Introduction

The Groceries Code Adjudicator has a remit to prevent unfair trading practices between the UK’s largest supermarkets and their direct suppliers. It has been an effective regulator, overseeing improved relationships in the groceries sector. However, the narrowness of its remit means that the GCA is powerless to support improved trading practices for businesses that supply supermarkets indirectly. For this reason, many politicians, industry groups and civil society organisations support the extension of the GCA’s remit to include indirect suppliers to supermarkets. This document explores how the government could extend the GCA’s remit and tackles further questions such as what that remit should include and what powers the extended GCA would need.

Why is an extended GCA needed?

1) Disproportionate costs and risks continue to be placed on the weakest part of the supply chain. For example, when retailers make short-notice changes to the size of orders there is a ripple effect on the rest of the supply chain: suppliers either purchase less product, perhaps wriggling out of previous agreements, or source more product at short notice. This results in systematic over-production and over-procurement of perishable products at every stage of the supply chain.

The GSCoP, and GCA, are intended to prevent such unfair practices being placed upon the supply chain. However, direct suppliers may choose to pass risks and costs onto their supply chain rather than challenging the retailer. Furthermore, unfair practices may arise not from retailers, but from large suppliers or manufacturers abusing their relatively powerful position.

In either case, bringing indirect suppliers into scope would enable the GCA to support fair dealing in the parts of the supply chain where unfair risk and cost are most frequently borne.

2) Smaller suppliers, or those undertaking labour-intensive activity, are typically the least capitalised and resilient part of the supply chain and have the most to gain by stopping the transfer of disproportionate risks and costs. At present, they have no insight into whether parts of the chains they sell into are transgressing the GSCoP and are therefore unable to complain to the GCA. Bringing the whole supply chain into scope would mean that the GCA would receive evidence from the businesses with the greatest interest in preventing transfer of risk and cost.

What we want to see
DISCUSSION DOCUMENT

Vertical extension to the GCA’s remit

- The extended regulator to cover anyone who trades a product that ends up being sold as groceries\(^1\) in one of the 10 largest UK retailers\(^2\). (nb: the jurisdictional limits of a UK regulator are understood)
- For the extended regulator to enforce a Code including a Principle of Fair Dealing (GSCoP, Paragraph 2) on the parts of the supply chain newly brought into scope. This might either be an updated GSCoP code, a supplementary code, with similar wording, that covers suppliers.
- For the extended regulator to have the same/similar powers to those that she currently holds. These include the ability to receive anonymous complaints, to initiate investigations based upon reasonable suspicion of a breach, and to apply fines of up to 1% of a business’ UK turnover.

- Further changes that we would like to see are:
  - The revision of the definition of ‘groceries’ in the Code to include plants and flowers, perishable products where many of the same unfair practices are experienced by suppliers
  - The revision of the list of 10 supermarkets to include other large retailers that may satisfy the threshold of £1 billion UK turnover, or other businesses known to purchase unfairly from their suppliers.

What would need to be considered in the design of a new regulator?

1: Who should the extended regulator cover?

**Explanation:** Groceries supply chains are complex and international. Each business involved in groceries supply chains may have a number of customers, suppliers and product lines, and an

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\(^1\) The definition of ‘groceries’ in this case is taken from the 2006 Office of Fair Trading referral [https://www.gov.uk/cma-cases/grocery-market-investigation-reference-oft](https://www.gov.uk/cma-cases/grocery-market-investigation-reference-oft): “includes food (other than that sold for consumption in the store), pet food, drinks (alcoholic and non-alcoholic), cleaning products, toiletries and household goods - excludes petrol, clothing, DIY products, financial services, pharmaceuticals, newspapers magazines, greetings cards, CDs, DVDs, videos and audio tapes, toys, plants, flowers, perfumes, cosmetics, electrical appliances, kitchen hardware, gardening equipment, books, tobacco and tobacco products.”

\(^2\) Tesco, Sainsbury, Asda, Morrisons, Waitrose, Lidl, Aldi, Iceland, Marks & Spencer, Cooperative
extended regulator would need clarity over who fell within its regulatory scope. The GCA currently applies to 10 named retailers and their direct suppliers.

**Suggestion:** The regulator should cover any commercial exchange involving goods, some of all of which are intended to comprise some or all of a product sold as groceries in one of the ten named UK retailers. The regulator would not cover professional services, or supply of goods that did not directly comprise a grocery product (i.e. sale of agricultural fertiliser).

Additionally, the regulator would only cover commercial exchanges of goods that could be subjected to UK contract law - that is, those involving at least one company that bases all or part of its operations in the UK.

There may be a case for defining a size/market power threshold for businesses that would fall within the regulatory scope of the extended regulator. However, this carries a number of problems:

- Who would be responsible for calculating and updating the threshold, and for monitoring which businesses were in or out of scope?
- Would such a threshold effectively cover the businesses with dominant market positions?
- Could businesses dodge such regulation (by splitting as legal entities etc.)?

Suppliers in the supply chain may pass on risk and cost pushed down onto them, as well as initiating such practices themselves.

### 2: What does an extended GCA enforce?

**Explanation:** The GSCoP exists to stop the transfer of excessive risks and unexpected costs onto suppliers which were found to have had an adverse effect on competition in relation to suppliers’ ability to invest and innovate. The GSCoP includes a principle of fair dealing, followed by other clauses which specify certain outlawed practices peculiar to the retailer-direct supplier relationship (such as payment for promotions or shelf placing).

**Suggestion:** A new code would need to include the principle of fair dealing, followed by additional clauses to cover practices relevant to relationships at the middle of the supply chain. Key considerations would be that there should be no unilateral or retrospective changes to trading arrangements which impact upon unit price, volume/weight/number of items sold, standards, or the timing of payments. Clarity should also be given on the exact point at which the ownership of products transfers between parties, and exactly what is determined to have been transferred (e.g. ‘drop and drive’ practices).

### 3: What will the GCA office do and how will the GCA’s office function given its expanded remit?

**Explanation:** The extended GCA would be charged with enforcing a code of fair dealing upon a great many more businesses and trading relationships than was previously the case.

Currently the GCA’s office receives anonymous complaints, conducts an annual supplier survey, produces an annual report, and undertakes a prioritisation process to focus its resources on strategic problems. Based on the information the GCA gathers the office is able to:

- Communicate with retailers at quarterly meetings – including instructing them to change practices that are transgressing the Code
- Issue Code clarification (after consultation)
• Issue best practice note (after consultation)
• Initiate an investigation. At the end of an investigation GCA can make a) recommendations to the retailer to improve particular practices, b) apply a fine up to 1% UK turnover, c) require that the retailer pays for an advert indicating that the retailer was guilty of breaching GSCoP; d) issue code clarification; e) a referral to the CMA if there are problems with how the GSCoP is worded, or if the GSCoP isn’t incorporated into supply agreements;
• Adjudicate between a retailer and a supplier, if the supplier is willing to be identified.
• On an annual basis she is able to retrospectively levy the 10 retailers for the cost of running her office. This is calculated by a formula which includes whether certain retailers had caused more work for the GCA office compared to others.

Suggestion: The GCA at present does not at present ‘monitor’ compliance with the code. Rather, she continues to hear anonymous complaints and prioritises which to act upon, publishing top priority concerns areas each year. The GCA would not necessarily have to operate in a materially different way if regulating a larger market.

Only businesses experiencing excessive risks and unexpected costs will complain to the GCA, so it is not the case that the GCA will be instantly overwhelmed by 1000s of contacts/complaints.

It will be up to the GCA to determine whether and how to conduct an investigation, mindful of the need to ensure that no single supplier is exposed to possible retribution by a more powerful mid-tier supplier or retailer. Following an investigation, the GCA should make relevant recommendations to deter future poor practice, including penalising mid-chain suppliers or retailers found guilty of transgressing the code.

4: How would the extended regulator interact with businesses in the supply chain, and what obligations would be imposed on mid-tier suppliers under extended-GCA scope?

Explanation: At present, the GCA interacts with the ten largest supermarkets via retailer-appointed Code Compliance Officers, who are trained staff responsible for ensuring the GSCoP compliance of their businesses.

The ten retailers also have to have supply agreements which are worded in a manner that is consistent with the Code, and contribute to the funding of the GCA’s office. The latter imposition is because it was found by the Competition Commission that the grocery retail sector had not complied with the legally binding Supermarkets Code of Practice, and so needed to pay for a regulator to ensure effective enforcement of the law.

The system of Code Compliance Officers and levy funding works well. However, the extended GCA may need to interact in a different way with suppliers covered by its expanded remit.

Suggestion:

Businesses that pass on excessive risk and unexpected costs would be expected to improve their purchasing practices, or otherwise risk being investigated and penalised by an extended GCA. These businesses might choose to appoint a responsible officer to monitor that process, and perhaps interact with an extended GCA. Alternatively, this could be something that the GCA requires of businesses that have been investigated and found to have breached the principle of fair dealing (the GCA has advised that its interactions with retailers’ Code Compliance Officers have resulted in improved GSCOP compliance.).
Mid-tier suppliers won’t proactively need to show the GCA that their supply agreements or contacts are compliant with the principle of fair dealing. The extended GCA will continue to focus on behaviours/practices which breach the principle of fair dealing, rather than on whether the text of a contract/supply agreement is legally consistent with the Code. If the GCA starts an investigation, then she might ask to see supply agreements if they are useful to her investigation.

Other possibilities which partially address the problems experienced by indirect suppliers: (i) Retailers requiring in their terms and conditions of purchase that a direct supplier undertakes to comply with GSCOP in relation to its own suppliers (ii) Retailers committing to the Prompt Payment Code (presently only 5 of the 10 are signatories) and requiring in their terms and conditions of purchase that a direct supplier undertakes to similarly promptly pay its own suppliers.

Ultimately it will be down to the GCA to determine how it interacts with suppliers newly brought into scope.

5: How would the extended regulator adjudicate in cases where more than one party is to blame?

Explanation: The extended adjudicator will be monitoring code compliance in multi-layered supply chains. This may mean that unfair practices in a given supply chain are the result of decisions made at more than one level.

Suggestion: Given that the blame for unfair cost and risk being passed down the supply chain may be attributable to retailers and mid-level suppliers. In such a situation, the extended adjudicator will need to be able to investigate and apportion blame to different parts of the supply chain, calculating penalties accordingly.

The circumstances in which the GCA might need to appropriate precise costs, and therefore take a more forensic approach, would be where an indirect supplier requested adjudication on a case in which unfair dealing had been perpetrated by two other parts of the supply chain.

6: How would the GCA’s office be resourced to handle the extended remit?

Explanation: Dealing with an extended remit may have significant resource implications for the GCA’s office.

Current: The GCA office is run by c. 7 staff (some of whom are part time), with additional resources/expertise hired as needed, for example when an investigation is launched.

Suggestion: There is currently no limit on the staff that the GCA is able to employ. There may be a case for altering the fact that GCA staff can only be secondees from the Civil Service. Additionally, there may be a case for appointing one or more Deputy Adjudicators, as provided for in the GCA Act, to handle the expanded workload. We understand the GCA is able to subcontract investigation work to appropriately skilled and resourced legal or accountancy firms.
7: How would the extended GCA be funded?

**Explanation:** The current model would need to evolve if the GCA needs to investigate mid-tier suppliers as well as retailers, for having breached the principle of fair dealing.

**Current situation:** The GCA’s costs are funded by BEIS, who then recoup 100% of the costs via a retrospective levy on the ten supermarkets. The calculation of the levy takes consideration of whether a supermarket had been found to have breached the code that year and therefore caused additional work for the GCA.

**Suggestion:** The initial running costs of the office could be funded by the largest 10 supermarkets as currently. However, if the extended GCA uncovers practices that contravene the Code in the upstream supply chain, it could levy a proportion of its costs from those suppliers found guilty of breaching the extended-GSCoP code.