

not significantly limited by the rule which required the Association merchant to trade in washed sand and gravel from Association sources only ; a customer who wanted non-Association washed sand and gravel could buy it ex-pit or through a non-Association merchant. Conversely, the non-Association producer could deal with non-Association merchants or sell direct to customers. A customer who wanted Association sand but did not want to order through an Association merchant could obtain the material direct from an Association member. The Associations did admit, however, that the system might operate to the disadvantage of a non-Association merchant because he could only obtain the Association washed sand and gravel at delivered prices and with no $7\frac{1}{2}$ per cent. merchant discount (so that in practice it might not be worth the while of a non-Association merchant to deal in Association products at all); they also agreed that a customer might be inconvenienced in some circumstances, e.g. if he would have preferred to obtain all his building materials from a non-Association merchant.

281. The Associations told us that their reason for refusing to supply non-Association merchants at ex-pit prices was to prevent such merchants from undercutting the Association minimum prices on short hauls in the Scheduled Areas. The reason for allowing a $7\frac{1}{2}$ per cent. discount only to Association merchants was that there was no call for paying it to other merchants ; other merchants could if they wished apply to become Association merchants.

282. The Associations argued that their merchanting arrangements had not reduced competition in the distribution of washed sand and gravel because non-Association merchants could obtain supplies from non-Association producers, because Association merchants had an incentive to sell more goods in order to earn more $7\frac{1}{2}$ per cent. discounts, and because the customer had freedom of choice and was "not unduly restricted at any rate in selecting the pit or the merchant to whom he goes".

283. On the subject of the qualifications which they require of an Association merchant, the Associations said that they considered that their agents should be qualified to give advice to customers about the types of materials suitable for particular purposes, and this was why their agents had to be established builders' merchants. The £500 deposit required from an Association merchant was a far smaller financial outlay than a builders' merchant would expect to have to make to finance his purchases of washed sand and gravel in the ordinary way ; the deposit was a perfectly reasonable requirement which satisfied the Association members as to the financial stability of the merchant and gave them some security for the payments for sand and gravel for which the merchants were liable to them.

284. The Associations said that a newcomer to the trade of builders' merchant would be able to establish himself without being able to supply Association washed sand and gravel. Therefore their stipulation that an Association merchant must be already established was not in itself any hindrance to a newcomer to the trade. There were indeed many well established builders' merchants who did not deal in sand and gravel at all.

CHAPTER 7: CONCLUSIONS ON THE PUBLIC INTEREST AND RECOMMENDATIONS

285. In this inquiry we are concerned with the supply of a class of building materials which is widely used over a large part of Scotland, including the main industrial area. Sand and gravel suitable for building or civil engineering purposes are supplied in the Area of this reference by some eighty producers, but over a third of the total output is supplied by five producers who are members of the Washed Sand and Gravel Association (the

“ West Association ”) or the Mid-Scotland Washed Sand and Gravel Association, or of both, together with another producer whose sales are normally invoiced through the West Association and who observes all Association rules and prices (see paragraph 82). Taking washed sand and gravel alone, these producers supply three-quarters of the total. They and the Association merchants operate practices and arrangements which restrict competition. We have found no evidence of practices or arrangements restrictive of competition in sand and gravel on the part of others in the Reference Area.

The Common Minimum Price and Haulage Rate System

286. In the report we have used the expression “ the common minimum price and haulage rate system ” to denote the charging by members of each Association of agreed common minimum ex-pit and delivered prices and common minimum Recorded Haulage Rates, together with the observing by members of each Association of the other Association’s prices when selling in its area and the exchanging of price information between the Associations. These arrangements are described in Chapters Two and Four. In this chapter we refer to them for convenience as the minimum price system.

287. In considering the effect of this system on the public interest, we have first examined its effect on the level of washed sand and gravel prices in the Reference Area. In this connexion two factors have seemed to us to be of special significance: the first is the wide variation of costs among producers; the second is the great weight and bulk of the product in relation to its value, which causes transport costs to account for a high proportion of the delivered price.

288. Because of the varying quality and workability of the individual deposits, a wide variation of costs among producers is to be expected in an extractive industry such as this, as was emphasized by the Associations. This means, however, that producers with low-cost pits would have considerable scope for reducing their ex-pit prices if that was necessary in order to compete. Whether in practice they would be forced to do so if price competition was unrestricted would be determined by the facts of their particular situation.

289. The delivered prices charged in any market under unrestricted price competition would depend on the size of the demand at particular prices, the production costs of the suppliers by whom it could be met, and the distance of the suppliers both from that market and from other markets to which their products might be sent. It is necessary to emphasize this factor of location because of the importance of transport costs in the industry; the cost of moving sand fourteen miles, for example, may be as great as its ex-pit price (see paragraph 46). Delivered prices would thus be low in markets whose needs could be fully met from competing nearby low-cost pits from which other markets were further away. They would be high in markets which had to draw part of their supplies from a distance, or from high-cost producers, or from low-cost producers with little competition to face. Similarly, ex-pit prices would be high at pits situated near markets which had to draw part of their supplies from a distance or from high-cost producers, and would be low at pits which had to sell part or all of their output to distant markets, or which were faced in nearby markets with competition from low-cost pits which were also close to them.

290. It follows that, taking into account the wide variations in production costs and the heavy incidence of transport charges, under price competition

both ex-pit and delivered prices would be certain to vary, and might well vary considerably, from one place to another. Under the Associations' arrangements, by contrast, throughout each of the Scheduled Areas there is only one ex-pit price and one delivered price for any given grade of sand or gravel. As the prices are common *minimum* prices, the intention of the system is clearly to prevent prices from falling below the agreed level, and it is significant that the great majority of sales take place at the minimum prices. It seems to us to follow from this that both sets of prices have been set at, or above, the highest prices at which transactions might be expected to take place in any part of the Scheduled Areas under unrestricted price competition. For if they had not been so set, transactions in those places where prices would be high under unrestricted price competition would be effected at prices above the Associations' minimum prices. We conclude, therefore, that at least some consumers in the Scheduled Areas are paying more, and in some places possibly much more, than they might expect to pay if there were price competition. Their position is somewhat eased by their being able to buy at the Associations' ex-pit prices or at the Associations' delivered prices, as suits them (the buyers) best. A few consumers whose nearest pit is at a comparatively great distance from them and has ex-pit prices close to those which might be expected under price competition, may be obtaining their sand and gravel at lower delivered prices than would be expected under price competition.

291. In the Associations' Merchanting Areas, on the other hand, the delivered prices vary from one place to another and the position is somewhat different. Under the Associations' arrangements the consumer has the option of either paying their delivered prices or paying the common ex-pit price and making his own arrangements for delivery. As long as this option is effective, the haulage element in the Associations' delivered prices cannot be far out of line with the cost of haulage by contractors or by the consumer's own transport; indeed, the evidence we have suggests that the Associations' haulage charges are in general about the same as those of other hauliers. The delivered cost to consumers in the Merchanting Areas, which is what really matters to them, is thus the sum of a haulage charge which is about the same as it might be expected to be under price competition and an ex-pit price which we have found to be often higher than could be expected under price competition. We conclude, therefore, that in the Merchanting Areas also some consumers at least are paying more than they might expect to pay under price competition.

292. The unsystematic way in which prices are decided (see paragraphs 216 to 223 above) also supports the view that the Associations' arrangements tend to keep them high. There is no attempt to calculate the prices on the basis of the costs of the most efficient member, on the average costs of all the members, or on a minimum or average rate of profit. The practice is simply to fix prices at a level which commands the general assent of all the members notwithstanding the wide variation in their circumstances; one of the Associations told us that the agreed price was a compromise price having in view what the market would stand. In this the Associations appear, quite naturally, to rely on their dominant position in their market, particularly in certain parts of Central Scotland, though they have to take account of the competition from non-Association producers of washed sand and gravel and from other materials, notably whinstone. In these circumstances the tendency will be to fix prices that are on the average higher than those which would prevail if each firm pursued its own policy. This view of the Associations' price-fixing activities is supported by their origin and history.

There was, for example, the West Association's quota scheme together with the restrictions on opening new pits and extending plant (see paragraphs 163 to 169 and 171 to 177). That prices are intended to be at a higher level than they would be in the absence of the Associations' arrangements is also to be inferred from some of the arguments they advanced, in particular the importance of avoiding price cutting and the claim that competition is transferred to service and quality, with the implication that there would be scope for selling more cheaply at some loss in service and for selling a wider range of qualities, including lower qualities at lower prices.

293. Further light is thrown on the system by certain cases which have come to our notice where it has been departed from. There are the special low prices given by the West Association on several occasions to two customers, when the Association made concessions in order to meet competition from whinstone (see paragraph 97). Another possible example is the special arrangement between one West Association member and a producer of ready-mixed mortar for supplies of washed building sand below Association prices for washed sand (see paragraph 98). These cases indicate that, when there is outside competition, prices can be, and are, brought down. At present, the only price competition comes from outside the Associations. If this competition were extended to members of the Associations, it is reasonable to conclude that differences in price would be more numerous. This conclusion is supported by the cases in which excess stocks have been accumulated: this is what may be expected to happen when prices are artificially kept higher than they would be if there were price competition and when it is not possible to reduce the price in order to dispose of the excess. In one case (see paragraph 140), the Association agreed that the producer concerned should be allowed to sell off stocks at prices below the prescribed minima and in fact the producer resigned from the Association in order to be free to settle his own prices. In the other case, described in paragraph 226, large stocks of gravel have been accumulated, presumably because they could not be disposed of at Association prices, and they have been entirely written off in the producer's books.

294. We have derived little assistance from examining the profits made by those producers whose accounts we studied (see Chapter Four). The profits of these producers, both the Association members and the non-members (including a producer of unwashed sand), show a wide variation. Among the Association members the figures range from substantial profit rates in the case of some producers down to losses on some of the operations of the largest producer. The wide variation is, however, typical of an extractive industry in which costs vary greatly from pit to pit and does not necessarily afford any criterion of relative efficiency. Moreover, the fact that each pit has to some extent, by reason of its situation, its own market, in which conditions may differ markedly from the market available for other pits, is a distinctive feature which has to be taken into account. These factors make it impossible for us to attach any special significance to variations in costs and profits among producers whether or not they belong to the Associations.

295. We have considered the fact that the largest producer (responsible in 1953 for about 45 per cent. of all sales of Association producers) has in recent years been making the lowest rates of profit among Association members and that one of his pits has consistently shown a loss (see paragraphs 225, 226 and 293). This may be thought to show that the abolition of the Associations' minimum price system might not lead to any material reduction in prices in the districts where his strategic position is strong. In other districts, however, there is the possibility of quite substantial reductions

if competitive market conditions are allowed to operate. The pit showing a loss, moreover, has a large accumulation of certain sizes of gravel and for this a market might conceivably have been found if the producer had been free to sell the output at a lower price. We are unable to attach any particular significance to this producer's profit and loss figures.

296. We have also considered the profits made by the two Mid-Scotland Association members referred to in paragraphs 241 and 273 above, before and after the start of the Association in 1951, and the Associations' argument that these figures show that the coming into being of the Association did not put up profits. The profit rates for the two firms together rose from 21.4 per cent. in 1950 to 30.1 per cent. in 1953; this was a bigger increase than that of members of the West Association during the same period. There were changes in output over this period but in so far as the figures demonstrate any trend it is that these producers' profits increased noticeably when the Mid-Scotland Association had become well established.

297. Our conclusion is that the effect of the minimum price system has been to keep the general level of prices for washed sand and gravel in the Reference Area higher than it would be under price competition.

298. Higher prices are in themselves an obvious disadvantage to the consumer, but it remains to be considered whether, in the circumstances of this industry, they have compensating advantages. The Associations have represented to us that, by preventing price cutting between Association members, the minimum price system makes for stability in the prices of washed sand and gravel in their areas and also removes the danger of "cut-throat" competition. We agree that the system tends to promote stability of prices but we are unaware of any evidence to suggest that in its absence prices would fluctuate to an extent which would seriously prejudice the interests of either producers or consumers. As for the threat of "cut-throat" competition, there is no evidence that the washed sand and gravel trade in the Reference Area has ever experienced competition which might reasonably be so described. Moreover, this is one of the industries where output is least likely to be affected by a general depression in trade; it can, we think, be assumed that Government action to deal with a depression would include measures at least to maintain activity in public works, and this could be expected to call for large quantities of sand and gravel. In fact, washed sand and gravel has been an expanding industry in Central Scotland. It seems to us that any apprehensions which the Associations feel on this matter are founded on the experience of other industries a quarter of a century ago.

299. The Associations emphasized that by their efforts they had developed the washed sand and gravel industry in the Area and had satisfied a public demand for the material (see paragraph 267). While admitting that there was no competition in price between their members, they contended that competition between them was thereby directed to quality and service. We have considered whether this concentration of competition on quality and service has, by promoting the use of good material, operated in the public interest by protecting the public from the use of inferior materials. This would be in line with the Associations' claims in connexion with screened unwashed concrete sand (see paragraph 278). We see no grounds for thinking that price competition would deprive the market of good washed sand and gravel, or that building contractors, local authorities, and other users would not insist on the standard of quality they regarded as adequate for any particular use. In fact, it is possible that there would be a greater variety of qualities produced at more varied prices, a result which appears likely judging by the variety of prices for washed sand and gravel now charged

by the non-Association producers from whom we have collected price figures. Similarly, we see no reason why under price competition those purchasers who wish for a high quality of service should not continue to obtain it.

300. The Associations claimed that their arrangements facilitated the transfer of orders between their members. This may well be so, but we doubt whether their customers derive any great advantage from the facility. The number of producers in each Association is small, and it does not appear to us that consumers would be put to much inconvenience if they had to find another supplier for themselves when a particular firm could not supply them. Nor does it seem to us impossible that similar facilities would be provided under a competitive system if they met the needs of both producers and consumers.

301. We recognize that, as the Associations argued, the exchange of technical information may be promoted by membership of the Associations, but it seems to us that this also could be achieved without restricting competition.

302. It is claimed by the Associations that their system has promoted efficient development. It is a fact that the industry has grown substantially in recent years, but the causes of this growth are numerous and we see no reason to suppose that it would not have occurred in the absence of the minimum price system. Indeed, since the system protects high-cost producers, the probability is that it tends to discourage, rather than to hasten, the introduction of improvements in methods. It is true that, even without a system of minimum prices, some of the producers, because of their existing location and the nature of their deposits, would still be in a quasi-monopolistic position, and to them the presence or the absence of the system would make only a slight difference. Others, however, would be exposed to keen price competition if the present arrangements were abolished. In this sector of the trade, therefore, it is reasonable to assume that the abolition of the arrangements would contribute to greater efficiency.

303. To sum up, we have been unable to find any sufficient justification in this industry for the artificial maintenance of uniform prices higher in certain instances than the consumer would otherwise be called upon to pay. We conclude, therefore, that the minimum price system operates and may be expected to operate against the public interest, and we recommend that it be discontinued.

Practices and Arrangements incidental to the Common Minimum Price and Haulage Rate System

304. The practices and arrangements with which we are concerned here are central invoicing, the stop list procedure, water content allowances and rules about weighing, rules about screened unwashed concrete sand, and a rule about the submission of public and local authority schedules to the Association Secretaries. To a greater or less degree, each of these practices and arrangements supports the minimum price system, though each may have other purposes.

Central Invoicing

305. The Associations said that the main purpose of their central invoicing scheme was to control credit and that the scheme had a number of administrative conveniences not connected with the minimum price system. They agreed, however, that the scheme also provided a means of ensuring that the Association members strictly observed the minimum prices and

other arrangements ; we are satisfied that this is its most important effect and that central invoicing is in fact an integral part of the minimum price system. We also consider that, even in the absence of a minimum price system, central invoicing might in itself tend to the observance of common prices. We conclude, therefore, that the central invoicing scheme is against the public interest and should be discontinued.

Water Content and Method of Weighing

306. The actual water content of washed sand and gravel supplied by Association members is not a matter with which the Associations are concerned. We have been unable to ascertain how it compares on the average with that of other producers either in Central Scotland or elsewhere, but we have no grounds for thinking that it is either greater or less.

307. The water content allowances for sales in the West Association Areas are common agreed reductions in the minimum prices and haulage rates and therefore have the same effect as any other agreed variation in price. The minimum price system could not be maintained if producers were free to make whatever water content allowances they chose. Similarly, the stipulation of a place of weighing has a bearing on the price because of the loss of weight by drainage in transit, even though some exceptions are made to the advantage of the consumer with a weighbridge on the building site or en route to the site. Thus this practice to some extent supports the minimum price system. In the absence of the system, however, we should see no objection to the uniform water content allowances and the stipulation about weighing because other elements in the prices will be variable. In fact, if water content allowances are given, uniform rates of allowance will make it easier to compare net prices.

Unwashed Sand

308. Three West Association rules which touch on trade in unwashed sand were described in paragraph 119 above. Of these, the first and the second (not to supply washed sand in fulfilment of an order for unwashed sand and not to quote for washed sand and gravel to producers of unwashed sand) could operate to strengthen the Association's arrangements—the former by preventing price cutting in the form of false description of goods and the latter by restricting channels of distribution. However, these two rules are now of so little practical significance that the Association members appeared to have forgotten their existence. We have, therefore, not taken them into account in considering the effect of the Association's practices and arrangements on the public interest.

309. The other rule, not to produce or quote for screened unwashed concrete sand, is still operated and we have, therefore, examined it more closely. We consider that the rule has the effect of restricting the production of a material which might effectively compete with washed concrete sand for some grades of concrete. Besides this rule, which applies to Association members, trade in screened unwashed concrete sand is further restricted by the clause of the Merchant Agreement precluding Association merchants from selling this material, or offering it for sale, in the areas of either Association.

310. Unwashed sand, both screened and unscreened, is used in the Reference Area for making concrete. The evidence we have from users on this point suggests that their choice between washed sand and unwashed sand, screened or unscreened, has been made on the usual technical and

cost considerations. There is no suggestion that their choice has been dictated by lack of supplies of screened unwashed concrete sand. Nevertheless, these rules about trading in screened unwashed concrete sand do to some extent support the minimum price system by lessening actual or potential competition from an alternative material. Furthermore, they are in themselves restrictions on trading freedom and they seem to us to have no beneficial results. In our view they may be expected to operate against the public interest and should be discontinued.

Submission of Public and Local Authority Schedules by West Association Members through the Association Secretaries

311. Whatever the intention of the West Association in introducing the arrangement that public and local authority schedules for the supply of washed sand and gravel should be submitted by members through the Association Secretaries, and even though in practice it may have been operated only in the case of one local authority and for the purpose of quoting reduced prices, we consider that the arrangement inevitably provides a further support for the minimum price system and is in itself restrictive of price competition without any compensating advantage. It is against the public interest and should be discontinued.

Stop Lists

312. The Associations' stop lists operate only on bad payers and are not obligatory on members. We should see nothing contrary to the public interest in the continuance of the stop lists on this basis if the minimum price system were terminated.

Other Association Arrangements

313. We have not thought it necessary to record any conclusions on a number of other Association rules which might in certain circumstances be used to support the minimum price system, because we have recommended that the system be discontinued and in its absence such rules would be of little or no significance. The most important rules in this category are the disciplinary and arbitration provisions of the Constitutions and of the Merchant Agreement (see paragraphs 133 to 138, 142 to 149).

Merchanting Arrangements

314. In considering the effects on the public interest of the merchanting arrangements, it is important to bear in mind the location of the non-Association pits producing washed sand and gravel and the fact that, of the total washed material supplied in the Reference Area, three-quarters is supplied by the Association producers. The rule that Association merchants may not obtain washed sand and gravel from non-Association producers does not of itself make much difference to consumers' choice of washed sand and gravel supplies in the Glasgow district, where there is little such material produced from non-Association pits. In that district, however, the terms given to Association merchants and withheld from other merchants may have the result that a non-Association merchant does not supply washed sand and gravel, and accordingly that a consumer's choice of merchant is limited if he desires to place his orders for all building materials with one merchant. Outside the Glasgow district, in the southern part of the West Association area and in the Mid-Scotland Association area, there is more potential competition from non-Association producers, but the business of most Association merchants appears to be centred on Glasgow, so that outside

Glasgow the consumers' choice of either suppliers or merchants is probably little affected by the merchanting arrangements.

315. The exclusive-buying arrangement is probably little or no hindrance to non-Association producers, actual or potential, of washed sand and gravel because there are many builders' merchants who are not Association merchants.

316. On the other hand, competition among merchants is clearly restricted as a result of the merchanting arrangements. This is because the combined effect of the exclusive-buying rule and the refusal to allow trade discounts or ex-pit prices to non-Association merchants is to divide the washed sand and gravel merchant trade into two parts—Association supplies handled by Association merchants only and non-Association supplies handled by non-Association merchants only. This division of itself restricts competition in distribution, and in the Association sector the restriction is reinforced by the minimum prices and haulage rates and by the fixed merchant discount of $7\frac{1}{2}$ per cent.

317. In so far as they support the minimum price system, we cannot regard the operation of the merchanting arrangements as being in the public interest, and we can see no way in which the exclusive character of the arrangements is advantageous. In effect, the argument of the Associations is simply that they are entitled in law to select their agents collectively and to make an exclusive arrangement with them. We accept this, but we have to go further and consider whether there are any beneficial effects of the arrangements to be set against the adverse effects on the public interest which we have found to flow from them. Finding no such benefits, we conclude that the arrangements are against the public interest.

318. It is possible that, if the minimum price system were brought to an end and the merchanting arrangements ceased to be exclusive, the Associations would still wish to have a selected list of merchants who would accept responsibility for payment of customers' accounts and make a deposit as a guarantee of financial stability and would receive a special discount in return—subject always to any individual producer being free to give to other merchants what discounts he chose. There would then be no rigid division of the merchant trade between two classes of merchants, and merchants who were not on the list would probably be able to obtain supplies of washed sand and gravel from Association members on terms which would make it worth their while to supply the goods. In these circumstances we should not consider the maintenance of such a list to be against the public interest.

319. Since we contemplate that a list of selected merchants might continue to exist, we have considered whether the conditions at present laid down for admission to the list are unreasonable. The applicant must be an established builders' merchant and he must put down a deposit of £500. Requiring the applicant to be already established as a builders' merchant is a reasonable practical stipulation for ensuring that Association merchants can operate as agents with the necessary technical knowledge to advise their customers on the choice of building materials. That this does not even at present hamper the newcomer who wants to establish himself as a builders' merchant is suggested by the existence of numerous non-Association merchants in the whole area. As a guarantee of financial stability £500 seems to us to be a reasonable sum and unlikely to impose a serious burden on the merchants. We conclude that the conditions laid down for acceptance as an Association merchant do not in themselves operate against the public interest and could not be expected so to operate in the altered conditions which we envisage for the future.

Summary of Conclusions and Recommendations

320. Our principal conclusions and recommendations may be summarized as follows:

(1) Under the common minimum price and haulage rate system, the general level of ex-pit and delivered prices for washed sand and gravel is higher than it might be expected to be under price competition, and we have been unable to find any justification for the artificial maintenance of these prices. The system operates against the public interest and should be discontinued.

(2) The stop lists, the fixed water content allowances in the West Association areas, and the prescribed methods of weighing all support the common minimum price and haulage rate system to a greater or less extent. They are not in themselves contrary to the public interest, and in the absence of the system we should not expect them to operate against the public interest. Central invoicing, the rules about trade in screened unwashed concrete sand, and the West Association's arrangements about the submission of public and local authority schedules through the Association Secretaries are against the public interest and should be discontinued.

(3) The existing merchanting arrangements operate against the public interest and should be discontinued. In the absence of the common minimum price and haulage rate system, however, we should see no objection to the maintenance by the Associations of a selected list of merchants, always provided that the new merchanting arrangements were not exclusive.

DAVID CAIRNS (*Chairman*)

G. C. ALLEN

JAMES ARCHDALE

W. GAVIN CULLEN

BRIAN DAVIDSON

C. N. GALLIE

C. H. P. GIFFORD

A. L. GOODHART

GORDON STOTT

J. A. R. PIMLOTT (*Secretary*)

3rd November, 1955.