

## Conclusions

### A. The monopoly situation

6.1. Our reference requires us to investigate and report whether a monopoly situation in relation to the wholesale supply of car parts in the United Kingdom exists by virtue of section 6(1)(c) of the Fair Trading Act 1973. A monopoly situation (called, under section 11 of the Act, a complex monopoly situation) will exist by virtue of section 6(1)(c) if at least one-quarter of the car parts supplied by wholesale in the United Kingdom are supplied by two or more persons who so conduct their respective affairs as in any way to prevent, restrict or distort competition in connection with the production or supply of car parts. In investigating this we are required to limit consideration to the practice whereby suppliers of car parts require persons to whom they supply car parts to acquire those parts exclusively from them or from sources approved by them.

6.2. Wholesale supply of car parts is defined by the reference as wholesale supply of parts 'for resale as such or for replacement of existing parts in a motor car'. The reference therefore relates to replacement equipment (usually known as RE) and excludes the supply by component manufacturers of parts for use as original equipment in the manufacture of cars (usually known as OE). For the purpose of ascertaining the total supply of replacement parts in the United Kingdom we have taken wholesale supply to mean the stage of supply at which replacement parts are supplied for resale by car manufacturers and importers, by other importers of parts and by component manufacturers (other than to car manufacturers and car importers).

6.3. In the absence of any official statistics or reliable estimates, our own estimate (arrived at as described in Appendix D) is that by value the total wholesale supply, in this sense, of car parts in the United Kingdom in 1980 was approximately £1,480 million.

6.4. Where car manufacturers or importers require car parts to be bought exclusively from them, the requirement is normally expressed in a clause in a franchise agreement; but, as we have pointed out in Chapter 4, there are in addition various practices which, it is alleged, tend to induce franchised dealers to buy exclusively whether or not they are contractually bound to do so. Any of these practices (which we consider further in paragraphs 6.11 to 6.15 below) might amount to a requirement to buy exclusively, but we did not find that at present any of them in fact do so. Therefore for the purpose of establishing which car manufacturers or importers do (in the words of the reference) 'require' their franchised dealers to buy exclusively, and thus might be parties to a complex monopoly situation, we took into account only those who impose a contractual obligation to buy exclusively. Similarly, we considered component manufacturers only where there is an express exclusivity requirement. As we have recorded in paragraph 2.12, the larger component manufacturers either own, or have interests in, certain distributing

organisations. These include factoring businesses, cash-and-carry warehouses and retail shops. It was suggested to us that this forward integration by component manufacturers implied that distribution of their production was characterised by widespread exclusive buying requirements. In fact, however, we found only two cases of component manufacturers placing any formal requirement on distribution outlets (either owned or independent) to buy exclusively from them (see paragraphs 4.60 to 4.64). In Appendix B we set out the names of the 22 car manufacturers and importers and of the two component manufacturers who impose such contractual obligations, together with the relevant extracts from their agreements.

6.5. One of the likely effects on competition of exclusive buying requirements is that they may lead to a restriction of competition in that, if a supplier imposes exclusivity on any person, other suppliers and potential competitors may be prevented from competing for that person's custom and part of the market may thus be closed to them. For reasons which we discuss in paragraphs 6.21 to 6.25, we consider that the exclusive buying requirements of car manufacturers and importers do in fact materially restrict the ability of component manufacturers to compete in this way. The car manufacturers and importers concerned (those listed in Appendix B) in 1980 supplied replacement parts to the value of about £546 million in the United Kingdom, or about 37 per cent of the total of £1,480 million supplied in the United Kingdom (see paragraph 6.3).

6.6. The exclusive buying requirements of the two component manufacturers found to impose such requirements do not, on the other hand, appear in practice to have any material restrictive effect on competition. Lucas's exclusive arrangements with its service agents, described in paragraphs 4.63 and 4.64, do not prevent them from acquiring parts from other sources, though they do require them not to acquire parts which are in direct competition with Lucas parts. The service agents concerned appear, however, to be in effect a part of the Lucas group's distributing organisation; factors and other customers who wish to buy Lucas parts buy from them rather than from the Lucas factories (though a large customer may, exceptionally, buy from the factories) and are themselves free to buy competing products from other sources. Lucas's exclusive arrangements impose no restriction on retailers who sell Lucas parts or on wholesalers from whom retailers normally buy.

6.7. Similar considerations apply to the exclusive buying requirements of Automotive Products; but in addition only a very small proportion of this company's parts are supplied through the sub-depots required to buy exclusively (see paragraph 4.61) and the remainder through outlets which have no such obligation.

6.8. There is no evidence that the exclusive arrangements of Lucas or of Automotive Products have in practice any restrictive effect on competing component manufacturers, and we received no complaints from competitors that they were denied access to the market. Competing component manufacturers are indeed not prevented from selling to any wholesale or retail outlets supplied by Lucas service agents or Automotive Products' sub-depots.

6.9. In our view the exclusive arrangements of these two component manufacturers have no material restrictive effect on competition.

6.10. We conclude that a complex monopoly situation under section 6(1)(c) of the Act exists in favour of the car manufacturers and importers listed in Appendix B, who together supply at least one-quarter of the car parts supplied in the United Kingdom and so conduct their respective affairs as to restrict competition in connection with the supply of car parts in that they require persons to whom they supply car parts to acquire them exclusively from them or from sources approved by them.

## **B. The public interest**

### **Practices other than exclusive buying requirements**

6.11. In assessing the effect on the public interest of the practice of requiring exclusive buying of car parts, we think it is essential to keep in mind the general economic background of the car and components industries as we have described it in Chapter 2. Both industries have been adversely affected by the decline in demand for British cars, and in the market for replacement parts they have increasingly become rivals. In these circumstances component manufacturers took the opportunity afforded by our inquiry to draw our attention to a variety of practices which they considered are impeding the components industry or even threatening its survival. It was represented to us that the components industry needed protection against what it saw as a process of monopolisation of the parts market by vehicle manufacturers and importers, and that exclusive buying requirements imposed by them were part of the monopolisation process. The Accessories and Components Section of the SMMT drew our attention to the decline in the United Kingdom car industry and said that 'the resulting struggle for the profitable sectors remaining available to UK business should not in our view be distorted by perpetuation or extension of entrenched anti-competitive practices'. The practices to which our attention was drawn include those (considered in paragraphs 4.6 to 4.28) concerned with minimum stock requirements and stock control systems, sales or purchase targets, and discounts and bonuses, by all of which it is alleged that car manufacturers and importers restrict the freedom of their franchised dealers to buy parts; they also include those (considered in paragraphs 4.37 to 4.60) concerned with the use of tooling, branding and copyright and with use of a car manufacturer's name in advertising, by which it is alleged that manufacturers restrict the freedom of component manufacturers to sell parts.

6.12. We recognise that the future of the components industry has important implications for the public interest, affecting, as it does, the employment directly and indirectly of a very large number of workers and the export of a substantial volume of goods (see paragraph 2.7). But our terms of reference are narrowly drawn and it is therefore necessary to consider whether by adopting any of the practices mentioned in the previous paragraph car manufacturers and importers 'require persons to whom they supply car parts to acquire them exclusively from them or from sources approved by them'.

6.13. Since there is a system of restricted distribution for new cars, their distribution being through dealers who are franchised by the manufacturer

or importer (and the merits of this system are not the subject of our inquiry), we think it is inevitable that the franchisors should seek to ensure that their dealers also provide an adequate and efficient supply of approved parts to meet the demands of their customers. We regard this as a legitimate commercial objective and as one that is generally in the interests of the car-buying public. Minimum stocking requirements are in principle an acceptable method of achieving this, provided that the levels required are reasonable and not so high as to ensure that in practice no other parts are stocked. The levels now required appear to us to be reasonable in this sense, and we therefore consider that minimum stocking requirements as they exist at present do not amount to a requirement of exclusivity. The considerable assistance given by car manufacturers and importers to their franchised dealers in the installation and operation of computerised stock control systems (see paragraphs 4.23 to 4.28) may tend to reduce the extent to which dealers buy parts from other sources; but we consider that this too does not amount to requiring exclusivity.

6.14. The sales or purchase targets mentioned in some franchise agreements (paragraphs 4.10 to 4.13) are all, insofar as they relate to parts, inducements to buy parts from the franchisor. Though there may be no penalty if a dealer fails to achieve his target, it is nevertheless one of the standards by which his performance as a franchisee is judged and to that extent he clearly has an incentive to achieve his target. Discounts and bonuses related to the volume of business done with the supplier (paragraphs 4.14 to 4.17) are also inducements to franchised dealers to buy from their franchisors. Moreover, the inducement may be more marked when, as we found in a few cases, discounts or bonuses are stated to be conditional on exclusive buying. Even this does not necessarily ensure exclusivity, and the levels of discounts and bonuses in the volume-related schemes of which we obtained details, whether or not they were conditional on exclusive buying, are not in our view high enough to have any material tying effect. Neither sale or purchase targets nor volume-related discounts or bonuses as they occur at present can in our judgment fairly be held to fall within our terms of reference.

6.15. On the evidence available to us we do not think that any of the practices referred to in the two preceding paragraphs are at present being operated in such a way as to ensure that franchised dealers buy parts exclusively from their franchisors. However, they undoubtedly could be operated in this way, and if exclusivity clauses were to be removed from franchise agreements, any of them separately, or all of them together, might be used as an alternative method of achieving exclusivity. In that event action could if necessary be taken under the Competition Act or, if it were more appropriate, under the appropriate provisions of the Fair Trading Act to investigate them or, if necessary, to investigate the working of the whole franchise system.

6.16. The restrictions which, according to component manufacturers, are placed on them by some car manufacturers whom they supply (described in paragraphs 4.37 to 4.60) relate to the use of tooling owned or partly owned by car manufacturers, the use of a component manufacturer's brand name, the use of copyright by car manufacturers to prevent manufacture of parts by component manufacturers except under licence, and the use of a car manufacturer's name in advertising by a component manufacturer.

6.17. All these practices may well have the effect of restricting the extent to which component manufacturers can compete in the replacement parts market; they may also limit the extent to which it is possible for franchised dealers to buy parts other than exclusively from their franchisors. They appear to us, however, to have no relevance to the practice referred to us. They are all defended by the car manufacturers as being reasonable steps to protect their own commercial interests. Since the practices have not been included in the reference we consider that it would be beyond the scope of this inquiry for us to express a view on the balance between the effect on the public interest of any restriction of competition involved and the commercial interests of the car manufacturers and importers.

6.18. These practices may, however, raise issues of public interest. The use of copyright to protect functional articles in the absence of any element of invention appears to us to be particularly capable of being directed towards unreasonable restriction of competition, and there may well be a case for some change in the law. However, this matter has been considered by the Whitford Committee (see paragraphs 4.55 and 4.56) and we note that the possibility of a change in the law is considered in a recent Green Paper (Cmnd 8302). Other practices concerned might be made the subject of inquiry under the Competition Act or the Fair Trading Act, particularly if the removal of exclusive buying clauses led to any of them being operated with greater emphasis on restricting the extent to which component manufacturers can supply the replacement parts market.

### **The effect on the public interest of exclusive buying requirements by vehicle manufacturers and importers**

#### **Restriction of access to the market**

6.19. A major potential objection to the requirement that franchised dealers of car manufacturers and importers must buy parts exclusively from their franchisors is that component manufacturers are excluded from part of the market.

6.20. Most parts for cars made in the United Kingdom are obtained from British component manufacturers, and to this extent, although the British components industry is prevented by exclusivity arrangements from supplying replacement parts direct to franchised outlets, it nevertheless supplies this part of the market indirectly through the car manufacturers.

6.21. However, although this is true of the component industry as a whole, it is not true of each individual component manufacturer separately. There are some small component manufacturers who benefit from the existing pattern of trade and who, in the absence of any elaborate selling organisation of their own, rely on their business with car manufacturers, through whom their output reaches the replacement market both in this country and in some cases abroad. On the other hand there are also many component manufacturers who are not only prevented by exclusivity from supplying franchised outlets directly, but do not supply car manufacturers (if only because they are unable to do so in the required volume) and therefore are excluded from supplying the franchised sector of the market even indirectly. The extent to which they

can compete in supplying the replacement parts market as a whole is restricted by the fact that, whether directly or through factors, they can supply only the non-franchised sector of it.

6.22. Even for those component manufacturers who do supply car manufacturers with replacement parts, the scope for competing for business in the franchised sector of the market is more restricted than it would be if they were able to sell, either directly or through factors, to franchised dealers as well as to their franchisors and thus had a wider range of potential customers.

6.23. A proportion of United Kingdom car manufacturers' approved parts is imported by them from overseas component manufacturers, and to the extent that this is so, British component manufacturers are prevented by the car manufacturers' exclusivity requirements from competing with imports in the supply of those parts to franchised outlets.

6.24. In the case of importers of foreign cars, although some approved parts (both OE and RE) are obtained in the United Kingdom, the great majority of approved replacement parts supplied by them to their franchised dealers are imported from the country of origin of the car. It follows that United Kingdom component manufacturers are to this extent prevented by exclusivity from competing with imports for a share of the market for replacement parts for imported cars. Since an increasing proportion, now more than a half, of new car sales is accounted for by imported cars (see paragraph 2.3), a substantial share of the market for replacement parts is foreclosed to British component manufacturers by car importers' exclusivity arrangements.

6.25. Insofar as component manufacturers are prevented by exclusive buying requirements from competing with one another and with car manufacturers and importers to supply part of the market, there is some limitation of the extent to which the most efficient component manufacturers can expand their business at the expense of the less efficient. In addition, insofar as component manufacturers are prevented from competing with imports, this is, on the face of it, likely to lead to a greater quantity of imports than would otherwise be the case, and so to an adverse effect on the United Kingdom balance of payments and on the prosperity of, and employment in, the components industry.

6.26. It was argued on behalf of the car manufacturers and importers that these adverse effects on imports, the balance of payments and employment are not in practice the effects of exclusivity but that they would indeed be the effects of its removal (see paragraphs 5.42 to 5.48). It was asserted that, since the British component industry was not fully competitive in price and quality with imports, the franchised sector of the market would, if it were free to buy parts from sources other than its franchisors, turn to imports. It is not possible to predict with certainty what would be the effect on imports of terminating exclusivity; but representatives of the components industry who gave evidence to us, both orally and in writing, contested the assertion that the industry would be unable to compete successfully in price or quality

with imports, and we see no justification for forcing protection against imports upon an industry which expressly disclaims the need for it.

6.27. We do not think that the existence of exclusivity does in practice provide protection against imports, since circumstances other than exclusivity determine whether parts supplied to the franchised sector of the market are of British or foreign origin and, to the extent that they see advantage in importing, the franchisors will, and indeed do now to differing extents, themselves supply imported parts to that sector of the market. In any case, even if it were established that the components industry and other industries dependent on it needed protection against foreign competition, the desirability of providing it and the method of doing so should be matters of considered government policy and should not be left to the operation of an anti-competitive practice adopted to further sectional commercial interests.

### **Price competition**

6.28. We considered what effect, if any, the exclusive buying requirements of car manufacturers and importers have on price competition in the replacement parts market and on the level of both wholesale prices charged to franchised dealers and retail prices to the motorist buying from franchised dealers.

6.29. It was argued by car manufacturers and importers that because the public has ample opportunity to buy replacement parts from alternative sources (non-franchised garages and High Street shops) the pressure on prices is such that the car manufacturers and importers are compelled to price competitively the parts they supply to their franchisees. They also claimed that the pricing of spares and its effect on insurance grouping were important competitive considerations in the marketing of their cars. However, these constraints may in practice be less effective than they were represented to be, since we think that many car owners (particularly first owners) are likely generally to go as a matter of course to a franchised dealer for spares, servicing and repairs and would not always regard other outlets as an appropriate alternative. Indeed the car manufacturers and importers themselves emphasised that it is only by going to a franchised outlet that the motorist can be assured that parts are suitable, reliable and safe; to the extent that a motorist is influenced by this argument he is unlikely to be influenced by the possibility of lower prices at other outlets. In any case the price of parts may seem of minor importance if the major item in a bill is the labour charge.

6.30. We do not suggest that there is no competitive limit to the prices that can be charged to or by franchised outlets, but we do believe that price competition is not fully effective, and that car manufacturers and importers have a substantial element of discretion in the determination of their prices. Since they are virtually the sole suppliers of replacement parts to their franchisees, we think it inherently likely that their prices are in many cases higher than they would be if there were other suppliers to that sector of the market. Some confirmation that this tends to be so is to be found in the Price Commission's report on 'Prices, Costs and Margins in the Manufacture and Distribution of Car Parts' (HC 220, October 1979). As a result of a survey covering

a limited number of parts the Price Commission stated (summary, paragraph 76, page 10):

In almost all cases we found that vehicle assemblers were able to buy the product lines in our survey at prices below those paid by factors. Main dealers, who also act as wholesalers, generally bought from vehicle assemblers at prices slightly above those paid by factors. Further along the distribution chain, there was a tendency for the prices paid by retail dealers for the product lines we studied to be higher than those paid by non-franchised garages.

Since franchised outlets usually sell to the public at the franchisor's recommended price one would expect any tendency for wholesale prices to be higher in the franchised sector to be reflected in higher retail prices. Here again there is some confirmation in the Price Commission's report. Paragraph 99 (page 12) states:

Many car parts are distributed in the aftermarket through a complex multi-tier system in which parts may go from specialist component manufacturer to vehicle assembler through his distribution network to franchised main dealers and then on to retail dealers and other distributors. The alternative chain of component manufacturer, factor and garage is shorter and the final price to the motorist tends to be lower although factors' buying prices are generally higher than those of vehicle assemblers.

6.31. The results of a limited inquiry which we ourselves made into the retail prices of selected parts also suggest that final prices to the motorist are generally higher when parts are distributed through the franchised network (see Appendix E).

### **Service**

6.32. The ready availability of parts is generally a matter of considerable importance to car owners, and is indeed in some circumstances of greater importance than price. The car manufacturers' and importers' stocking and distribution arrangements for parts appear generally to be good; there are regular deliveries at frequent intervals to franchised dealers in all parts of the country, and there are also arrangements for special deliveries of urgently needed parts. Nevertheless there are undoubtedly cases where suitable parts can be obtained even more quickly from local factors (see paragraph 5.20); while service of this kind is available to non-franchised garages, exclusive buying requirements largely prevent franchised garages and car owners who are their customers from benefiting from it.

### **Competition among factors**

6.33. The effects on factors of car manufacturers' and importers' exclusive buying arrangements are similar to the effects on component manufacturers as we have described them above. Since factors can supply only the non-franchised sector of the market and are virtually prevented from supplying the franchised sector, there is some limitation of their scope for competing with one another and with car manufacturers and importers both in price and

in service. If there were no such restriction, the widening of the market accessible to factors might enable the more efficient of them to provide a better and cheaper service to all sectors of the market.

### **Summary of adverse effects of exclusivity**

6.34. In the foregoing paragraphs we have described the adverse effects of exclusive buying requirements of car manufacturers and importers. These may be summarised as follows:

- limitation of the extent to which component manufacturers can compete with one another and with car manufacturers and importers (paragraphs 6.19 to 6.27);

- restriction of price competition (paragraphs 6.28 to 6.31);

- some limitation on the level of service from which the franchised sector of the market can benefit (paragraph 6.32);

- restriction of competition among factors (paragraph 6.33).

We consider that all these effects of exclusive buying requirements of car manufacturers and importers are against the public interest and that therefore the exclusive arrangements themselves are *prima facie* against the public interest.

### **Arguments in favour of exclusivity**

6.35. A number of arguments were put to us in defence of exclusivity, and we now need to consider whether there are any benefits to the public interest and if so whether they outweigh the detriments we have identified. We consider these matters under the following headings:

- the need for cars to be sold as part of a package;

- consumer choice;

- safety;

- warranties.

### **The need for cars to be sold as part of a package**

6.36. Car manufacturers and importers argued that it was necessary for them not only to supply cars but also to ensure that adequate supplies of suitable spare parts as well as adequate and technically satisfactory service were always available to the purchasers of their cars. They claimed a legitimate commercial interest in ensuring that all parts supplied through their franchised outlets should be of original equipment standard, tested and proved suitable and safe for the particular application in which they were to be used. This was important to them as being one of the ways in which they were able to compete with one another, and because it would be damaging to their reputation and therefore against their commercial interests if inferior, unsuitable or unsafe parts were put into their cars since any subsequent failure which might result would tend to be associated with the car itself rather than attributed to the parts concerned. Insistence on exclusive buying of parts by their franchised dealers enabled car manufacturers and importers to ensure the provision of appropriate parts, which together with the provision of

adequate and competent service was part of the package they must offer if they were to compete successfully in the sale of cars.

6.37. We agree that car manufacturers and importers have a legitimate interest in ensuring that adequate supplies of safe and suitable spare parts are available to purchasers of their cars. We have already said (paragraph 6.13) that we regard this as a legitimate commercial objective, and generally in the interests of the car-buying public. For this purpose, however, it is not necessary for a manufacturer or importer to insist that his franchisees obtain spare parts exclusively from him. A requirement that a franchisee carry a certain level of stock of spare parts obtained from the franchisor or from sources approved by the franchisor is sufficient to ensure that such parts are available to purchasers, without the added insistence that the franchisee obtain no competing parts from any other source. As we have said in paragraph 6.13, we consider that minimum stocking requirements are acceptable, provided that the minimum level required is no higher than reasonable.

6.38. The argument of the car manufacturers and importers, however, goes beyond this. They claim a legitimate commercial interest, not only in ensuring that an adequate supply of safe and suitable parts is available from their franchisees, but also in ensuring that all parts stocked by their franchisees are of a standard approved by them. The question which we are considering at this point is whether exclusivity benefits the public, not whether it suits the interest of car manufacturers and importers. Our view is that the public interest is protected because franchisees have their own interest in ensuring that they do not supply their customers with inferior parts. For franchisors to attempt by insisting on exclusive buying to ensure that all parts stocked are of a standard approved also by them does not, in our judgment, confer on the public any additional benefit commensurate with the adverse effects set out in paragraphs 6.19 to 6.34.

6.39. We do not consider, therefore, that the argument summarised in paragraph 6.36 shows that there is on balance any benefit to the public dependent on the requirement of exclusive buying.

6.40. Car manufacturers and importers also put forward a further argument. This is that exclusive dealing is necessary to ensure that parts for which there is only an infrequent demand are in fact readily available and that their prices are reasonable. It was argued that, since most of the parts in a car are slow-moving parts the prices of which do not cover the full cost of stocking and supplying them, it was necessary for car manufacturers and importers to maintain adequate business in the supply of the more profitable high-volume fast-moving parts. If franchisees were free to buy parts from other sources the franchisors would, it was claimed, lose a proportion of this profitable business and would then either be unable to afford to continue stocking slow-moving parts on the same scale and would thus fail to provide the necessary package in full, or would have to increase the prices of such parts or even the prices of their cars. However, no car manufacturer or importer whom we asked was able to give a realistic estimate of the likely loss of profitable business or of the order of magnitude of any price increases that might result.

6.41. The stocking and supply of slow-moving parts is not only a service to the customer, but in our view it is also a commercial necessity, since in the long run no manufacturer could expect to compete successfully in the sale of cars if the supply of spares were not reasonably assured for a substantial number of years. We do not think therefore that the removal of exclusivity would in practice be likely to have much adverse effect on the availability of slow-moving parts. There might be some effect on the period for which parts for cars no longer in production would be stocked by their manufacturers or importers; but we think it likely that as long as there were any significant demand for their parts other suppliers would if necessary meet the demand. We do not know what effect removal of exclusivity would have on prices of slow-moving parts or of cars. If car manufacturers and importers found it necessary to make some increase in the prices of slow-moving parts or of cars (or both) because of increased competition and consequent reduction in prices of fast-moving parts, this might involve difficult commercial considerations for them in determining how it might best be done. In our view the existing high level of competition in the supply of cars and the increased competition in the supply of parts that would result from removal of exclusivity would be sufficient safeguards for the public interest in this context.

6.42. In our view, therefore, the argument that cars must be sold as part of a package including the provision of parts and service does not carry weight in our assessment of the effects on the public interest of exclusive dealing.

#### **Consumer choice**

6.43. Car manufacturers also argued that exclusivity and their (as they saw it) consequent ability to provide the package which includes the assured provision of suitable parts had a beneficial effect on consumer choice. It had the effect of giving car owners a clear-cut option between obtaining fully tested parts of known and guaranteed quality and safety from a franchised outlet and obtaining parts from other outlets possibly at lower prices but without the same certainty as to their quality. This was an option which car owners ought to have; and to remove the obligation on franchised outlets to buy exclusively would mean that the car owner would no longer have two clear-cut alternatives. Exclusivity therefore was beneficial in this respect, and to remove it would impair consumer choice.

6.44. If the clear-cut choice is as important to car owners as it is represented to be it would not necessarily be brought to an end by the removal of insistence by franchisors on exclusivity, since some franchised dealers would see the commercial advantage to them of offering, and being known to offer, only the franchisor's approved parts to their customers.

6.45. Moreover, franchised dealers generally would be likely to be discriminating in their procurement of parts from other sources and would see it as against their own interests to supply possibly inferior parts. This would be not only because of the value to them of their franchises and a consequent need for good relations with their franchisors, but also because dealers feel the first impact of consumer complaints and would therefore see the need, as much as do their franchisors, to maintain their own reputations and the

goodwill of their customers. The possibility of their using inferior parts unwittingly cannot be eliminated; but, since to a great extent car manufacturers' checks of parts are on a sample basis only, this possibility is not eliminated even if dealers use only the car manufacturer's approved parts.

6.46. Some dealers, if they were free to do so, would no doubt use additional sources for the supply of parts; but in those circumstances any car owner who was sufficiently aware of the distinction between approved and other parts, and who thought it sufficiently important, could insist on approved parts being supplied. In fact, we think it likely that for many private car owners the choice of a dealer depends on the reputation and trustworthiness of the dealer and not on the source of parts he supplies.

6.47. For these reasons we do not think that the choice for a car owner between approved parts and parts of supposedly less certain quality is dependent upon exclusive buying by franchised dealers; and we consider that even if the choice in its present form were to disappear in the absence of exclusivity, the car owner could still protect himself against unsuitable parts.

### **Safety**

6.48. We have already considered safety in the context of car manufacturers' and importers' commercial interest in ensuring that only suitable and safe parts are supplied by their franchisees. Of more apparent relevance to the public interest, however, is the argument that it is important in the interests of road safety to ensure that potentially dangerous parts are not used. In principle this argument would apply only to safety-related parts; but car manufacturers and importers told us that in practice there was no clear dividing line between safety-related parts and other parts, and that failure or malfunction of almost any part could lead to an accident.

6.49. Car manufacturers and importers accepted that there are undoubtedly many component manufacturers in the United Kingdom and in other countries who have good reputations to preserve and who produce parts that are identical with, or equal in quality to, those supplied by car manufacturers and importers to their franchised dealers. Acceptance of this is, indeed, implied by the fact that the major United Kingdom car manufacturers themselves supply parts for other makes of car under their all-makes programmes, and often obtain from component manufacturers the parts which they supply in this way. Nevertheless, they argued that it was only by their insisting on exclusive buying that they could be certain, and that the motorist could be certain, that parts supplied through franchised outlets were safe.

6.50. If there were a need to prevent the manufacture or importation of unsafe parts or the retailing of them to the public exclusivity would not achieve this, since only about 37 per cent of the wholesale supply of parts is by suppliers who insist on exclusive buying and the balance by suppliers who do not do so. There is no evidence of any significant threat to road safety from unsafe parts being supplied through the non-franchised sector of the market.

6.51. Even if there were such a threat we do not think it would be increased if franchised dealers were free to buy parts from any source. The franchised dealers' interests in this context would be the same as those we have described in paragraph 6.45. We believe that they would generally be able to distinguish between reputable and other component manufacturers, and their need to maintain good relations with the franchisors as well as to preserve their own reputations and the goodwill of their customers would deter them from supplying unsafe parts or from taking the risk of supplying parts which might be unsafe.

### **Warranties**

6.52. Arguments put to us concerning warranties in connection with exclusivity are set out in paragraphs 5.34 to 5.41. The question of the relevance of exclusive buying requirements to, or the effect of their removal on, the operation of warranties does not appear to us to present any difficulty. We accept, first, that, since warranty work is carried out on behalf of the car manufacturer by a dealer acting for this purpose as his agent, the car manufacturer can legitimately insist that only 'genuine' parts be used; and, secondly, that a car manufacturer's warranty liability does not apply if a failed part is found not to be 'genuine' (ie the original part has already been replaced by a part not approved by the manufacturer). We accept that car manufacturers may insist on exclusive use of 'genuine' parts in warranty work; but this is different from a requirement that a franchised dealer shall not acquire or stock 'non-genuine' parts.

### **Conclusion on exclusive buying requirements of car manufacturers and importers**

6.53. In paragraph 6.34 we have stated our view that the exclusive buying requirements of car manufacturers and importers are *prima facie* against the public interest, and for the reasons we have explained in paragraphs 6.35 to 6.52 we have not found that the arguments adduced in favour of exclusivity are such as to change this view. We conclude that the complex monopoly situation which we have found to exist (paragraph 6.10) operates and may be expected to operate against the public interest and that the particular effects adverse to the public interest are those described in paragraphs 6.19 to 6.33 and summarised in paragraph 6.34.

### **Recommendation**

6.54. We accordingly considered whether we should recommend that car manufacturers and importers should be required to abandon insistence on exclusive buying. We recognise that, even in the absence of any formal requirement to buy parts exclusively from car manufacturers and importers, it is virtually certain that franchised outlets would in practice continue to buy mainly from them. Removal of the restrictions could probably not be expected to result in any sudden or dramatic change in the pattern of trade. Nevertheless component manufacturers and factors appeared to be confident that if the formal restrictions were removed they would in practice be able gradually to penetrate the franchised sector of the market to a significant extent. We therefore recommend that car manufacturers and importers should be required to exclude from their franchise agreements any clause having the effect of

requiring franchisees to buy car parts exclusively from them or from sources approved by them<sup>1</sup> and to cease enforcing any such clauses in current franchise agreements.

6.55. It would be possible, even after the abandonment of such clauses, for franchisors to ensure exclusive, or near-exclusive, buying by their franchisees by other methods. In paragraph 6.15 we have expressed the view that various practices which could have this result are not in fact being used to enforce exclusivity. However, as we have also pointed out in paragraph 6.15, if in the future it appeared that any particular car manufacturer or importer were adopting any practice which led to exclusive buying to the extent that it was materially anti-competitive, it could be made the subject of an inquiry under the Competition Act or under the appropriate provisions of the Fair Trading Act. We have also pointed out in paragraph 6.18 that certain other practices, though not relevant to this inquiry, could if necessary be dealt with in the same way.

J G Le Quesne (*Chairman*)

K D George

H L G Gibson

D G Goyder

H H Hunt

C M Miles

N E D Burton (*Secretary*)

18 February 1982

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<sup>1</sup> This recommendation is not intended to prevent car manufacturers and importers from insisting that 'genuine' parts be used by franchisees in warranty work (see paragraph 6.52).