dealing with the retailer in future. That is why the Government thinks that the Adjudicator's primary lever should be to require a retailer found to be in breach of the Code to publish information about the investigation and its outcome and publicise it, for example, through a press release, in the retailer's annual report, online and in national newspapers.

5.2 However, should this level of deterrence prove insufficient in promoting successful compliance with the Code, the Government will consider introducing financial penalties against retailers who breach the Code. The draft Bill provides the Secretary of State with a residual power to enable the Adjudicator to levy penalties. Prior to activating this power, the Secretary of State would consult the Adjudicator, the retailers, the OFT and Competition Commission, suppliers and consumer bodies. The Secretary of State would need to set a maximum penalty when activating this power.

6. Independence

6.1 The Government recognises the importance of the independence of the Adjudicator from the Government and OFT, particularly to maintain confidence of retailers and suppliers. The draft Bill achieves this in several ways: for example, the Adjudicator is the only person who can perform the functions of the Groceries Code Adjudicator. The Adjudicator will have added independence as he or she will not be a civil servant. The Adjudicator will initially be appointed for a specified period of up to 4 years and this appointment can only be terminated if the Adjudicator is unable or unwilling to perform his or her functions. The Bill makes no provision for direction of the Adjudicator by the Secretary of State and the Adjudicator will be expected to exercise his or her own decision making. In regard to financial independence, the Adjudicator will have separate accounts and will be accountable for his or her spending as an accounting officer.

7. Evaluating the impact of the Adjudicator

7.1 In line with all Government policies, the GCA will be reviewed to assess its effectiveness and whether it is achieving its objective. The draft Bill provides that the GCA will be reviewed two years after the end of the financial year in which the office is set up, and three-yearly thereafter. The review will be carried out by the Department for Business, Innovation and Skills and will include consultation with the Adjudicator, Competition Commission, Office of Fair Trading, retailers, suppliers, and consumers. The Secretary of State will have powers to abolish the Adjudicator if it is found that he or she has not been effective in enforcing the Code and the functions can no longer be justified.

8. Setting up the Adjudicator

8.1 The Government response to consultation announced that the Adjudicator would be based within the Office of Fair Trading but would be established independently from its consumer and competition activities. However, as the Government has now proposed to merge the competition functions of the OFT and Competition Commission to create a single Competition and Markets Authority it is no longer practical to increase the functions of the OFT. We have therefore decided that the Adjudicator should be created as a statutory office holder. The intention remains that the Adjudicator should benefit from the skills and expertise of the OFT and this will be achieved through co-locating the Adjudicator within the OFT, resourcing the office mainly through secondments from the OFT and sharing its back office functions. The Adjudicator's relationship with the OFT is intended to be on an arm's length terms basis and subject to appropriate safeguards being in place to protect confidentiality and avoid conflicts.

9. Funding the Adjudicator

9.1 The GCA will be funded by the large retailers.

9.2 The Competition Commission proposed a formula to calculate each party's share of the cost of the GCA, taking into account the retailer's turnover, the number of recommendations made to the retailer by the Adjudicator and the number of disputes between the retailer and suppliers. The Government is not in favour of using this formula as, although it is intended to be fair and capture the costs associated with each retailer, it would not do so accurately. Currently, there is insufficient evidence to suggest a relationship between the turnover of a retailer and the extent to which it would breach the Code. In addition the formula does not take it into account that the cost of a dispute would vary according to the length and scale of an investigation conducted by the Adjudicator. The Government therefore proposes the alternative approach set out below.

9.3 The costs of the Adjudicator will fall into three main categories:

- i) the costs of the Adjudicator's arbitration function. The Adjudicator will be able to apportion the costs of the arbitration function as set out in Part 5 of the Competition Commission's 2009 Order.
- ii) the costs of an investigation under the Code where the Adjudicator is satisfied that a retailer has breached the Code. The Government intends that costs of such investigations should normally be recovered from the retailer concerned, and the draft Bill empowers the Adjudicator to do so.
- iii) all other costs of the Adjudicator in carrying out his or her functions under the Code, including the costs of investigations where the Adjudicator is satisfied that the retailer is not in breach of the Code. The Government intends that these costs should be shared equally between all the retailers to which the Code applies, and that the Adjudicator should recover these costs by means of a levy on retailers. The amount of each levy must be agreed with the Secretary of State.

9.3 Costs will be calculated on a full cost recovery basis.

9.4 The Adjudicator will be able to recover costs from another person such as a supplier if he or she finds that a complaint which initiated an investigation was vexatious or wholly without merit.

9.5 The draft Bill requires the Adjudicator to inform retailers when levy payments are due, how much they will be and to publish the details of the levy and how it has been arrived at.

9.6 The Bill also proposes that the Secretary of State may by order enable the Adjudicator to require retailers to pay a greater or lesser share of the levy if this is justified in the light of experience. For example, this might be in order to reflect the level of complaints generated by particular retailers and thus the impact on the costs of the Adjudicator. The Government hopes this prospect will be an additional incentive for retailers to comply with the Code so as to be liable in the future for less of the Adjudicator's costs.

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