

## GROCERIES MARKET INVESTIGATION

### Notice of possible remedies under Rule 11 of the Competition Commission Rules of Procedure

#### Introduction

1. On 9 May 2006, the Office of Fair Trading (OFT) referred the supply of groceries by retailers in the United Kingdom to the Competition Commission (CC) for investigation. The reference was made under section 131 of the Enterprise Act 2002 (the Act).
2. In its provisional findings published on 31 October 2007, the CC has provisionally found that there are features of the markets for the supply of groceries by retailers in the UK, either alone or in combination with each other, that prevent, restrict or distort competition in connection with the supply or acquisition of groceries by retailers. Hence, there is a provisional finding of an adverse effect on competition (AEC) within the meaning of section 134(2) of the Act. The provisional findings report identified those features that give rise to the AEC and the detrimental effects on customers that have resulted from or may be expected to result from the AEC.
3. This notice invites comments on the actions that the CC considers might be taken by the CC, or recommended for implementation by others, for the purpose of remedying, mitigating or preventing the AEC concerned or any resulting detrimental effects on customers.

#### Provisional findings

4. We have identified separate product markets for: the supply of groceries by larger grocery stores; the supply of groceries by mid-sized and larger grocery stores; and the supply of groceries by all grocery stores, including convenience stores. We have also identified that the geographic markets for grocery retailing are local.
5. We have provisionally found that a combination of one or more of the following features prevent, restrict or distort competition in certain local markets for the supply of groceries by larger grocery stores:
  - (a) A significant number of local markets have high levels of concentration, and these high levels of concentration have persisted over a number of years.
  - (b) The planning regime (in particular, PPS6 in England, SPP8 in Scotland, PPS5 in Northern Ireland and MIPPS 02/2005 in Wales), and the manner in which the planning regime is applied by Local Planning Authorities, acts as a barrier to entry or expansion in a significant number of local markets:
    - (i) by limiting construction of new larger grocery stores on out-of-centre or edge-of-centre sites; and
    - (ii) by imposing costs and risks on smaller retailers and entrants without pre-existing grocery retail operations in the UK that are not borne to the same extent by existing national-level grocery retailers.

- (c) The control of land in highly-concentrated local markets by incumbent retailers acts as a barrier to entry, by limiting entrants' access to potential sites for new larger grocery stores.
- 6. We have provisionally found that a combination of one or more of the following features prevent, restrict or distort competition in certain local markets for the supply of groceries by mid-sized and larger grocery stores:
  - (a) a significant number of local markets have high levels of concentration, and these high levels of concentration have persisted over a number of years; and
  - (b) the control of land in highly-concentrated local markets by incumbent retailers acts as a barrier to entry, by limiting entrants' access to potential sites for new mid-sized and larger grocery stores.
- 7. We have provisionally found that the following features prevent, restrict or distort competition in certain local markets for the supply of groceries by all grocery stores:
  - (a) the control of land in highly-concentrated local markets by incumbent retailers acts as a barrier to entry, by limiting entrants' access to potential sites for new mid-sized and larger grocery stores.
- 8. We have provisionally found that the exercise of buyer power by certain grocery retailers and symbol groups with respect to their suppliers of groceries, through the adoption of supply chain practices that transfer excessive risks and unexpected costs to those suppliers, is a feature of the markets for the supply of groceries by all grocery stores, which prevents, restricts or distorts competition in connection with the acquisition of groceries by those grocery retailers and symbol groups.

### **Criteria for consideration of remedies**

- 9. In choosing appropriate remedial action, the CC has a duty to achieve as comprehensive a solution as is reasonable and practicable to the AEC and any detrimental effects on customers resulting from it, as set out in section 134(6) of the Act.
- 10. The CC will consider the effectiveness of different possible remedies and their associated costs and benefits and will have regard to the principle of proportionality. Between two remedies that the CC considers equally effective, it will choose that which imposes the least cost or restriction.
- 11. The CC notes that some of the remedies discussed below may, if implemented, have implications beyond the market for grocery retailing in the UK. In considering the reasonableness and practicability of any remedy, the CC may have regard to any such wider implications, and may, in particular, take account the interaction between its remedies and any wider public policy objectives (for example, in relation to the planning system).
- 12. The CC will also have regard to the effects of any remedial action on any relevant customer benefits within the meaning of section 134(6) of the Act arising from a feature or features of the market giving rise to the AEC. Such benefits comprise lower prices, higher quality or greater choice of goods or services or greater innovation in relation to such goods or services. The CC welcomes views on the nature, scale and likelihood of any such benefits and the potential impact on such benefits of possible remedies.

## **Possible remedies on which views are sought**

13. The various measures, alone or in combination, that are currently being considered by the CC as possible remedies to the AEC and customer detriments that have been identified in the provisional findings report for the supply of groceries by retailers in the UK, and on which comments are invited, are set out below.
14. These comprise:
  - (a) measures designed to address local concentration, by:
    - (i) addressing barriers to entry arising from the planning system; and
    - (ii) addressing barriers to entry from controlled land, including land holdings, in highly-concentrated local markets;
  - (b) measures designed to address the exercise of buyer power by grocery retailers and symbol groups so as transfer excessive risks and unexpected costs to suppliers.

### ***Measures to address local concentration***

15. The CC intends that its remedies to address local concentration should focus on measures that would have the effect of opening up local markets by reducing barriers to entry. The CC has identified two principal means by which this may be achieved:
  - (a) measures to address barriers to entry from the planning system; and
  - (b) measures to address barriers to entry from controlled land, including land holdings, in highly-concentrated local markets.

### ***Measures to address barriers to entry from the planning system***

16. The CC is considering recommending changes to the planning system that would facilitate greater availability of land for development outside the town centre. In particular the CC is considering and invites views on the following issues:
  - (a) Whether the planning system should distinguish edge-of-centre sites from out-of-centre sites, recognizing that edge-of-centre stores can benefit the town centre.
  - (b) The extent to which a possible amended planning test should recognize quantitative and qualitative aspects of need.
17. The CC is considering recommending measures that would result in a streamlining of the planning system. In particular the CC is considering and invites views on the following issues:
  - (a) Whether to recommend the abolition of one or more of the various tests included in the current system and if so how?
18. The CC is considering recommending changes to the planning system that would see the inclusion of a 'competition test' at some point in the planning process. In particular, the CC is considering and invites views on the following issues:
  - (a) Whether grocery retailers should be required to pass a competition test before being permitted to submit a planning application for a grocery retail store? If so:

- (i) Whether all grocery retailers should be required to pass this test or whether the test should only be applied to certain grocery retailers and if so which ones?
  - (ii) Whether developers should also be required to pass this test if they wish to include a grocery retail store in a planned development (in relation to identifying which grocery retailers would be approved to move into the grocery retail store—see 18(b)(iii) below)?
  - (iii) How such a test should be framed? For example, should it be framed so that a particular retailer would only be permitted to submit a planning application for a grocery retail store if the planned store would not result in its acquiring more than a certain percentage of the market in a given local area, what would be the appropriate metric for that percentage, what would be the appropriate percentage limit, and how should a local area be defined?
  - (iv) Who should apply such a test? Should the test be applied by the OFT and if not by the OFT then by whom?
- (b) Whether the planning system should be changed to ensure that planning officers and local authority planning committees take account of the effect on competition of a proposed scheme in their decision on whether to grant consent? If so:
- (i) How should competition be taken into account in the planning system? Should there be a relatively mechanistic test (for example based on number of fascia and/or shares of net sales area in a particular local area) or should competition be included in a list of factors to which local planning authorities should have regard?
  - (ii) Are local planning authorities well placed to apply any such competition test themselves or should a specialist body such as the OFT apply any such competition test? If a specialist body were to apply the test should that body have the status of a statutory consultee? Should that body be expected to take part in appeals on planning decisions that raise questions about the application of the competition test? How should any body applying the competition test be resourced to do so?
  - (iii) Should the CC recommend changes to the planning system to permit local planning authorities to give fascia-specific consents or impose fascia-specific restrictions (ie granting consent for a grocery retail store operated by a particular retailer, or granting consent with a restriction that a particular retailer does not operate from the store)?
19. In relation to all these possible remedies in relation to the planning system, the CC invites views on how these (or other planning remedies) could best be implemented, bearing in mind the differences between the systems in place in England, Wales, Scotland and Northern Ireland. As noted in paragraph 14 above, in choosing its remedies the CC may have regard to the way in which its remedies would interact with any wider public policy objectives. The CC therefore invites views on whether any of possible remedies in relation to the planning system, as outlined above, would work against the wider public policy objectives of the planning system and how any such tensions should affect its choice of remedies and their design.

## **Measures to address barriers to entry from controlled land**

20. The CC is considering remedies that would prevent grocery retailers using various mechanisms available to them to control land with the effect of creating a barrier to entry. The CC is in particular considering:
- (a) Prohibiting grocery retailers from imposing or entering into restrictive covenants or other agreements—either in relation to their sales or acquisitions of land—that have the effect of reducing the likelihood of the land being used for a competing grocery retail store.
  - (b) Prohibiting grocery retailers from enforcing restrictive covenants or other agreements that have the effect of reducing the likelihood of the land being used for a competing grocery retail store. This may be accompanied by a requirement on grocery retailers to write to all parties subject to such restrictive covenants or agreements informing them that these will not be enforced.
  - (c) Recommending an amendment to the Land Agreements Exclusion Order so that restrictive covenants and exclusivity arrangements entered into by grocery retailers should no longer benefit from exclusion from the *Competition Act 1998*.
  - (d) Requiring grocery retailers to notify the OFT of all restrictive covenants that it imposes, and all exclusivity arrangements from which it benefits. This measure could be adopted on a stand-alone basis or in conjunction with (c).
  - (e) Requiring all subleases of closed stores above a given size to be notified to the OFT for prior approval.
21. The CC is considering and invites views on the following issues in relation to such a remedy:
- (a) Whether such measures should be applied uniformly, or only to certain grocery retailers and/or in certain circumstances.
  - (b) Given that the CC has found that this is most significant in the product market for larger grocery stores, should this measure only be applied in relation to land suitable for development as a larger grocery store (and smaller packages of land that could impede the development of a site by another grocery retailer), or would the need to assemble sites from smaller packages of land make this inappropriate?
  - (c) If such measures should be applied only to certain grocery retailers and/or in certain circumstances, to which retailers and in which circumstances should they be applied?
  - (d) What would be involved in considering restrictive covenants and exclusivity arrangements under the Competition Act 1998, and whether a simplified procedure might be applied?
  - (e) Would the OFT be the most appropriate body to be notified of restrictive covenants, exclusivity arrangements or subleases of closed stores? If not, who would be the most appropriate body?
  - (f) Are there other means of addressing barriers to entry from controlled land?

22. The CC is considering remedies that would, in certain circumstances, require grocery retailers to divest land holdings in order to facilitate new entry within a short period of time. The CC is considering and invites views on the following issues in relation to such a remedy:
- (a) Should divestitures of land holdings only be required in areas of existing high concentration or also applied in areas where land holdings would, if developed, produce high concentration?
  - (b) In how many areas is it likely that local concentration would need to be addressed in this way? In how many areas is it likely that prospective local concentration would need to be dealt with by divestiture of land holdings?
  - (c) Should the CC impose a condition on grocery retailers' that any land holdings not developed within a given period must be divested ? If so:
    - (i) Should such a condition only be applied in areas of high concentration?
    - (ii) Should such a condition only be applied to land holdings above a certain size, for example to allow for site assembly?
    - (iii) After how long a period of holding the land should a retailer be obliged to divest?
    - (iv) Is there the possibility, and how should the CC deal with the possibility, that grocery retailers may seek to undermine such a remedy, for example by selling land on to third parties shortly before the end of the permitted holding period with an understanding that it would be bought back shortly thereafter?
    - (v) How should the CC distinguish between situations where site assembly is difficult and necessarily takes and those where the process is unnecessarily taking too long?
  - (d) Should the CC permit divestiture of land holdings only to purchasers that would operate or facilitate the operation of a competing grocery retail store on the site? If so, given that there may be a need for site assembly, how should this criterion be applied, particularly if the land has not previously been used for retail purposes?
  - (e) What process should be put in place to monitor those divestitures?
  - (f) Would a prohibition on reacquisition by the divesting party be necessary?
  - (g) Are there other means of directly addressing land holdings as a barrier to entry?

***Other measures to address local concentration***

23. The CC currently expects that the measures outlined above, in relation to the planning system and controlled land, could together be expected to address the high concentration it has provisionally found in some local markets. If the CC considers that there are local markets in which these measures would not be expected to address high concentration, the CC may need to consider addressing concentration more directly.
24. The CC is therefore considering what other measures it may need to take directly to address high concentration in certain local markets, such as store divestitures.

Whether such measures are appropriate will depend on local circumstances, for example whether the local market could be expected to support multiple competing stores.

25. In particular, the CC is considering and invites view on the following issues:
- (a) whether and in what circumstances it would be appropriate to require store divestitures;
  - (b) how stores for divestiture should be selected;
  - (c) whether there are any other measures that could be used to address high concentration in local areas where addressing barriers to entry resulting from land holdings, controlled land and the planning system would not address the issue.

***Measures to address the transfer of excessive risks and unexpected costs to suppliers***

26. The CC is considering remedies that would address the transfer of excessive risks and unexpected costs to suppliers by grocery retailers and symbol groups:
- (a) changing the threshold according to which grocery retailers are included within the Supermarkets Code of Practice (SCOP);
  - (b) changing the SCOP such that symbol groups are included within it;
  - (c) changing the SCOP such that only certain suppliers are included within it, and if so which those suppliers should be;
  - (d) changing the nature of the restrictions contained within the SCOP;
  - (e) changing the SCOP so as to improve the visibility of compliance or non-compliance; and
  - (f) changing the institutional arrangements for the monitoring and enforcement of the SCOP.
27. The CC invites views on the following issues in relation to such a remedy:
- (a) whether the SCOP should be retained in its present form with no changes.
  - (b) whether all grocery retailers should be included in the SCOP? If not which retailers should be included and why? How could any threshold for inclusion best be designed in order to ensure that the SCOP remained relevant over time?
  - (c) whether symbol groups should be included in the SCOP? If so, which symbol groups—if any—should be included and why? How could any threshold for inclusion best be designed in order to ensure that the SCOP remained relevant over time?
  - (d) do the current restrictions in the SCOP adequately cover those problematic behaviours in which grocery retailers, wholesalers and buying groups engage? If no, what restrictions should be added?

- (e) are there restrictions currently in the SCOP which are no longer necessary? If so, should they be removed or changed? If they should be changed, how should they be changed?
  - (f) does the way in which the current restrictions in the SCOP are phrased militate against complaints, monitoring or enforcement? If so, how could the phrasing be changed?
  - (g) is the monitoring of compliance with the SCOP effective? Do suppliers need encouragement to raise complaints about the behaviour of grocery retailers, wholesalers or buying groups? If so, how could this be achieved? Are there practicable ways in which suppliers could be offered anonymity? Would a requirement on those within the SCOP to submit regular reports to the monitoring body increase the visibility of compliance or non-compliance? In order to be meaningful, what should such reports contain? Would a requirement on those within the SCOP to conduct business with suppliers in writing (eg written contracts, discussions by email) usefully increase the visibility of compliance or non-compliance?
  - (h) is the OFT best placed on its own to monitor compliance with the SCOP, bearing in mind the changes that the CC's remedies may bring? Could the OFT usefully receive expert assistance in its compliance monitoring and enforcement role? If so, from whom? Would a 'supermarkets ombudsman' be appropriate? Would it be appropriate to introduce some dispute resolution or mediation mechanism within the SCOP? How would any such expert assistance be paid for?
28. In addition, the CC is considering whether there is scope to identify best practice in relation to grocery retailers' dealings with their suppliers and how any such best practice might be best disseminated among grocery retailers. The CC invites views on:
- (a) Should the CC itself seek to identify best practice? If so, how? Should the CC instead seek to establish a mechanism by which retailers, wholesalers and buying groups should identify best practice? If so, how should this be done?
  - (b) How could such best practice be disseminated among grocery retailers?
  - (c) How could the adoption of such best practice be encouraged?

### ***Other possible remedies***

29. The CC is willing to consider any practical alternatives to the possible remedies outlined above that the parties to the inquiry or other persons would like to propose, which they consider would appropriately address the identified AEC or resulting detrimental effects.

### **Relevant customer benefits**

30. The CC will also have regard to the effects of any remedial action on any relevant customer benefits within the meaning of section 134 (8) of the Act arising from the feature or features of the market concerned. Such benefits comprise lower prices, higher quality or greater choice of goods or services or greater innovation in relation to such goods or services. The CC welcomes views on the nature, scale and likelihood of such benefits and on the impact of its possible remedies on any such benefits.

## **Next steps**

31. A copy of this notice will be posted on the CC website. The parties to this inquiry and any other interested persons are requested to provide any views in writing, including any additional or alternative remedies they wish the CC to consider, by 23 November 2007 (see note below).

*(signed)* Peter Freeman  
Group Chairman  
31 October 2007

### **Note:**

This Notice of possible actions to remedy the AEC and any resulting detrimental effects is given having regard to the CC's provisional findings published on 31 October 2007. The parties to the inquiry or other interested persons have until 30 November 2007 to respond to the provisional findings report. In the light of any responses by the parties or by other interested persons, the CC's findings may change and the CC may consider other possible remedies, if appropriate.