Domestic electrical goods

A review of the Restriction on Agreements and Conduct (Specified Domestic Electrical Goods) Order 1998, and associated undertakings and assurances

June 2011

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Note: [ ]

This report is published pursuant to section 4(4) of the Enterprise Act 2002. It has been edited for publication in accordance with Part 9 of that Act. Among other things, this Part requires that the Office of Fair Trading has regard to the need for excluding from the published report, so far as is practicable, commercial information whose disclosure it thinks might significantly harm the legitimate business interests of the undertaking to which it relates.
EXECUTIVE SUMMARY

Introduction

This report presents the findings of the OFT’s review (the Remedy Review) of the Restriction on Agreements and Conduct (Specified Domestic Electrical Goods) Order 1998 (the Order) and associated undertakings (collectively the Remedies). The remedies were implemented following the 1997 reports of the Monopolies and Mergers Commission (MMC) into the supply of certain domestic electrical goods (DEGs).

The OFT has a statutory duty to keep under review the carrying out of Orders made and undertakings given under sections 56 and 88 of the Fair Trading Act 1973 (FTA73), and, from time to time, to consider whether, by reason of any change of circumstances, an Order and/or undertaking is no longer appropriate. If the OFT considers that an Order and/or undertaking is no longer appropriate, it provides such advice to the Competition Commission (CC), which takes the final decision on what should happen to the Order and/or undertakings.1

Background

Following a reference from the then Director General of Fair Trading (DGFT) in 1995, the MMC investigated the supply of certain brown and white DEGs in the UK (the Reference DEGs).

The MMC published two reports following this reference in July 1997, one on brown and the other on white goods. In these reports, the MMC identified practices by DEGs suppliers which, in accordance with the then statutory test, operated or may be expected to operate against the public interest:

1 The OFT has also conducted a review of the assurances which were given by certain parties to comply with parts of the Order. Given that the assurances were given to the then Director General of Fair Trading it is for the OFT to take the final decision on what should happen to them. Further details regarding the remedies and the assurances are included in the Annexe.
• Steps taken by some suppliers to influence the prices at which dealers\(^2\) resold DEGs, particularly how Recommended Resale Prices (RRPs) were set and used.

• Discriminatory application of selective distribution criteria, which was used to refuse supply of DEGs to warehouse clubs.

• The withholding of supply of DEGs by Combined Independents Holdings (CIH), a buying group for independent retailers, to non-members of local CIH groups.

1.5 The MMC concluded that these practices:

• caused retail prices to be higher than they otherwise would be

• reduced choice for consumers

• discouraged innovation in retailing, and

• restricted new entry into the market by retailers.

1.6 To remedy these concerns, the then Secretary of State for Trade and Industry (SoS) implemented the Order. In addition, several parties entered into undertakings. The key aspects of these remedies were to:

• Prohibit suppliers from publishing or notifying dealers of RRPs, or making agreements that restricts, directly or indirectly, the dealer’s determination of the prices at which he advertises or sells the reference DEGs.

• Prevent suppliers from refusing supply of the reference DEGs to all dealers which request them (except for certain permitted reasons).

• Prohibit CIH from refusing membership to any dealer who applied for it and meets certain conditions.\(^3\)

\(^2\) Dealers are businesses selling DEGs by wholesale or retail.
Findings

1.7 The OFT considers that, since the MMC reported, there have been numerous changes of circumstances which mean that the adverse findings identified by the MMC are unlikely to re-emerge and that the remedies are therefore no longer appropriate. These changes of circumstances are:

- **Changes in technology**: The changes in DEGs technology, particularly for brown goods, mean that several of the DEGs covered by the MMC’s report have significantly diminished in importance, such that they are largely obsolete.

- **Changes in the retailing of DEGs**: There has been a significant growth in the proportion of DEGs sales through non-specialist high street retailers and through online retailers. This has had the following effects:
  
  - These non-specialist high street retailers and online retailers often focus their offer to consumers on a value based pricing proposition and are therefore less likely to demonstrate the significant 'antipathy' to price discounting which existed when the MMC reported. They are therefore less likely to adhere to RRPs in the absence of the Order as an inability to discount would weaken their ability to acquire and retain customers.
  
  - The significance of non-specialist high street retailers and online retailers as a source of DEGs sales means that suppliers are likely to have a greater incentive to supply DEGs to those retailers. This is because they now account for a significant proportion of DEGs sales and, ultimately, a supplier’s turnover.

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3 Other parties also gave undertakings regarding aspects of their individual conduct.
- The online channel provides an effective mechanism for lower cost entry into DEGs retailing, which has facilitated entry and/or expansion for a wider range of retailers.

- **Changes in consumer behaviour**, particularly consumers taking advantage of the increased price transparency which has been created by the internet to shop around for DEGs:

- Given the significant amount of consumer research for DEGs and a greater consumer focus on the price of the DEG, a retailer which discounts from a RRP is likely to be able to reach and acquire a much greater range of customers than was the case when the MMC reported. It, therefore, would have less of an incentive to adhere to RRPs absent the Order as an inability to discount would weaken its ability to acquire and retain customers.

1.8 In addition, a further change of circumstances has been the introduction of the Competition Act 1998 (CA98) which now provides an effective mechanism to address issues of the type which are covered by the remedies in the unlikely event that they re-emerge in the future.

**Advice to the CC**

1.9 The OFT considers that there have been numerous changes of circumstances which mean that the remedies are now no longer appropriate. In this instance, the OFT is of the view that an appropriate outcome would be that:

- The Order is revoked.

- Those parties which gave undertakings should be released from them in their entirety.

**Conclusion on the assurances**

1.10 The assurances require certain parties to comply with aspects of the Order. For the same reasons as the OFT’s conclusion on the Order, it has
provisionally decided that all of the parties which gave assurances can be released from them in their entirety. However, before taking a final decision on this issue, the OFT will consider any relevant issues which arise from the CC’s consideration of the OFT’s advice regarding the Order and undertakings.
2 INTRODUCTION AND BACKGROUND

2.1 This report presents the findings of the OFT’s review of the Order and associated undertakings which followed the MMC’s investigation of the supply of DEGs in the United Kingdom which reported in 1997.

2.2 The OFT has a statutory duty to keep under review the carrying out of Orders made and undertakings given under sections 56 and 88 of the FTA73, and, from time to time, to consider whether, by reason of any change of circumstances, an Order and/or undertaking is no longer appropriate. If the OFT considers that an Order and/or undertaking is no longer appropriate, it provides such advice to the CC, which takes the final decision on what should happen to the Order and/or undertakings.\(^4\)

2.3 The OFT has also conducted a review of the assurances which were given by certain parties to comply with parts of the Order. As these assurances were given on a voluntary basis to the then DGFT, it is for the OFT to decide whether they remain appropriate or whether they should be changed or removed.

2.4 On 25 November 2010, the OFT announced the start of the remedy review, alongside wider work on aftermarkets for DEGs.\(^5\)

The MMC report 1997

2.5 In April 1995, the then DGFT referred the supply of certain white and brown DEGs to the MMC. The DEGs included in this reference were:

- **Brown Goods**: televisions, video cassette recorders (VCRs), video camcorders and hi-fi systems (the brown reference DEGs)

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\(^4\) Sections 88(4) and Section 88(5) of the FTA73, which continues to apply in respect of the Order and undertakings by virtue of schedule 24 of the Enterprise Act 2002. With respect to removing an Order or undertaking, the statutory wording is to revoke an Order and to release a party from an undertaking.

• **White Goods**: washing machines, tumble dryers, dishwashers and cold food storage equipment (the white reference DEGs).\(^6\)

2.6 The MMC published two reports following this reference in July 1997. One report related to the supply of the brown reference DEGs and the other to the supply of the white reference DEGs.\(^7\)

**Findings on prices**

2.7 The MMC found that there were several practices undertaken by some suppliers to influence the prices charged by dealers of the reference DEGs. These included:

- the setting of RRPs
- reducing or threatening to reduce discounts to dealers who advertised or displayed prices below the RRPs
- making support for dealer advertising costs conditional upon the advertisement not quoting prices below those approved by the supplier
- providing point-of-sale material that included the display of RRPs.\(^8\)

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\(^6\) A definition of what is meant by each of the reference DEGs is included in article 1 of the Order.

\(^7\) *Domestic Electrical Goods I: A report on the supply in the UK of televisions, video cassette recorders, hi-fi systems and camcorders* and *Domestic Electrical Goods II: A report on the supply in the UK of washing machines, tumble dryers, dishwashers and cold food storage equipment*. Reference to these reports in footnotes in the remainder of this document are denoted by MMC (1997a) for the MMC’s report in relation to the reference brown DEGs and MMC (1997b) for the MMC’s report in relation to the reference white DEGs.

\(^8\) MMC (1997a), paragraph 1.20 and MMC (1997b), paragraph 1.19.
Findings on refusal to supply

2.8 The MMC also found that almost all suppliers made use of selective distribution systems to select dealers for supply, with a common criterion being the provision by retailers of pre- and post-sales service. These criteria were often used as grounds for refusing to supply warehouse clubs, which were viewed by suppliers as discounters.9

2.9 Furthermore, the MMC also found that CIH, a buying group for independent retailers, would only supply DEGs to those retailers which were members of its local groups. These local groups would only admit prospective members who could submit audited accounts for a period of three years. Some local groups also required new members to be acceptable to existing members.10

MMC findings on the public interest11

2.10 The MMC concluded that the following practices operated or may be expected to operate against the public interest:

- Actions by suppliers to influence the prices at which resellers sell the reference DEGs. In particular, the MMC concluded that the use of RRPds had the effect of influencing the transaction prices of retailers. This influence resulted from the strength of the relationship between dealers and suppliers. Aspects of this relationship included a shared antipathy to unrestrained price competition, which was associated with an emphasis on non-price offers.

- The discriminatory application of selective distribution criteria, which the MMC concluded was used to limit supply to warehouse clubs.

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9 MMC (1997a), paragraphs 1.23 to 1.24, and MMC (1997b), paragraphs 1.22 to 1.23.

10 MMC (1997a) and MMC (1997b), both at paragraph 1.13. MMC (1997a), paragraph 1.24 and MMC (1997b), paragraph 1.23.

11 MMC (1997a), paragraphs 1.18 to 1.26, and MMC (1997b), paragraphs 1.17 to 1.25.
• The withholding of supply of DEGs by CIH to non-members of local CIH groups, which prevented some retailers from taking advantage of CIH’s purchasing power.

2.11 The MMC concluded that these adverse effects:

• caused retail prices to be higher than they otherwise would be

• reduced the choice for consumers

• discouraged innovation in retailing, and

• restricted new entry into the market by retailers.

2.12 The MMC also found that certain actions undertaken by individual suppliers and dealers operated or may be expected to operate against the public interest.

**MMC recommendations and the remedies**

2.13 To address these adverse findings the MMC recommended that:

• suppliers be prohibited from publishing or notifying dealers of RRPs, or otherwise taking actions to influence the pricing decisions of dealers

• the discriminatory application of selective distribution criteria be prohibited and that supply be granted to all creditworthy warehouse clubs

• CIH local groups should be prohibited from refusing membership to any retailer who applies for it and could demonstrate the ability to pay for any reference DEGs that he may order.12

2.14 The SoS implemented most of these recommendations through the Order, which took effect on 1 September 1998. The Order prohibited:

12 MMC (1997a), paragraph 1.27 to 1.35, and MMC (1997b), paragraphs 1.26 to 1.32.
• Suppliers from publishing or otherwise notifying dealers of recommended or suggested prices.

• Suppliers entering agreements that would act to restrict, directly or indirectly, a dealer’s ability to determine its retail prices.

• Suppliers from withholding the reference DEGs from any requesting dealer, except in certain specified circumstances.

2.15 The remaining recommendations were implemented through undertakings, notably those undertakings given by CIH which restricted its ability to refuse membership to retailers which applied for it and met certain criteria. In addition, GDA, Dixons and Empire also gave undertakings to address the MMC’s specific findings as they related to those parties.

2.16 Following the implementation of the remedies, nine parties gave voluntary assurances to the DGFT that they would comply with article 2 of the Order and would therefore not make recommendations to dealers regarding the retail prices to be charged for DEGs.13

Approach

2.17 During this remedy review, the OFT has engaged with parties active across the DEGs sector, including manufacturers, retailers and trade associations. The OFT has also considered information from independent market research providers, including GfK.14

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13 Further information regarding the Order, undertakings and assurances can be found in the Annexe.

14 GfK Retail and Technology UK Limited (GfK) information was provided by various parties during the remedy review. The information was already pre-approved by GfK and was channel level information only. GfK has asked the OFT to emphasise that when the information was provided to parties for use in the remedy review, no individual retailer numbers were provided from one retailer to another; this was done on its confidential level between individual retailer and GfK. GfK asked the OFT to emphasise that any opinion, comments on conclusions drawn from the remedy review are not that of GfK and as a fact based market research company it
2.18 Where possible, the OFT’s analysis is based upon information relating specifically to the reference DEGs, which represent the focus of this review.\textsuperscript{15} However, the reference DEGs do not represent a recognised sub-group within the DEGs sector. This has meant that the OFT has often had to use information which relates to a wider group of DEGs (or the retailing of all DEGs which is referred to in this report as the wider DEGs retailing market).

2.19 This review has also focused upon the retailing of DEGs. This is because the MMC’s specific adverse effects related primarily to restrictions in competition for the retailing of DEGs. However, in order to understand the overall context of DEGs retailing, the OFT has also considered, where appropriate, other relevant aspects of the DEGs sector including the manufacturing of DEGs and the behaviour of consumers.

Structure of this report

2.20 The remainder of this report is structured as follows:

- Chapter 3 considers relevant developments in the markets for the supply of the reference DEGs since the MMC reported.

- Chapter 4 considers relevant developments in the legal framework since the MMC reported.

- Chapter 5 sets out the OFT’s conclusions and its advice to the CC.

- Further information regarding the remedies and assurances is in the Annexe.

remains impartial at all times www.gfkrt.com/uk. Throughout this report, the 2010 data provided by GfK is generally for the twelve months to November 2010.

\textsuperscript{15} The OFT, however, has considered, where appropriate, other DEGs products to ensure an understanding of the context in which the reference DEGs are sold.
3 DEVELOPMENTS IN THE SUPPLY OF DEGS

Introduction

3.1 During the remedy review, parties have highlighted that the supply of DEGs has developed significantly since the MMC reported. This chapter does not consider all of those developments, but only those which the OFT considers are of most direct relevance to the continued appropriateness of the remedies.

3.2 The OFT considers that there have been three principal changes of circumstances in the market since the MMC reported, which impact on the appropriateness of the remedies. These are:

- **Changes in technology**, particularly in relation to the brown reference DEGs, some of which are now largely obsolete.

- **Changes in the retailing of DEGs**, particularly the significant growth of the importance of non-specialist high street retailers and online retailers.

- **Changes in consumer behaviour**, particularly the increased shopping around for DEGs, which has been facilitated by the internet, and the increased importance of price as a key factor for a consumer in deciding which DEG to purchase.

3.3 The OFT has also considered, more generally, the extent to which these changes of circumstances have affected competition in DEGs retailing since the MMC reported.

Changes in technology

3.4 There have been significant technological developments in DEGs since the MMC reported, for example the development of high definition television and improvements in the energy efficiency of white goods. Although technological developments have occurred across the reference DEGs, they appear to have had the greatest impact on certain reference brown
goods, particularly video based technology and hi-fi systems where product innovation has been considerable.

**Video cassette based technology**

3.5 When the MMC reported, sales of DEGs using analogue, video cassette technology, such as VCRs and video camcorders, were highly significant. Since then, that technology has been substantially superseded both by digital technology and, in the case of VCRs, by DVD players and Blu-Ray devices.

3.6 In relation to VCRs, UK sales values of VCRs have significantly declined from £611m in 1995\(^{16}\) to an estimated value of less than £100m by 2007.\(^{17}\) The OFT has received evidence which confirms that this trend has continued. For example, one retailer informed the OFT that VCRs were 'virtually redundant'. Another has provided evidence (Figure 3.1) which demonstrates the share of sales of VCRs as a proportion of the wider video market to virtually nil in 2010, with other products taking their place. The more recent decline of DVD technology, which largely replaced VCRs, illustrates the speed of technological change in this sub-sector of the DEGs market.

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\(^{16}\) MMC (1997a), table 1.1.

\(^{17}\) Keynote (2008), *Household Appliances (Brown Goods)*, page 12.
3.7 The value of the UK market for video based camcorders was £204m in 1995. At that time, digital camcorders were 'much more expensive' than the video based product.

3.8 By 2004, however, evidence seen by the OFT indicates that digital camcorders accounted for over 90 per cent of the sales value of the market, with sales of the tape-based analogue product considered to be 'residual'. More recent evidence seems to confirm this, with a large DEGs retailer informing the OFT that no tape based camcorders were sold in 2010.

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18 MMC (1997a), table 1.1.

19 MMC (1997a), paragraph 5.11.

20 Mintel (2005), Video Cameras, pages 7 and 37.
Hi-fis

3.9 The MMC’s terms of reference defined hi-fi systems as fixed stand-alone CD and cassette-playing audio systems, which were the available products at the time. Since 1997 there has been significant development in audio playback technology, with the emergence of a wider range of products, including computer based and portable products, such as MP3 players and docking stations.

3.10 By 2007, evidence seen by the OFT indicates that sales of midi and mini systems had declined significantly.\textsuperscript{21} More recent evidence provided to the OFT indicated that UK sales of MP3 player speaker docks in 2010 were 1.9m units compared with 1.8m units for home audio systems.\textsuperscript{22} This indicates that although hi-fi systems are still apparently purchased by many consumers, a greater range of audio play back devices are now available. All of these new products, except for hi-fi systems as defined in the Order, are excluded from the scope of the remedies.

Conclusion on technological developments

3.11 The significant technological developments since the MMC reported have led several of the reference DEGs products, primarily those using video based technology, to become largely obsolete. Although this is not yet the case for hi-fi systems, there is a greater diversity of products available for audio playback, most of which are not included within the scope of the remedies. With respect to those products not included within the scope of the remedies, it is worth noting that the OFT has not received any significant concerns that the practices about which the MMC came to adverse findings have emerged in relation to those products.

\textsuperscript{21} Mintel (2007), \textit{Audio Equipment}, page 30.

\textsuperscript{22} GfK information.
3.12 The technological developments across the product range as set out above have changed the circumstances considerably since the MMC’s report, indicating that the scope of the Order is no longer appropriate.

Developments in the retailing of DEGs

3.13 There have also been significant developments in the retailing of the reference DEGs since the MMC reported. This section considers those developments, focusing particularly upon the relative growth of non-specialist high street retailers of DEGs, at the expense of specialist high street retailers, and the increased role of internet retailing.

3.14 The DEGs retailing market is generally subdivided into specialist and non-specialist retailers:

- **Specialist retailers** are those retailers for whom DEGs retailing contributes all or a very significant proportion of total turnover, such as Dixons or Comet.

- **Non-specialist retailers** are those retailers for whom DEGs retailing contributes only a relatively small part of their turnover, such as multiple grocers, catalogue retailers and department stores.

3.15 The MMC identified that, in 1995, specialist retailers were by far the biggest retail channel for the sale of DEGs, accounting for some 80 per cent of the reference DEGs sold. Since the MMC reported, the share of the non-specialist retailers of DEGs has grown. This is shown in table 3.2 which gives retail market shares for the reference DEGs in 1995, and in 2010.²³

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²³ GfK data. This information includes information in relation to DVD players and electric cookers which the OFT included within the scope of the remedy review as comparator products. The OFT has no reason to believe that the retailing of these products differs in any significant way from the retailing of the reference DEGs.
Table 3.2: Market shares of retailer types of the reference DEGs

<table>
<thead>
<tr>
<th>Retailer types</th>
<th>Market share for brown reference goods (per cent)</th>
<th>Market share for white reference goods (per cent)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1995</td>
<td>2010</td>
</tr>
<tr>
<td>Electrical chains</td>
<td>56.8</td>
<td>30.8</td>
</tr>
<tr>
<td>Independents(^{25})</td>
<td>21.2</td>
<td>27.1</td>
</tr>
<tr>
<td>Mass merchandisers(^{26})</td>
<td>12.3</td>
<td>33.5</td>
</tr>
<tr>
<td>Mail order and web specialists</td>
<td>9.7</td>
<td>8.6</td>
</tr>
<tr>
<td>Furniture / DIY</td>
<td>n/a</td>
<td>n/a</td>
</tr>
</tbody>
</table>

Source: Information provided by Comet, based upon MMC (1997 a and b), table 7.8 and GfK data

3.16 Table 3.2 shows that the non-specialists' relative share of the retail market for brown reference DEGs has almost doubled in that time, while their share of the retail market for the white reference goods has increased by almost 80 per cent. This significant expansion has come at the expense of the specialist retailers, particularly the electrical chains.

\(^{24}\) The OFT notes that the definition of the retailer types may not be directly comparable over time. However, the OFT has not received evidence which is directly comparable and notes that this evidence is consistent with other sources which shows significant growth in the significance of the non-specialist retailers (for example, information produced by Verdict – see for example, Verdict (2011), UK electricals 2011, page 61).

\(^{25}\) Amongst others, this includes retailers which are members of buying groups. In addition to Euronics (operated by CIH) which is a long standing buying group, the Sirius buying group, which was formed in April 2001, also now facilitates the purchase of the reference white goods.

\(^{26}\) Defined as supermarkets, department stores and mixed goods retailers such as Argos.
such as Dixons and Comet, whose proportionate share of the retail market has decreased by over 45 per cent for brown goods and over 34 per cent for white goods.

3.17 The next section considers in more detail the specific developments which have occurred in the DEGs retailing market, including:

- The entry and expansion of non-specialist high street retailers.
- The growth of online retailing.
- The entry of Best Buy.

**The entry and expansion of non-specialist high street retailers**

3.18 Since the MMC reported the importance of the non-specialist high street retailers (referred to generally as mass merchandisers) as a source of DEGs has grown considerably. This is shown in table 3.3.

**Table 3.3: The market shares of the major non-specialist high street retailers across the wider DEGs retailing market**

<table>
<thead>
<tr>
<th>Retailer</th>
<th>Market share of DEGs retailing 1997 (per cent)</th>
<th>Market share of DEGs retailing 2009 (per cent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Argos</td>
<td>3.6</td>
<td>11.2</td>
</tr>
<tr>
<td>John Lewis</td>
<td>2.2</td>
<td>4.0</td>
</tr>
<tr>
<td>Grocers</td>
<td>1.6</td>
<td>8.8</td>
</tr>
</tbody>
</table>

Source: Based upon Verdict data

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27 This section focuses upon those retailers with a significant high street presence. However, the OFT fully recognises that these retailers also sell through the internet.
3.19 A major source of this growth has been the entry and expansion of the multiple grocers. Their increase has been facilitated by the development of new format large stores, which stock a wide range of non-food products, including DEGs. Furthermore, most grocery multiples have also taken advantage of the internet to sell DEGs.

3.20 Parties which provided evidence to the OFT referred to the relative strengths of the grocery retailers as retailers of DEGs. Most particularly, they benefit from having sophisticated buying operations, established retail brands, access to a wide customer base and other profit streams to support their expansion in the DEGs market. These advantages are also enjoyed, at least to some extent, by other non-specialist high street retailers, such as Argos and John Lewis.

The growth of online retailing

3.21 Since the MMC reported, DEGs retailing over the internet has emerged and grown rapidly. This is demonstrated by evidence provided to the OFT that, for the reference DEGs, internet sales represented 17.5 per cent of the reference markets in 2010, including 16.4 per cent of the reference brown goods sales and 19.6 per cent of the reference white goods, whereas no reference DEGs were sold online in 1995.28

3.22 This expansion has had a significant impact on DEGs retailing, both by providing a mechanism for bricks and mortar retailers (both specialist and non-specialist) more readily to expand the range of DEGs which they offer, but also through facilitating entry by online only retailers, such as Amazon, eBay, Play.com and Dabs, and a wide range of smaller retailers. Indeed the OFT notes that retailers which only sell online accounted for an estimated 6.5 per cent of the wider DEGs retailing market in 2010, up from 2.7 per cent in 2006.29

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28 This information may understate DEGs sales through the internet as sales made to customers who buy on-line and collect in-store are recorded as store sales rather than internet sales

Several parties during the remedy review submitted that the internet has reduced entry barriers for DEGs retailing, as retailers no longer have to invest in establishing costly physical retail outlets and can benefit from lower overheads. Indeed, one major retailer, has noted that a 'huge surge' of internet retailers have entered the market since the MMC reported, creating both 'retailing giants' (such as Amazon) and opportunities for new entrant small independent retailers.

**Characteristics of non-specialist high street retailers and online retailers**

3.24 The growth of non–specialist high street retailers and online retailers has had a significant impact on the DEGs retailing sector. This is particularly because most of these retailers have developed a value based proposition whereby their competitive offer is strongly focused upon providing DEGs at highly competitive retail prices.

3.25 The more price based focus of the non-specialist retailers is consistent with information the OFT has seen regarding how those retailers are perceived by consumers. This evidence (displayed in table 3.4) shows that, with the exception of John Lewis, a larger proportion of consumers shopping in non-specialist retailers (indicated by NS in table 3.4), refer to price as a factor driving loyalty to a particular retailer, than is the case for specialist retailers.
Table 3.4: Proportion of surveyed main users of particular retailers referring to particular factors as a reason for their loyalty to that retailer, 2011

<table>
<thead>
<tr>
<th>Retailer</th>
<th>Price</th>
<th>Range</th>
<th>Service</th>
<th>Quality</th>
</tr>
</thead>
<tbody>
<tr>
<td>eBay (NS)</td>
<td>73.9</td>
<td>27.6</td>
<td>13.5</td>
<td>1.9</td>
</tr>
<tr>
<td>Amazon (NS)</td>
<td>59.1</td>
<td>32.6</td>
<td>28.0</td>
<td>5.0</td>
</tr>
<tr>
<td>Argos (NS)</td>
<td>58.4</td>
<td>43.2</td>
<td>15.3</td>
<td>6.2</td>
</tr>
<tr>
<td>Tesco (NS)</td>
<td>56.1</td>
<td>39.3</td>
<td>5.1</td>
<td>6.3</td>
</tr>
<tr>
<td>Comet</td>
<td>52.6</td>
<td>43.5</td>
<td>17.1</td>
<td>7.1</td>
</tr>
<tr>
<td>Currys</td>
<td>48.9</td>
<td>50.6</td>
<td>15.0</td>
<td>6.3</td>
</tr>
<tr>
<td>John Lewis (NS)</td>
<td>37.6</td>
<td>31.3</td>
<td>65.0</td>
<td>36.3</td>
</tr>
</tbody>
</table>


3.26 Table 3.4 also indicates that, from a consumer’s perspective, there appears to be significant differentiation between retailers, with different retailers apparently offering different price, range, service and quality propositions. This diversity is substantially different from the situation when the MMC reported.

3.27 Specialist retailers have submitted to the OFT that they have responded to the expansion of the non-specialists by ‘raising their game’, including differentiating their offer and by ensuring that their prices are sufficiently competitive to compete with the non-specialist high street retailers and online retailers.
The entry by Best Buy

3.28 There has also been a significant recent development in relation to specialist DEGs retailing. This is the entry into the UK DEGs retailing market of Best Buy, one of the world’s largest consumer electronics retailers, which opened its first store in the United Kingdom in late 2009. As of June 2011 it had 10 physical retail outlets, as well as an online business. It has indicated that it intends to open further physical retail outlets during the course of 2011.

Conclusion on developments in the retailing market

3.29 Since the MMC reported, there has been a transformation in the market for the retailing of DEGs. In addition to new entry by Best Buy, a large specialist retailer, the entry and expansion of the non-specialist high street retailers and online retailers has significantly changed the dynamic of the market, leading to greater diversity and an enhanced focus on price competition. Moreover, the internet has established an entirely new retailing channel which did not exist when the MMC reported, which appears to have facilitated entry and expansion.

3.30 These changes have had the following effect on the appropriateness of the remedies:

- These non-specialist high street retailers and online retailers often focus their offer to consumers on a value based pricing proposition and are therefore less likely to demonstrate the significant 'antipathy' to price discounting which existed when the MMC reported. They are therefore less likely to adhere to RRP in the absence of the Order as an inability to discount would weaken their ability to acquire and retain customers.

- The significance of non-specialist high street retailers and online retailers as a source of DEGs sales means that suppliers are likely to have a greater incentive to supply DEGs to those retailers. This is because they now account for a significant proportion of DEGs sales and, ultimately, the supplier’s turnover.
• The online channel provides an effective mechanism for lower cost entry into DEGs retailing, which has facilitated entry and/or expansion for a wider range of retailers.

Changes in consumer behaviour

3.31 There also appears to have been some significant changes in consumer behaviour since the MMC reported, particularly in:

• The use of the internet to facilitate consumers shopping around for DEGs.

• The factors consumers take into account when deciding which DEGs to purchase.

Shopping around by consumers

3.32 When the MMC reported, it identified that there were restrictions on the ability of consumers to shop around for DEGs which meant that consumers 'did not engage in substantial search activity'.30 In particular, it found that:

• Relatively few consumers engaged in significant research prior to purchasing DEGs. For example, only 10 per cent of consumers undertook research through media resources such as specialist magazines or Which? Indeed, that information would often be out of date by the time that the consumer purchased the DEG.31

• There were difficulties for consumers wishing systematically to search for DEGs. Amongst other things, these difficulties included the tendency of retailers to sell a distinct range of products to that offered

30 MMC (1997a) and MMC (1997b), both at paragraph 1.7.

31 See, for example, MMC (1997a), paragraph 2.76.
by their competitors, which ultimately made it difficult for consumers to make comparisons between DEGs retailers.  

3.33 Since the MMC reported, there has been a significant change in the accessibility of pre-purchase information for consumers. Most significantly, the internet has substantially increased the transparency of pricing in DEGs retailing and provides a more convenient means for consumers to compare the offers of various retailers without the need to visit multiple physical outlets. It is worth noting that expansion in the availability of information online is a feature of retail markets generally and therefore does not arise from the Order.

3.34 All significant retailers of DEGs now have websites which include information on the prices at which they sell particular DEGs, as well as details on product specifications. In addition, there are a large number of independent websites which provide consumers with information, both on the pricing and features of DEGs. These include:

- Online review sites providing reviews of new products (such as Trustedreviews.com and appliancereviews.co.uk).
- Specialist on-line technology magazines (such as WhatHifi.com).
- Online shopping services and price comparison sites, which allow consumers readily to compare the prices of the same DEGs model at different retailers (such as Google Shopping, Shopzilla, Kelkoo and PriceRunner). The OFT understands that these websites are often updated in real time, giving consumers the latest product and price information.
- Specialist consumer online magazines (for example, Which? provides information on best buys and offers price comparison tools).

32 See, for example, MMC (1997a), paragraph 2.73.
3.35 The evidence indicates that consumers are actively using these sources to engage in significantly greater search activity than was the case when the MMC reported. For example:

- One large retailer of DEGs provided research that around 80 per cent of shoppers look at the internet when researching which DEGs to buy, and the majority change their mind about the brand they purchase after researching online.

- Mintel consumer research in 2010 and 2011:
  - showed that around 23 per cent of surveyed consumers used price comparison websites to shop for DEGs.\(^{33}\)
  - 53 per cent used the internet to compare prices/features then bought online. 53 per cent also used the internet to compare prices/features then bought in store. Only four per cent of the consumers surveyed did not do product research and/or price comparisons on the internet.\(^{34}\)

- Even as early as 2003, the CC’s report on Extended Warranties noted that the evidence it had seen from different surveys supported the view that consumers shop around for DEGs.\(^{35}\)

3.36 The OFT notes the MMC’s concerns that retailers stocking different models of DEGs restricted consumers’ ability to shop around. Indeed, the

\(^{33}\)Mintel (2011), *Researching Purchases Online*, page 61. 23 per cent of consumers surveyed used price comparison sites for consumer electronics and 22 per cent used price comparison sites for household appliances.

\(^{34}\)Mintel (2011), *Digital Trends Spring – UK*. Referred to at page 27 of Mintel (2011), *Extended Warranties*. This figure does not sum to 100 as consumers were able to provide multiple responses.

OFT has seen evidence that, with the increasing range of non-specialist retailers, there has been an increase in the number of own brand DEGs which are therefore not available from other retailers. The OFT has also received some representations that DEGs suppliers are increasingly offering exclusivity on certain models to a particular retailer, which could restrict consumers' ability to shop around.

3.37 However, the OFT has also seen evidence from one of the UK’s largest manufacturers of white goods that almost all of its top selling models are available in at least two of the major DEGs retailers, with the large majority of its top selling products being available in at least three DEGs retailers. This is consistent with OFT information showing that the large majority of the top selling televisions and home appliances sold at Dixons.co.uk are also available at other retailers.

3.38 The internet has impacted on the ability of consumers to shop around, notwithstanding retailers stocking different models. Even where a model is exclusive to a particular retailer, several websites (for example, pricerunner.co.uk, Amazon.co.uk, Dixons.co.uk) also include sections entitled 'items which other consumers who looked at this product also looked at' or 'similar products'. This means that, even if a DEGs retailer stocked an exclusive model, consumers are more readily able to compare that exclusive model with DEGs of similar functionality which may be available at other retailers.

3.39 Therefore, whilst the OFT recognises that exclusive models may increase search costs and have some impact on the ability of consumers to shop around, the OFT notes that the most popular models seem to be available from a range of different retailers. In addition, the internet may enable

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36 Such as Technika, which is a Tesco own brand for electrical products.

37 Based upon Dixons ‘top sellers’ section on the homepage of Dixons.co.uk. The OFT checked which of these models were available from other retailers. As of 1 June 2011, five out of the six top selling appliance models were available from other retailers and four out of the six available television models were available from other retailers.
consumers to more readily compare similar models, even where exclusive models are stocked.

Factors consumers take into account when purchasing DEGs

3.40 The MMC cited the reputation of the supplier as a highly significant factor that influenced consumers’ purchasing decisions for DEGs when it reported. One of the strongest statements in support of this was from a Sony survey, which stated that 81 per cent of respondents rated brand reputation as being of high importance in their purchasing decision.38

3.41 The OFT notes that there are significant difficulties regarding the comparability of the evidence received during the remedy review with that provided to the MMC.39 However, the OFT has seen evidence that price is now a more significant factor than brand in the consumer’s decision making process.

• The CC, in its extended warranties report in 2003 concluded that ‘price is the primary determinant for DEGs choice’. In particular, the CC cited a survey showing that price was given as the main reason for selection of a DEG by 23 per cent of respondents, whilst brand was referred to by only 10 per cent of respondents.40

• Mintel research indicated that, in 2009, only eight per cent of television buyers were loyal to a single brand. In addition, when purchasing televisions, consumers were most concerned with price (with price being considered important by 86 per cent of those

38 See, for example, MMC (1997a), paragraph 7.21.

39 For example, different surveys of consumers use different samples, ask different questions and use different methodologies.

40 CC (2003), paragraph 9.18.
surveyed), whereas brand was referred to by 27 per cent of respondents.41

- Although Mintel research on white goods showed that 'sticking to a well known brand' was cited by 50 per cent of consumers as a factor in their purchasing decision, only 12 per cent are loyal to a single brand.42 In addition, a survey conducted by GfK, on an annual basis since 2006, showed that the two most significant factors cited for a consumers' choice of brand for white goods were generally 'price compared to other brands' and 'offers good value for money', which collectively were referred to by 34 per cent of consumers in 2010, which is similar to results for previous years. This contrasts with reputation of the supplier which was only referred to by 12 per cent of respondents.

- Table 3.4 demonstrates that, across a wide range of retailers, price was the main driver of loyalty which was mentioned by consumers.

3.42 Furthermore, the OFT notes that Beko, a manufacturer of a wide range of 'value' white goods,43 has experienced very significant increases in its market share in recent years, such that it is was the largest UK supplier of freezers and the second largest UK supplier of washing machines and fridge freezers in 2009.44 This would suggest that, at least for many consumers, price is a significant factor in their purchasing decision. Finally, the significance of price in consumers' purchasing decisions is also reflected in the importance of promotional activity. A major non-specialist retailer has, for example, submitted that 'promotions are one of the key drivers of sales'.


43 Mintel (2010), *White Goods*, page 61. Consumer research showed that Beko 'eclipses' the other manufacturers in terms of the extent to which it is perceived as value by consumers.

44 Mintel (2010), *White Goods*, pages 41 to 44.
Conclusions on consumer behaviour

3.43 The OFT's analysis indicates that the internet has made it significantly easier for consumers to compare competing offers than was the case when the MMC reported. In addition, there is evidence that consumers are using these information sources to engage in much greater pre-purchase searching than was the case when the MMC reported. The OFT's analysis also suggests that, particularly for brown goods, prices appear to be a more significant factor in consumers' decisions as to which DEGs to purchase.

3.44 Given the significant amount of consumer research for DEGs and the greater consumer focus on the price of the DEG, a retailer which discounts from an RRP is likely to be able to reach and acquire a much greater range of customers than was the case when the MMC reported. It, therefore, would have less of an incentive to adhere to RRPs absent the Order as an inability to discount would weaken its ability to acquire and retain customers.

Competition in DEGs retailing

3.45 When the MMC reported, it concluded that:

'If the market were as competitive as has been claimed, it could be argued that any steps taken by suppliers to influence retail prices and the withholding of supply from dealers ... would have little effect on the level of retail prices or of consumer choice.'\textsuperscript{45}

3.46 Every party which has provided a view on competition for DEGs to the OFT during the remedy review has submitted that DEGs retailing has become more competitive since the MMC reported. This was also the conclusion of the CC in \textit{Extended Warranties} which found that market concentration was relatively low and 'consistent with a competitive

\textsuperscript{45} See for example MMC (1997a), paragraph 2.66.
market structure in DEGs retailing’. Moreover, it considered that there was 'vigorous price competition' in the DEGs retail market.46

3.47 The evidence which the OFT has seen during this review, and which is generally described above, supports these comments. In particular:

• The DEGs retailing market is relatively unconcentrated, with the largest ten retailers combined accounting for just over 47 per cent of the wider DEGs retailing market in 2009.47

• There is evidence of significantly greater diversity in the DEGs retailing market than was the case when the MMC reported, with a wider variety of retailers competing for business.

• There is evidence of competition between retailers, with evidence of significant changes in market share over time, including the significant declines in the market share of the major electrical chains.

• There is evidence of substantial new entry into the market, some of which appears to have been facilitated by the internet.

3.48 The OFT notes that this is consistent with indicators of the effectiveness of competition which it has seen during the remedy review:

• There has been a significant decline in the retail prices of DEGs over time, with retail prices in the wider DEGs market declining, in nominal terms, by an average of over eight per cent each year between 2000 and 2009.48 The OFT recognises, however, that this is likely to reflect efficiencies in manufacturing as well as competition in DEGs retailing.

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46 CC (2003), paragraph 13.117 and CC announcement, Warranties opened up to greater competition, 18 December 2003.


48 Verdict (2011), UK electricals 2011, page 36. This excludes information for 2010 and 2011 which are based upon estimates. The OFT notes that the information for these years also shows significant price declines.
• Retailers appear to be more actively benchmarking their retail prices against their competitors. For example, one retailer of electrical goods has noted that whereas in 1997 prices were established monthly, they are now monitored more regularly and adjusted accordingly (including on a daily basis).

• There has been significant innovation in retailing, with a wide range of different retailing propositions now available to consumers.

• There is evidence that operating margins for retailers are relatively low. For example, one DEGs retailer has submitted that operating margins across the sector are approximately two to four per cent (in comparison to, for example, the operating margins of the multiple grocers which, in 2006/7, averaged 4.5 per cent).  

3.49 This significantly increased level of competition may suggest that supplier actions to restrict retail competition would now be less likely to have a substantial effect on the level of retail prices or of consumer choice.

The impact of the current economic climate

3.50 The OFT has also considered whether the changes referred to above are likely to persist into the future. In particular it has considered whether the current economic climate has led to a temporary enhanced focus by consumers on obtaining the best possible price for the DEGs which they purchase, which may have contributed to the significant expansion of non-specialist high street retailers and online retailers with a value based proposition.

3.51 However, the CC’s Extended Warranties investigation in 2003 (referred to at paragraph 3.41), suggests that price was a significant factor in consumers’ purchasing decisions before the commencement of the recession.

49 CC (2008), The supply of Groceries in the UK market investigation, Figure 3.3.
3.52 The OFT also notes that the growth of DEGs retailing through non-specialist retailers is a longer term trend. According to Verdict data, for example, non-specialist retailers had already grown strongly by 2007, when they accounted for almost 35 per cent of the wider DEGs retail market. The OFT is also aware that several non-specialist retailers have announced plans to expand their DEGs business in the future, suggesting that non-specialist retailers will continue to play a significant and expanding role in the retailing of DEGs.\textsuperscript{50}

\textsuperscript{50} For example, Tesco’s annual report (2011) refers to Tesco’s plan to ‘continue to pursue growth in all parts of the business – in the UK, internationally, in services and across general merchandise, clothing and electricals’.
4 DEVELOPMENTS IN THE LAW

4.1 The OFT has also considered the impact of changes in competition law since the remedies were first implemented in 1998, including the:

- implementation of the CA98 in 2000, which replaced the Resale Prices Act 1976 (the RPA), and
- the adoption, from 2000, of an EU block exemption for vertical agreements (VABER).

The RPA and the CA98

4.2 At the time of the MMC report, the RPA was the primary legislative mechanism to deal with suppliers attempting to impose fixed or minimum price levels for dealers to observe when reselling products, otherwise known as resale price maintenance (RPM).\textsuperscript{51} Although the MMC recognised that some of the practices about which it came to adverse findings were tantamount to RPM, it considered that the practical shortcomings of the RPA meant that a specific remedy would be required.\textsuperscript{52}

4.3 The RPA was repealed when the CA98 was implemented. The CA98 includes two primary elements:

- the Chapter I prohibition, which prohibits anti-competitive agreements between undertakings, and
- the Chapter II prohibition, which prohibits abuse of a dominant position by an undertaking.

\textsuperscript{51} A summary of the provisions of the RPA can be found at MMC (1997 a and b), both at Appendix 6.2.

\textsuperscript{52} MMC (1997a) paragraph 1.29 and MMC (1997b), paragraph 1.28.
4.4 Since 1 May 2004, following the implementation of the Modernisation Regulation,\(^{53}\) the OFT has been empowered to fully apply Articles 101 and 102 of the Treaty on the Functioning of the European Union (‘TFEU’). These articles are identical to the Chapter I and II prohibitions, except they are applicable to behaviour or conduct which may affect trade between European Union member states, as opposed to the CA98 which applies to behaviour or conduct that affects trade only within the UK.\(^{54}\)

4.5 The OFT has extensive powers of investigation when investigating suspected breaches of the CA98, including the power to require the production of specified information or to enter premises with or without a warrant.\(^{55}\)

4.6 There are potentially very serious consequences for parties which engage in behaviour or conduct which infringe the prohibitions in CA98. These are:

- Financial penalties of up to 10 per cent of total worldwide turnover.
- The possible disqualification of directors of an undertaking for up to 15 years.
- The possibility of third party actions against undertakings.\(^{56}\)

4.7 Agreements which infringe the Chapter I prohibition will also be void and unenforceable.

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\(^{53}\) EC Regulation 1/2003.

\(^{54}\) This chapter focuses upon the effect of the CA98. However, where an agreement affects trade between member states, action under Articles 101 or 102 of TFEU would be relevant.

\(^{55}\) Sections 26 to 28 of the CA98.

Vertical agreements and exemption

4.8 Agreements between parties at different levels of the supply chain are known as vertical agreements. These can contravene the Chapter I prohibition where such agreements have as their object or effect an appreciable restriction, prevention or distortion of competition. However, where an agreement meets certain criteria (the exemption criteria), in that it is indispensable to the attainment of certain demonstrated efficiencies, it can be exempted from the Chapter I prohibition.57

4.9 The VABER,58 creates a presumption of legality for vertical agreements which meet certain criteria, including market share thresholds, provided they do not contain certain 'hard core' restrictions of competition.

4.10 This is on the basis that vertical agreements may provide substantial scope for efficiencies regarding the production or distribution of goods and that most vertical restraints only give rise to competition concerns where there is some degree of market power at the level of trade of the supplier or the buyer or at both levels. An agreement which is covered by the VABER, but which only affects trade within the UK, is exempt from the Chapter I prohibition by virtue of a parallel exemption under section 10 CA98. The European Commission has also produced Guidelines on Vertical Restraints59 ('Vertical Guidelines') to assist parties to self-assess their distribution agreements. The OFT is obliged to have regard to the Vertical Guidelines when applying the CA98, pursuant to section 60 of the CA98.

57 Such an exemption is applicable to both vertical and horizontal agreements.

58 EC Regulation 330/2010.

Relevance of the CA98 to the remedies

Past practice

4.11 The introduction of the CA98 has been a significant factor in previous decisions of both the SoS and the CC to remove monopoly remedies following OFT advice. Amongst others, this has included decisions to remove monopoly remedies in relation to contraceptive sheaths, estate agents, dental goods, roadside advertising and pest control services.60

Supplier influence on resale prices

4.12 The Chapter I prohibition, amongst other things, prohibits agreements which have as their object the restriction of competition by imposing fixed or minimum retail prices. Indeed, since the coming into force of the CA98, the OFT has taken a number of infringement decisions against parties which engaged in RPM, some of which included the imposition of a financial penalty upon the infringing party.61

4.13 The VABER will not apply to vertical agreements which, directly or indirectly, in isolation or in combination with other factors has their object the restriction of a buyer’s ability to determine its sale price, without prejudice to the ability of a supplier to impose a maximum sale price or recommend a sale price, provided they do not amount to a fixed or minimum sale price as a result of pressure from, or incentives offered by, any of the parties.

4.14 In addition to direct RPM, where the suppliers establish the retail price directly, indirect means to achieve RPM62 include:

60 Details of the OFT’s advice in those cases can be found at: www.oft.gov.uk/OFTwork/markets-work/register-orders-undertakings/advice.

61 For example, Agreements between Hasbro UK Limited and distributors fixing the price of Hasbro toys and games CA98/18/2002 [2003] UKCLR 150.

62 Vertical Guidelines, paragraph 48.
• Fixing the distribution margin.

• Making the grant of rebates or reimbursement of promotional costs by the supplier subject to the observance of a given price level.

• Threats, intimidation and warnings...in relation to the observance of a given price level.

• Linking the resale price to the resale prices of competitors.

4.15 Furthermore, direct and indirect RPM can be made more effective when combined with measures which may reduce the buyer’s incentives to lower the retail price. These include:

• The implementation of a price monitoring system and/or reporting obligations on retailers in respect of undertakings which are not adhering to minimum price levels.

• The supplier printing a RRP on the product.63

4.16 The OFT notes that several of the practices referred to in paragraph 4.14 and 4.15 are identical, or substantially similar, to the steps taken by suppliers to influence resale prices of DEGs when the MMC reported. Following the implementation of the CA98, these practices are now capable of being addressed as RPM under the Chapter I prohibition.

4.17 The OFT considers that the CA98 is an effective mechanism to address future instances of suppliers unduly influencing retail prices in the absence of the remedy.

The Modernisation Regulation

4.18 As referred to in paragraph 4.4, the Modernisation Regulation took effect on 1 May 2004. Amongst other things, this requires national competition authorities, such as the OFT, to apply and enforce Articles 101 and 102

63 Vertical Guidelines, paragraph 48.
of TFEU, when national law is applied to agreements which may affect trade between member states. Article 3 of the Modernisation Regulation provides that national competition law may not lead to the prohibition of an agreement which would be permitted under Article 101 TFEU or covered by a block exemption.

4.19 Recommended resale prices are generally permitted where they fall within the scope of the VABER (paragraph 4.13). However, article 2 of the Order prohibits a supplier from making such recommendations in any circumstances. This creates a risk that article 2 of the Order may go beyond what is permitted under EU law. Given the OFT’s views on the changes of circumstances (considered in chapter 5), it does not need to form a view on this point. However, should the CC decide not to revoke article 2 of the Order it would need to consider this issue further, particularly considering whether variation or revocation was now appropriate.

Selective distribution

4.20 The MMC found that the practice whereby suppliers withheld supply of DEGs to warehouse clubs represented a discriminatory application of the selective distribution criteria which suppliers used to select dealers for supply and restricted competition in DEGs retailing.

4.21 Selective distribution agreements may fall within the scope of the Chapter I prohibition in certain circumstances.\(^\text{64}\)

4.22 Selective distribution agreements which meet the criteria for the application of the VABER will be exempt from the application of the Chapter I prohibition by virtue of the parallel exemption. However, where the VABER does not apply, any potential competition concerns raised by a

\(^{64}\) Paragraph 175 of the Vertical Guidelines summarise the circumstances in which purely qualitative selective distribution systems used to select dealers only on the basis of objective criteria required by the nature of the product in question may not be restrictive of competition and may fall outside the scope of the Chapter I prohibition/Article 101(1) TFEU based on a lack of anti-competitive effects.
selective distribution agreement (or agreements) can be considered under the Chapter I prohibition. Further, the withdrawal or disapplication of the VABER to certain categories of agreements can be considered where this leads to cumulative effects in a particular market. The OFT therefore considers that the CA98 is an effective mechanism to address future instances of selective distribution agreements which have an adverse impact on competition.

Conclusion

4.23 Since the remedies were introduced in 1998, the CA98 has been implemented. This provides an effective mechanism to address issues of the type which are covered by the remedies in the unlikely event that they re-emerge in the future. Any decision to take action under the CA98 would only be made following an assessment against the OFT’s prioritisation principles. A key aspect of this prioritisation assessment would be the impact that any action would have on consumer welfare.66

65 For example, potential competition concerns may include where selective distribution agreements lead to the foreclosure of certain distributors (such as price discounters). A more detailed discussion of the potential competition risks raised by selective distribution agreements is set out at paragraphs 177 to 186 of the Verticals Guidelines.

66 OFT (2008), Prioritisation Principles.
5 CONCLUSIONS AND ADVICE

5.1 This chapter sets out the OFT’s advice to the CC in relation to the remedies. It draws on the preceding analysis of the market and legal changes since the MMC reported.

View of parties

5.2 The OFT has carefully considered the views on the continued appropriateness of the remedies which it has received from parties across the DEGs sector. Around two thirds of the submissions received by the OFT considered that the remedies were less necessary, no longer necessary or irrelevant, due to the developments which are considered in chapters 3 and 4. Different parties placed a different emphasis on which developments were most relevant to the removal of the remedies.

5.3 In addition, some parties suggested that the remedies were having a harmful impact upon competition and consumers:

- One large supplier and several retailers submitted that RRPs could be useful to consumers by providing a benchmark they can use to determine whether the retailer is providing a competitive price for the DEGs which they are selling.

- One retail buying group, which acts on behalf of independent retailers, submitted that the Order restricts its ability to effectively organise effective price promotions, by preventing it from advertising a promotional price at which members participating in the promotion must resell. It has suggested that this restricts its members’ ability to compete and acquire business from other retailers.

5.4 Of the minority of parties which considered that the Order should be retained, all of those which provided a view on developments in competition for DEGs retailing highlighted that the DEGs market was competitive. Several of them noted that the Order had contributed to enhanced competition and should therefore be retained.
5.5 Two retailers submitted that, notwithstanding the Order, they have some difficulties in obtaining supplies of certain types of DEGs. One of these parties acknowledged, with respect to most of the refusal to supply provisions of the Order, that it is ‘unclear to what extent they go beyond the principles of UK and EU competition law’.

5.6 Each of the parties which entered into undertakings or assurances were invited to provide comments to the OFT. However, only the largest of the parties (such as Dixons and CIH) which gave undertakings made representations to the OFT regarding the undertakings. Furthermore, none of the parties which gave assurances made representations to the OFT regarding the assurances. In addition, the OFT invited comments from warehouse clubs, which were a particular focus of the MMC’s report. However, none of those warehouse clubs responded to the OFT’s invitation to comment.

OFT comments on key views from parties

5.7 The OFT has specifically considered the views of the minority of parties which have argued that the remedies should wholly or in part be retained. Its view on these arguments is below.

- The OFT notes that some retailers have argued that the Order should be retained as it has facilitated a more competitive market. The OFT has come to no specific conclusion on the extent to which the changes in competition arise directly as a result of the Order or from other factors. It has, instead, focused on the extent to which the adverse findings would re-emerge in the absence of the Order. The OFT considers that the changes of circumstances set out in this report mean that the market is unlikely to revert to the circumstances which existed at the time the MMC reported.

- The OFT notes the concerns expressed by retailers regarding access to certain DEGs. The OFT notes that these concerns have only been expressed by a few retailers. In addition, the OFT notes that such restrictions are likely to raise from lawful selective distribution
systems which are, in general, compatible with the Order and can lead to benefits to consumers, such as enhanced pre-sales service.67

Changes of circumstances

5.8 In conducting a remedy review, the OFT’s statutory duty is to consider whether, by reason of any change of circumstances, an Order or an undertaking is no longer appropriate.

5.9 The OFT considers that, since the MMC reported, there have been numerous changes of circumstances in this market which mean that the adverse findings identified by the MMC are unlikely to re-emerge and that the remedies are therefore no longer appropriate. These changes of circumstances are:

- **Changes in technology**: The changes in DEGs technology, particularly for brown goods, mean that several of the DEGs covered by the MMC’s report have significantly diminished in importance, such that they are largely obsolete.

- **Changes in the retailing of DEGs**: There has been a significant growth in the proportion of DEGs sales through non-specialist high street retailers and through online retailers. This has had the following effects:
  
  - These non-specialist high street retailers and online retailers often focus their offer to consumers on a value based pricing proposition and are therefore less likely to demonstrate the significant 'antipathy' to price discounting which existed when the MMC reported. They are therefore less likely to adhere to RRPs in the absence of the Order as an inability to discount would weaken their ability to acquire and retain customers.

67 See OFT 419 (2004), *Vertical Agreements*, paragraphs 7.19 to 7.29 for the benefits of vertical restraints. Chapter 4 includes further discussion of competition issues regarding selective distribution agreements.
- The significance of non-specialist high street retailers and online retailers as a source of DEGs sales means that suppliers are likely to have a greater incentive to supply DEGs to those retailers. This is because they now account for a significant proportion of DEGs sales and, ultimately, a supplier’s turnover.

- The online channel provides an effective mechanism for lower cost entry into DEGs retailing, which has facilitated entry and/or expansion for a wider range of retailers.

- **Changes in consumer behaviour**, particularly consumers taking advantage of the increased price transparency which has been created by the internet to shop around for DEGs:

  - Given the significant amount of consumer research for DEGs and greater consumer focus on the price of the DEG, a retailer which discounts from an RRP is likely to be able to reach and acquire a much greater range of customers than was the case when the MMC reported. It, therefore, would have less of an incentive to adhere to RRP prices absent the Order as an inability to discount would weaken its ability to acquire and retain customers.

5.10 In addition, the **introduction of the CA98**, now provides an effective mechanism to address issues of the type which are covered by the remedies, in the unlikely event that they re-emerged in the future.

5.11 Table 5.1 illustrates which change of circumstances relates to which element of the remedies.
Table 5.1: Changes of circumstances relevant to each aspect of the remedies

<table>
<thead>
<tr>
<th>The Remedy</th>
<th>Part of the remedy</th>
<th>Applicable changes of circumstances</th>
<th>Explanation</th>
</tr>
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<tbody>
<tr>
<td>The Order and undertakings</td>
<td>In so far as it relates to VCRs and video camcorders</td>
<td>Changes in technology</td>
<td>Changes in technology mean that those DEGs are now largely obsolete</td>
</tr>
<tr>
<td>The Order</td>
<td>In so far as it relates to supplier influence upon retail pricing</td>
<td>Changes in the retailing of DEGs</td>
<td>Greater significance of non-specialist retailers and online retailing with a value focus has facilitated a greater focus on price competition and provides retailers with stronger incentives to discount to acquire and retain customers</td>
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<tr>
<td>Changes in consumer behaviour</td>
<td></td>
<td></td>
<td>Increased price transparency through the internet, combined with greater consumer focus on price in their decision of which DEGs to purchase, provides retailers with stronger incentives to discount to acquire and retain customers</td>
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<tr>
<td>Changes in the law</td>
<td></td>
<td></td>
<td>The CA98 provides an effective mechanism to address any future concerns regarding RPM</td>
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<tr>
<td>In so far as it relates to supply to dealers</td>
<td>Changes in the retailing of DEGs</td>
<td>The non-specialist and online retailers represent a significant source of DEGs sales. A supplier which engages in refusal to supply could lose significant business</td>
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<tr>
<td>Changes in the law</td>
<td>The CA98 provides a mechanism to address selective distribution agreements which raise competition concerns</td>
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<tr>
<td>Undertakings given by CIH and others</td>
<td>Recommended resale pricing</td>
<td>Changes in the retailing of DEGs</td>
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<td></td>
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<td>Changes in consumer behaviour</td>
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<td></td>
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<td>Changes in the law</td>
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<td>As above in relation to supplier influence upon retail pricing</td>
<td></td>
<td></td>
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<tr>
<td>Entry into a buying group</td>
<td>Changes in the retailing of DEGs which facilitate retail entry</td>
<td>The internet now provides an effective mechanism to enable retailers to enter the DEGs retailing market, without the need to incur the costs of establishing a physical outlet network which will reduce entry costs. Other buying groups (for example, Sirius) now exist as an alternative to CIH (at least for most of the reference DEGs).</td>
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<tr>
<td>Undertakings given by Dixons</td>
<td>Preventing a contractual clause which discourages a supplier from permitting a 'disorderly market'</td>
<td>Changes in the retailing of DEGs</td>
<td>The growth of non-specialist high street retailers and online retailers means that a more 'disorderly' market has emerged and is likely to continue to exist in the future</td>
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<td></td>
<td>Changes in the law (in so far as the supplier would not be in a position to prevent a 'disorderly market')</td>
<td></td>
<td>The CA98 provides a mechanism to address supplier action to prevent a disorderly market (for example, through RPM)</td>
</tr>
<tr>
<td>Undertakings given by Empire</td>
<td>Preventing a contractual clause about requesting information from suppliers on current competitor prices</td>
<td>Changes in consumer behaviour (increased price transparency created by the internet)</td>
<td>Increased price transparency created by the internet means that real time, current information is readily available to retailers, without any requirement to request it from suppliers. Such a contractual clause would now be largely redundant</td>
</tr>
<tr>
<td>Undertakings given by GDA</td>
<td>Preventing a contractual clause regarding withdrawing promotional support in particular circumstances</td>
<td>Changes in the retailing of DEGs</td>
<td>Suppliers which attempted to impose contractual clauses to withdraw promotional support if a retailer engaged in discounting may come under significant commercial pressure from their retailers as an inability to discount would restrict their ability to acquire and retain custom</td>
</tr>
<tr>
<td></td>
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<td>The CA98 provides a mechanism to address supplier</td>
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action to impose indirect RPM, including action by suppliers to reduce promotional support should the retailer engage in discounting

5.12 Overall, the OFT considers that competition in DEGs retailing has significantly increased since the MMC reported, such that if the remedies were removed the MMC’s overall concerns about restrictions in choice for consumers and higher prices for DEGs would be unlikely to re-emerge into the future. To the extent that they did so, the CA98 provides an effective mechanism to address these issues into the future.

**Potential variation to the remedy**

5.13 During this review one party submitted that the Order should be varied to remedy or prevent the adverse effects specified by the MMC by alternative means, particularly through action to prevent suppliers from refusing to supply [a certain specific category of retailer]. That party submitted that an Order including such variation should be applied across DEGs, rather than only to the reference DEGs.

5.14 The OFT can only advise the CC to vary or supersede an Order where, by reason of any change of circumstances, it is no longer appropriate to remedy or prevent the adverse effects specified in the MMC’s report on the basis of the specific facts found by the MMC. The OFT cannot, therefore, advise the CC to vary the Order in order to remedy or prevent issues which go beyond the adverse effects on the basis of the particular facts found. The OFT has considered this suggested variation against this background.

5.15 The OFT notes that a variation to extend to address issues arising from [ ] fall outside of the scope of a solution to remedy or prevent the adverse effects specified in the MMC’s report. In addition, the Order cannot be extended to cover DEGs which are not included within the MMC’s adverse findings. In any event, the OFT notes that the recent review of
the verticals regime by the European Commission considered, in some detail, issues regarding the appropriate treatment of distribution agreements under competition law, [...]. The revised versions of the VABER and the Verticals guideline reflect this detailed consideration.68

Advice to the CC

5.16 The OFT considers that there have been numerous changes of circumstances which mean that the remedies are now no longer appropriate. In this instance, the OFT is of the view that an appropriate outcome would be that:

- The Order is revoked.
- Those parties which gave undertakings should be released from them in their entirety.

Conclusion on the assurances

5.17 The assurances require certain parties to comply with aspects of the Order. For the same reasons as the OFT’s conclusion on the Order, it has provisionally decided that all of the parties which gave assurances can be released from them in their entirety. However, before taking a final decision on this issue, the OFT will consider any relevant issues which arise from the CC’s consideration of the OFT’s advice regarding the Order and undertakings.

68 Further information on the verticals review can be found at:
ANNEXE: SUMMARY OF THE REMEDIES AND ASSURANCES

The Order

In force - 1 September 1998

(i) The Order covers the reference DEGs (referred to as 'the Goods').

(ii) Suppliers must not recommend resale prices to dealers

(iii) Suppliers must not make agreements with dealers which restrict dealers' determination of the prices at which they advertise or sell the Goods

(iv) Suppliers must not refuse dealers supplies of the Goods unless the supplier has confirmed to the dealer in writing that Goods are being withheld for any of the following reasons:

   (a) the value of the Goods ordered is, or is likely to be, less than a generally set minimum or more than a generally set maximum value in the calendar year in which the request is made,

   (b) the order value is below a generally set minimum or above a generally set maximum size,

   (c) the Goods are not available for supply,

   (d) the supplier thinks he will not get paid for the Goods or has not had the opportunity to check the dealer’s ability to pay,

   (e) the dealer does not meet the supplier’s criteria for supply, but such criteria must not include those which seek to maintain or increase resale or dealers’ advertised prices, relate to dealers’ profit margins on the sale of the Goods, or relate to the dealers willingness to sell to consumers or shop opening times.
(v) suppliers must supply Goods requested to all dealers that meet the supplier’s criteria unless one or more of the reasons in (iv) above applies,

(vi) Requesting dealers must be given a written statement of suppliers’ criteria currently in force in relation to the Goods requested.

(vii) Suppliers must not engage in price discrimination between dealers or give preference to any dealers on the grounds of the prices charged or advertised by dealers for any goods.

The Undertakings

Date of original undertakings: 15 May 1998

Companies giving undertakings: Note: There are five sets of undertakings. The number after each company’s name indicates to which set it is a signatory.69

Birmingham Combined Independents Limited (2)
Combined Independents Limited (2)
Combined Independents (Bedfordshire and Northamptonshire) Limited (2)
Combined Independents (Holdings) Limited (1)
Combined Independents (Lincs) Limited (2)
Combined Independents (Liverpool) Limited (2)
Combined Independents (North) Limited (2)
Dixons Group plc (3)
Empire Stores Group plc (or Redcats UK plc) (4)
Five Star Electric Holdings Limited (2)
Independent Electrical Supplies (Hull) Limited (2)
General Domestic Appliances Holdings Limited (5)
Manchester Combined Independents Limited (2)
Mid-Somerset Trading Company Limited (2)
North Derbyshire Independents Limited (2)
Pendle Valley Retailers Limited (2)

69 The below are the undertakings which were included in the Enterprise Act 2002 (Enforcement Undertakings and Orders) Order 2004 (SI 2181 of 2004).
Details of undertakings

(1) Combined Independents Holdings Limited undertook as follows:

   (i) Not to refuse membership on its standard terms to any dealer who:

       (a) applies for it,
       (b) satisfies the standard terms of membership of the company,
       (c) can demonstrate ability to pay for goods he may order from or through the Company or a local group, and
       (d) is a member of a local group or has applied for membership of a local group, provided that the Company can terminate his membership of the Company if the local group refuses membership.

   (ii) Where the Company refuses membership to a dealer, it will forthwith give the dealer a written statement of the grounds for its refusal.

   (iii) The Company will not make any recommendation restricting the sale of goods purchased from or through the Company or a local group.

(2) The companies concerned undertook in terms similar to (1) above.

(3) Dixons Group plc alone undertook that, in its and its subsidiaries' terms and conditions of purchase of Goods, it would not insert a clause reserving to the Company or any subsidiary the right to renegotiate prices or delivery dates or to cancel the contract in the event that disorderly market forces are allowed by the supplier of those goods to prevail which are to the detriment of the profitability or sales rate of the company or any subsidiary or a clause to like effect.

(4) Empire Stores Group plc alone undertook not to seek information from suppliers on competitors' prices for the reference DEGs.

(5) General Domestic Appliances Holdings Limited alone undertook that in its and its subsidiaries' terms and conditions of purchase, it would not insert a
clause providing that if at any time a dealer’s margin needs on any goods change, the level of promotional support or additional margin support required to support any jointly agreed plan of the company or a subsidiary and the dealer may be subject to a change, or a clause to like effect.

The assurances

Date of assurances: Various between 1999 and 2001

Companies giving assurances.

The CDA Group Limited
Bradshaw Appliances Limited
Maurice Lay Distributors Limited
Waterline Limited
PJH Group Limited
J P Distribution Limited
Maymarts Limited
Mark Two Distributors
Wolseley Centers Limited (Trading as Crangrove)

Details of assurances

Each of the parties which gave assurances agreed:

(i) Not to breach article 2 of the Order by publication, or otherwise, notification to dealers prices recommended or suggested as appropriate to be charged by those dealers for the reference DEGs.

(ii) Not supply any dealer with a price list, with the prices recommended or suggested as appropriate to be charged by the dealer for those reference DEGs.