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Hub-and-Spoke Cartels in the Cheese Sector – Is the OFT’s Case Full of Holes?

Angelene Duke (Sidley Austin LLP) · Wednesday, July 25th, 2012

The Office of Fair Trading’s (“OFT”) long-running *Dairy* investigation has been plagued by controversies right from the outset. Allegations have been made by the OFT and subsequently withdrawn, the scope of the investigation has been progressively narrowed and the OFT has even had to pay Morrisons £100,000 to settle a libel claim.

Against this backdrop, it was perhaps unsurprising that Tesco, the only addressee of the decision not to have settled with the OFT, appealed the eventual finding of infringement to the UK’s Competition Appeal Tribunal (“CAT”). In submissions during the CAT hearing (which finished on 13 July 2012), Tesco argued that the OFT’s case alleging that it had engaged in anti-competitive conduct in the UK’s *Cheese* sector was flawed. Although at the time of writing the CAT’s judgment is still pending, Tesco’s appeal clearly raises important issues, including: (i) the quality of the evidence relied upon by the OFT; (ii) the manner in which the OFT conducted its case before the CAT; and (iii) the interpretation of the legal test for liability in “hub-and-spoke” cartels. Before discussing each of these issues in turn, it is helpful first to give some background on the OFT’s case.

Background

Tesco was one of nine supermarkets and dairy processors found by the OFT in its August 2011 *Dairy* decision to have shared sensitive pricing information with a view to fixing the retail prices for certain dairy products in 2002 and 2003. The supermarkets were not found to have shared pricing information directly, but rather to have shared pricing information indirectly, via intermediaries working for the dairy processors who supplied them. In effect, the OFT found that the communications constituted a “hub-and-spoke” cartel along the lines of those sanctioned in the OFT’s *Replica Football Kits* and *Hasbro/Littlewoods/Argos* cases.

Supermarkets Asda, Sainsbury’s and Safeway, as well as dairy processors Arla, Dairy Crest, McLelland, The Cheese Company and Wiseman all received reduced fines after settling with the OFT. However, Tesco consistently denied that it had colluded to fix prices. In April 2010, the OFT offered to drop certain of its allegations against Tesco if Tesco agreed not to contest the remainder of the case. However, Tesco continued to defend its position. The OFT eventually removed Tesco from its related *Milk* investigation and dropped its allegations in relation to *Butter* in their entirety, but it proceeded with its *Cheese* case and issued a decision in August 2011 imposing a fine of £10.4 million on Tesco.

Evidential issues

Tesco has an impressive record in persuading the OFT that it should not pursue “hub-and-spoke” cases against it. Tesco successfully persuaded the OFT that there was no case for it to answer in the recent *Tobacco* investigation. In the Dairy case, Tesco ensured that it was not itself included in the *Milk* aspects of the decision and it appears to have had a part to play in the OFT’s decision to drop the *Butter* investigation.

Since the *Dairy* decision alleged the existence of a “hub-and-spoke” cartel, rather than direct co-ordination between retailers, Tesco argued that it was for the OFT to adduce evidence as to Tesco’s intentions when sharing information on its retail prices with its suppliers. However, judging from the arguments before the CAT, there appears to have been little, if any, direct evidence as to Tesco’s intentions in this regard. Tesco submitted that the OFT’s case against it relied only on e-mails and documents seized from the dairy processors. During the hearing, Dinah Rose QC, counsel for Tesco, also questioned the OFT’s selection and interpretation of written evidence and identified a number of the OFT’s submissions that she described as misleading and needing “to be treated with the greatest caution”. Tesco also criticised the lack of witness testimony to corroborate the written evidence, a key weakness in the OFT’s defence of its *Tobacco* decision, which was quashed by the CAT. Coming so soon after the collapse of the OFT’s *Tobacco* case, it will be interesting to see what the CAT makes of the OFT’s approach to these key evidential issues in the *Dairy* case.

Conduct issues

There may also be questions raised about the OFT’s conduct of its case before the CAT. In *Tobacco*, the OFT was heavily criticised for casting its original decision too narrowly and for redefining key aspects of its case on appeal. It appears from the course of the Tesco appeal before the CAT, that the OFT might again come in for criticism. After more than a month in court, the *Dairy* hearing was due to conclude on 31 May. However, at 5pm on 30 May, the OFT served a 200 page submission on Tesco’s solicitors. The CAT accordingly set an extra day to hear Tesco’s oral replies to those submissions and also gave Tesco time to prepare a written response. Tesco argued that the OFT’s 30 May submission contained new evidence and new allegations that had not previously been pleaded. Tesco also argued that the case contained in the OFT’s 30 May submission is “very radically different” to the case previously put by the OFT. Again, on the back of the CAT’s comments in the *Tobacco* judgment, it will be interesting to see how the OFT’s conduct of the case is assessed by the CAT.

“Hub-and-spoke” cartels

The judgment in the Tesco appeal is also likely to attract interest in terms of its substance. Okeoghene Odudu, writing on indirect information exchange for the European Competition Journal in 2011, stated that it is “one of the most interesting and challenging competition law questions of recent times”. There is considerable uncertainty surrounding the bounds of permissible exchanges in this area.

In the *JJB Sports* appeal of the OFT’s *Replica Football Kit* decision, the Court of Appeal found that there would be a competition infringement “if retailer A [Tesco in this case] discloses to supplier B [any of the dairy processors] its future pricing intentions in circumstances where A [Tesco] may be taken to *intend* that B [the dairy processor] will make use of that information to

influence market conditions by passing that information to other retailers [the other supermarkets]”. (Emphasis added.)

Stephen Morris QC, counsel for the OFT, argued that it was clear that Tesco intended the sensitive retail information to be passed to the other competing supermarkets. Conversely, Tesco denied that it passed information to the dairy processors with the required intent. Tesco stressed that it is vital for a finding of infringement that the retailer knows that the information provided to the supplier will be passed on to competing retailers. Even if it is difficult for the OFT to demonstrate the requisite intent, that in no way absolves the OFT of the need to demonstrate it.

Conclusion

The CAT’s judgment in the Tesco appeal seems set to: (i) provide clarity on the level and quality of evidence that is required to prove allegations of infringement; (ii) include observations of some kind on the OFT’s conduct of its defence; and (iii) provide guidance on the interpretation of the substantive test for finding that a “hub-and-spoke” cartel exists. Judgment is expected later this year and will be eagerly anticipated by private practitioners and OFT officials alike.

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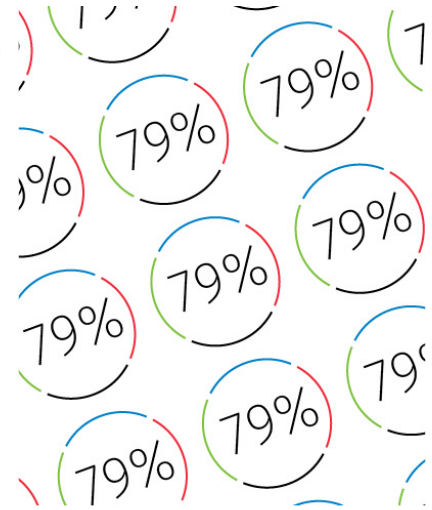
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