APPENDIX 2.1

*(referred to in paragraphs 2.35, 8.144, 8.283, 8.311, 9.366, 9.775 and 9.1159)*

# Issues letter sent to suppliers on 25 June 1999

1. I am writing to you on behalf of the Commission about their inquiry into the supply of new motor cars within the UK. As you know, the Director General of Fair Trading referred this matter to the Commission on 17 March 1999.

## Provisional finding of a complex monopoly situation

2. The Commission have provisionally concluded that a complex monopoly situation as defined in section 6(1)(c) and (2) of the Fair Trading Act 1973 (FTA) exists, in that at least one-quarter of new cars supplied in the United Kingdom are supplied by a group of manufacturers and importers (suppliers) who, not being interconnected bodies corporate, so conduct their respective affairs as to prevent, restrict or distort competition in connection with the supply of new cars in that they engage in one or more of the following practices relating to sales and distribution:

(i) refusing to supply new cars for resale except through the supplier's franchised dealer system;

(ii) preventing dealers from selling other suppliers' new cars from the same premises, under the same management and under the same legal entity as they sell the supplier's cars;

(iii) entering into agreements with dealers that, either in the agreement or related documents, contain one or more of the following restrictions:

- (a) exclusive territories are allocated to dealers within which no other dealer will be supplied;
- (b) dealers are prevented from soliciting customers by advertising directly to individuals or businesses residing outside the dealer's territory;
- (c) dealers are allowed to sell the supplier's new cars only to final customers, customers' authorised agents or other dealers within the supplier's franchised network;

(iv) limiting the number and location of the supplier's dealerships held by each dealer, and/or the total volume of the supplier's new cars sold through each dealer's outlets taken together;

(v) limiting the number and location of other suppliers' dealerships held by each dealer;

(vi) limiting the extent to which, or conditions under which, dealers can engage in other businesses;

(vii) publishing recommended retail prices (RRPs) for new cars;

(viii) entering into agreements with dealers that, either in the agreement or related documents, contain one or more of the following financial terms:

- (a) setting wholesale prices to dealers by reference to published RRPs;
- (b) requiring dealers to contribute towards the supplier's marketing costs and/or to spend specified minimum sums on their own promotion of the supplier's new cars; requiring dealers' advertising to conform with the supplier's specifications;
- (c) providing part of dealers' remuneration in the form of bonuses which are subject to change at short notice and are contingent on various factors;

(ix) discouraging dealers from advertising the supplier's new cars at prices below RRP;

(x) discouraging dealers from offering discounts on particular models of new car, or from offering discounts over certain levels;

(xi) refusing to give volume discounts to dealers or dealer groups;

(xii) pre-registering new cars before supplying them to dealers;

(xiii) segmenting the market by negotiating terms direct with certain categories of fleet customer and giving volume discounts which are not available to dealers;

(xiv) bundling non-price benefits with new cars without offering customers the alternative of a reduction in price;

(xv) requiring dealers to offer servicing of the supplier's make of cars;

(xvi) requiring dealers to maintain specified standards of showroom appearance;

(xvii) requiring dealers to participate in the supplier's promotions, including of the sales of other car-related goods or services—such as loan finance, insurance and extended warranties—selected by the supplier;

(xviii) discouraging dealers from obtaining supplies of the supplier's new cars from dealers in other countries for sale to UK residents;

(xix) through restrictive warranty terms, requiring customers to use franchised dealers for routine servicing;

(xx) discouraging dealers from providing after-sales service for new cars imported from countries outside the EU by parties outside the supplier's group ('grey imports').

The Commission are still investigating whether there is evidence of a further practice, namely linking new car sales bonuses to sales made only to customers residing within the dealer's territory.

3. The members of this group comprise those of the companies listed in the **appendix** to this letter which engage in any of the practices described above.

4. The Commission have provisionally concluded that the complex monopoly situation exists in favour of these companies.

5. The Commission invite your views on their provisional conclusions, including the question of whether engaging in one or more of the practices listed in paragraph 2 prevents, restricts or distorts competition.

6. Under the FTA and their terms of reference the Commission have to determine whether:

(a) any steps (by way of uncompetitive practices or otherwise) are being taken by the companies listed in the appendix for the purpose of exploiting or maintaining the monopoly situation and, if so, by what uncompetitive practices or in what other way;

(b) any action or omission on the part of these companies is attributable to the existence of the monopoly situation and, if so, what the action or omission is, and in what way it is so attributable;

(c) any facts found by them in pursuance of their investigations operate or may be expected to operate against the public interest; and

(d) if so, what action, if any, might be taken to remedy or prevent any adverse effects.

7. The Commission have prepared a number of papers [not reproduced] which are relevant to their provisional conclusions set out in paragraphs 2 to 4 of this letter and to their consideration of public interest issues:

**Annex 1** Market definition

**Annex 2** Market structure

**Annex 3** Dealer discounts to customers

**Annex 4** Comments and criticisms received from third parties. This paper comprises a general section together with sections specific to individual suppliers, the latter being sent only to the supplier in question.

These papers do not cover everything which is relevant to the Commission’s provisional finding and the public interest issues. We have already sent you the Ipsos report on consumer focus groups and a paper on international price comparisons. In addition we shall shortly be sending you two further papers:

(a) Discounts to fleet customers (based on replies to the suppliers' questionnaire).

(b) Results of our survey of dealers.

8. You are invited to comment on all this material. I should be grateful if you would confirm in any event that the information relating to your own company is factually correct, and would also inform the Commission of any developments which might affect the accuracy of the information as the inquiry proceeds.

9. **Annex 5** to this letter outlines issues which the Commission will wish to consider in the next stage of the inquiry and which are relevant to the assessment of the public interest. I should emphasise that these issues and the comments which accompany them do not represent any conclusions of the Commission. They are intended solely to indicate points on which the Commission would welcome your views. There may well be other matters which the Commission will wish to raise with you during the course of the inquiry.

10. The Commission recognise that, in considering the possible effects of selective and exclusive distribution arrangements within the United Kingdom, they must have regard to EC law. In this context they are taking account of the provisions and operation of EC Regulation 1475/95.

11. You are invited to provide written comments or representations, which the Commission would expect to cover all the issues which you consider relevant to your company. If you have already dealt with any of the issues raised in Annex 5 in earlier submissions to the Commission, it will be sufficient to refer to these in your response. May we please have your response by **Friday 30 July.**

## Manufacturers and importers of new cars in the UK

The companies referred to in paragraphs 3 and 4 of the covering letter are the following:

BMW (GB) Limited

Citroen UK Ltd

Colt Car Company Limited (The)

Daewoo Cars Ltd

Fiat Auto (UK) Limited

Ford Motor Company Limited

Honda Motor Europe Limited

Hyundai Car (UK) Ltd

MCL Group Ltd*

Mercedes-Benz (United Kingdom) Limited

Nissan Motor (GB) Limited

Peugeot Motor Company PLC

Renault UK Limited

Rover Group Ltd

SAAB Great Britain Ltd

Suzuki GB PLC

Toyota (GB) Ltd

Vauxhall Motors Limited

VOLKSWAGEN Group United Kingdom Limited

Volvo Car UK Limited

Each of these companies supplied at least 1 per cent of the new cars supplied in the UK in 1998.

*Together with its subsidiary Mazda Cars (UK) Ltd.

# Issues relevant to the complex monopoly finding

## Selective and exclusive distribution (SED)

1. Whether the distribution system operated by suppliers of new cars in the UK has adverse effects on the level and nature of competition and, if so,

(a) leads to UK customers paying higher prices for new cars than would otherwise be the case;

(b) increases consumers' search costs when buying new cars and unduly reduces their choice of retail outlets;

(c) reduces innovation on the part of dealers; and

(d) inhibits improvements in the efficiency of the distribution system.

2. Whether any of the individual provisions listed in paragraphs 2(ii) to (vi) of the covering letter have adverse effects on competition and, if so, whether these effects have been on price, service, choice or other aspects.

3. Whether

(a) the distribution system as a whole, and

(b) the individual practices listed in paragraphs 2(ii) to (vi) of the covering letter

bring benefits to the consumer, eg in ensuring the availability of servicing, repair and parts for the suppliers' cars throughout the EU; in giving assurance to consumers that a high standard of after-sales service will be provided.

## Prices

### *Recommended retail prices (RRPs)*

4. Whether the publishing of RRPs by suppliers, taken together with other practices listed in paragraph 2 of the covering letter, notably (viii)(a), (ix) and (x),

(a) contributes to prices of new cars in the UK being higher than they otherwise would be;

(b) misleads customers as to the relative prices of different models given that transaction prices differ from RRPs by varying and, in many cases, significant amounts as a result of discounts and other factors.

Whether, on the other hand, RRPs provide a valuable benchmark which is readily available to all customers and potential customers and which could not be satisfactorily replaced by other means.

### *Bundling*

5. Whether the bundling of non-price benefits, and the absence of price reductions as an alternative, helps protect suppliers' price structures based on RRPs and leads to prices being higher than they otherwise would be.

### *Price comparisons with other EU member states*

6. Whether

(a) RRPs, and

(b) transaction prices

of new cars in the UK are persistently higher than in other EU member states. If so, what are the causes of this situation.

### *Bonuses to dealers*

7. Whether the partial replacement of dealer margins by bonuses in recent years has reduced dealers' ability to compete on price. If so, whether this development reduces both inter-brand and intra-brand competition and causes prices to consumers to be higher than they otherwise would be.

8. Whether bonuses to dealers for the sale of extended warranties, insurance, financial packages and other supplier-promoted services distort consumer choice and reduce the overall value for money obtained by consumers when buying new cars.

### *Dealer discounts to customers*

9. Whether the collection of information on dealers' businesses by suppliers enables them to monitor and influence dealer discounts to customers.

10. Whether suppliers' influence over dealer discounts to customers reduces both inter-brand and intra-brand competition and causes prices to customers to be higher than they otherwise would be.

### *Lack of volume discounts to dealers*

11. Whether the inability of dealers and dealer groups to obtain volume discounts from suppliers reduces both inter-brand and intra-brand competition and causes prices to retail customers to be higher than they otherwise would be.

### *Pre-registration of cars*

12. Whether the pre-registering of new cars—either by suppliers themselves or by dealers under the influence of supplier bonuses—allows price discrimination between different customers. If so, whether this causes a lack of transparency in pricing and creates uncertainty in consumers' minds as to the true price of cars.

### *Discounts to fleet customers*

13. Whether suppliers' willingness to negotiate terms direct with particular categories of fleet customer, and the high discounts given to these customers:

(a) cause both RRPs and transaction prices to retail buyers to be higher than they otherwise would be because of suppliers' need to recoup a disproportionate share of their overhead costs from retail sales; and

(b) depress residual values, with a further adverse effect on retail buyers.

### *Dealers' costs*

14. Whether the restrictions placed on dealers, such as those listed in paragraphs 2(iv) to (vi), prevent dealers from spreading their costs over more activities and hence contribute to prices being higher than they otherwise would be. Whether suppliers' control over standards of showroom appearance raises dealers' costs and hence contributes to higher prices.

## Dealers' sourcing of cars in other EU countries

15. Whether suppliers' discouragement of dealers from buying the suppliers' new cars from franchised dealers in other EU countries results in prices to consumers in the UK higher than they otherwise would be and enables manufacturers to maintain price differentials for comparable models between the UK and other EU markets.

## Specifications

16. Whether

(a) the size of the fleet sector, and fleet customers' preference for highly specified cars; and

(b) the segregation of the UK from other EU markets

lead suppliers to offer new cars for sale in the UK which, in general, have a higher specification than those they offer in other EU countries. If so, whether this reduces consumer choice and leads to consumers paying higher prices than they otherwise would.

### Voluntary export restraints

17. Whether voluntary export restraints continue to limit and distort the sales of Japanese new cars in the UK, and whether as a result prices of new cars in the UK are higher than they otherwise would be.

## Grey imports

18. Whether discouragement of dealers from providing after-sales service for grey imports deters consumers from buying such cars, restricts consumer choice and causes car prices in the UK to be higher than they otherwise would be.

## Warranty terms

19. Whether the use of restrictive warranty terms causes consumers to pay higher prices for servicing than they otherwise would and contributes to the tying together of new car sales and servicing.

## Other matters

20. Whether there are (a) employment and (b) environmental considerations which should be taken into account in assessing the effects of the practices listed in paragraph 2 of the covering letter.

## Future developments

21. Whether new methods of selling new cars, eg via the internet, will fundamentally change the distribution system and/or the level of competition in the UK market for new cars within the foreseeable future.