

Ensuring that Markets Work Well for Businesses and Consumers – a Strategic Assessment of Markets in Scotland

June 2016

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EXECUTIVE SUMMARY

The Scottish Government will use its competition powers to ensure that Scotland's markets are competitive and fair to consumers and, where this is not the case, to work with stakeholders to develop the appropriate evidence to address these concerns. The Strategic Assessment of Markets in Scotland is the first step in highlighting markets that may not be working well for Scottish consumers.

Our distinct economic, social and geographic circumstances provide challenges in ensuring that markets work well for Scottish consumers. Scotland has a substantial rural population who often face different issues from urban consumers including in accessing key services and choosing providers in regulated markets. Scotland is also characterised by an increasing ageing population and considerable deprivation which means there are an increasing number of potentially vulnerable consumers who need effective protection when purchasing goods and services.

Competitive markets work best when consumers are empowered to make decisions and when businesses innovate to respond to consumer demand. Disruptive technologies bring significant benefits to consumers but it is important to ensure that consumers are protected and that any regulation is fair and proportionate. Businesses' awareness of competition law and engagement with competition policy remains low and more can be done to increase this engagement.

In the regulated sectors, consumer engagement levels remain low, and seem to be lower in Scotland, meaning there is little competitive pressure on businesses. Scottish consumers also face specific issues across the regulated sectors, in part due to our geographic and social make-up, and it is important that these issues are considered.

Well-informed consumers are a critical part of a functioning market. In both public and private markets, consumers often face complex decisions without clear information about prices and services available. In the property market, despite a series of market reforms, consumer switching of property factors and awareness of the opportunity to switch remain low. Similarly, in the market for legal services, consumers are unaware of the distinction between unregulated legal services, which are not covered by the same protections, and regulated legal services. More can be done to ensure that consumers are well informed of their choices and options.

The provision of public transport is an area where competition, regulation and public provision must be carefully balanced. In particular in rural areas, access to affordable and reliable public transport is essential in order to provide people with access to essential services such as health, education and work. In all transport markets, it is important to ensure the service is working well for consumers and that consumers are confident and knowledgeable.

BACKGROUND

Purpose and Methodology

Purpose

The Strategic Assessment of Markets in Scotland aims to:

- provide an overview of the efficient functioning of markets in Scotland and their contribution to economic growth;
- highlight where Scotland's economic, geographic and social circumstances may have an impact on the competitiveness of markets; and
- highlight issues with either current or potential consumer protection or competition concerns which may merit further investigation.

This Assessment of Markets in Scotland brings together existing intelligence and data on Scotland's economy, markets and consumers with evidence and insight from a range of key stakeholders. This evidence has been gathered by the Scottish Government and through consultation with Scottish Government and external stakeholders.

The information and data gathered for the Strategic Assessment of Markets in Scotland has been used to identify the key areas of current or potential competition concern in Scotland. This is the first step in identifying issues that may be causing detriment to consumers in Scotland. In addressing these issues, the Scottish Government will work in close partnership with stakeholders to address the detriment to Scottish consumers. This Assessment contains actions that the Scottish Government will take forward in order to address market failures in Scotland. In taking action on these issues, the Scottish Government will work in close partnership with stakeholders to address the detriment to Scottish consumers.

Methodology

Evidence Gathering

The Scottish Government has gathered evidence from a range of sources including internal policy colleagues, trading standards enforcers, regulators, stakeholders representing consumers and businesses and experts on consumer and competition issues.

The Scottish Government attended a series of workshops held by the Competition and Markets Authority (CMA) in order to identify issues that could inform the Strategic Assessment of Markets in Scotland, including:

- an internal CMA workshop to consider potential areas of study on markets that might have a particular Scottish dimension, local Scottish markets, or where there may be different causes or levels of detriment to consumers in Scotland; and
- a series of thematic meetings that helped to inform the Assessment on the following topics: vulnerable consumers, disruptive technologies and public services.

The CMA has supported the Strategic Assessment of Markets in Scotland by helping scope relevant issues through its workshops and by acting as a critical friend throughout the entire process.

Filtering of Evidence

Specific markets have been included within the Strategic Assessment of Markets in Scotland for one or more of the following reasons:

- there are indications that the market may not be working well for Scottish consumers;
- the issues in the market disproportionately affect Scottish consumers; or
- the relative size of the market means that the issue may pose a greater level of detriment to Scottish consumers. This includes demographic and geographic circumstances.

SUMMARY OF ACTIONS

Household Expenditure: The Scottish Government will seek to gain a better understanding of the variation in consumer spending based on an individual's social, geographic and economic circumstances.

Productivity: The Scottish Government will seek to gain a better understanding of the links between productivity and competition with the aim of developing metrics to measure this relationship.

Businesses: The Scottish Government will carry out research into Scottish businesses' attitudes to competition and competition issues and will consider how to engage businesses more in competition matters.

Disruptive Technologies: As part of a wider package of work considering the balance between competition and regulation, the Scottish Government will carry out research to consider how to ensure Scottish businesses are able to make the most of the arrival of disruptive technologies and that market structures do not unnecessarily restrict the entry of new disruptive business models.

Consumers: The Scottish Government will consider whether the demographic and geographic circumstances of Scottish consumers have an impact on their behaviour or whether there is a cultural tendency for Scottish consumers to be more loyal to Scottish brands, particularly in the regulated sectors.

Switching: The Scottish Government will undertake a survey to establish the extent of switching and the barriers that consumers face. We will use the results from this survey to identify the characteristics of different types of switchers with the aim of developing targeted policy interventions.

Delivery Charges: The Scottish Government will continue its discussions with stakeholders to explore a range of sustainable solutions for rural communities.

Regulated Sectors: The Scottish Government will continue to ensure that on-going competition and regulatory investigations and studies take sufficient account of Scottish issues.

Legal Sector: The Scottish Government will ensure that consumers are better informed about their ability to switch property factor and of unregulated legal services.

Localised Markets: The Scottish Government will work with key partners to undertake scoping research to establish the features of localised markets.

Public and Private Markets: The Scottish Government will consider how best to provide consumers with the information needed to make informed decisions in complex and difficult markets such as health and social care.

Transport: The Scottish Government will consider whether there is adequate provision of consumer advocacy and redress as the first stage of our in depth research into transport services in Scotland.

CONTEXT

Our distinct economic, social and geographic circumstances provide challenges in ensuring that competitive markets work well for Scottish consumers. The Scottish Government will seek to develop a clearer understanding of the impact that these circumstances have on markets and whether and how this impact can be addressed.

Recent Scottish Economic Developments

The Scottish economy grew by 1.9 per cent during 2015¹. However, the pace of growth slowed across the year – following robust annual growth of 3.1 per cent to Q1 2015, the pace of growth slowed to annual growth of 0.9 per cent to Q4 2015. Growth of 0.2 per cent in the final quarter of the year, remains below Scotland's trend rate and followed a contraction of 0.1 per cent in Q3. This slowing growth in 2015 was driven by a challenging external environment, including sterling appreciation, and exacerbated by the low oil price.

The modest growth in 2015 was driven primarily by household expenditure and public infrastructure investment. The former has been supported by the low inflation environment, high levels of employment and real wage growth; the latter has benefited from a surge in construction activities in the public sector during the year. Recent labour market data has indicated that the ongoing challenges in the Scottish economy are impacting on the labour market. The latest Labour Force Survey statistics for February - April 2016 show that the Scottish employment rate fell by 1.3 percentage points over the year to 73.2 per cent. The Scottish unemployment rate was unchanged from a year previously, at 5.8 per cent. Alongside this, the economic inactivity (those not in work or not actively seeking work) rate rose 1.4 percentage points over the year to 22.2 per cent.

Future Outlook

Growth in Scotland was 1.9 per cent for 2015 while for the UK as a whole growth was 2.3 per cent. For 2016, independent forecasts suggest GDP growth of around 1.3 per cent is expected². These forecasts represent downward revisions compared to earlier forecasts.

The Scottish consumer sentiment indicator has, however, risen slightly in the first quarter of 2016, mainly driven by improvements in expectations for economic performance over the next twelve months as well as increases in both households' current and future financial positions³.

Prospects for 2016 and beyond expect to see a rebalancing within investment towards private sector expenditure; similarly, the balance of growth should become broader based as improved productivity may drive export growth. Looking ahead, the positive outlook for the economy of two of the main markets for Scotland (that is, the US and rest of the UK) may favour growth. The labour market is expected to remain robust in spite of headwinds from the external environment.

¹ Scottish Government, [Scottish Quarterly Gross Domestic Product](#), Q4 2015

² 1.4 per cent for Fraser of Allander Institute, June 2016 and 1.2 per cent for Scottish ITEM Club, June 2016

³ Scottish Government, [State of Economy](#), 3 June 2016

Economic Context

While Scotland's economy is closely linked with the rest of the United Kingdom, the following key industries particularly characterise the economic base of the country:

- Scotland has one of Europe's largest life science clusters, with more than 670 organisations employing over 35,000 staff⁴.
- Scotland has a large abundance of natural resources from fertile land, suitable for agriculture, to oil and gas. While the fall in the oil price has affected markets worldwide, North Sea oil and gas production contributed £9.9 billion to the Scottish economy in 2015⁵.
- The food and drink sector performs an important role in the economy, with Scotch whisky accounting for over 78 per cent of all Scottish food and drink overseas exports in 2015⁶.

As of March 2015, there were an estimated 361,345⁷ private sector enterprises operating in Scotland, which is the highest figure since 2000. Almost the total of them (98.3 per cent) were small (0 to 49 employees); 1.1 per cent (3,870 enterprises) were medium (50 to 249 employees) and 0.6 per cent (2,295 enterprises) were large (250 or more employees). Over the last 15 years, the increase of around 50.6 per cent in the number of private sector enterprises has been driven by a significant increase of the smallest unregistered enterprises.

While the number of large enterprises is small, they still account for 44.4 per cent of private sector employment and 60.6 per cent of private sector turnover. Medium-size enterprises instead have a modest role for both employment and turnover, at just above 10 per cent.

At the start of 2015, Scotland had the fewest registered private businesses per 10,000 adults in the UK at 767, followed by 803 in Northern Ireland, 839 in Wales, 1,072 in England and 1,028 in the UK as a whole⁸. Following the same composition of the rest of the UK, last year the two largest industries in Scotland were 'Professional, Scientific & Technical Activities' (53,450 enterprises) and 'Construction' (48,135 enterprises). Together, these two sectors assemble 28.1 per cent of all private sector enterprises in Scotland.

The industrial structure of any economy is a key determinant of both its economic performance and the nature of its growth. Scotland has witnessed a shift in recent decades towards services, such as business services and finance, and away from manufacturing.

⁴ Scottish Enterprise & Scottish Annual Business Statistics database

⁵ Scottish Government Quarterly National Accounts Scotland, 2015 Q4

⁶ Figure derived from UK overseas Scotch whisky exports, sourced from [HMRC Overseas Trade Statistics 2015](#), and Scotland's overseas food exports, sourced from [HMRC Regional Trade Statistics 2015](#)

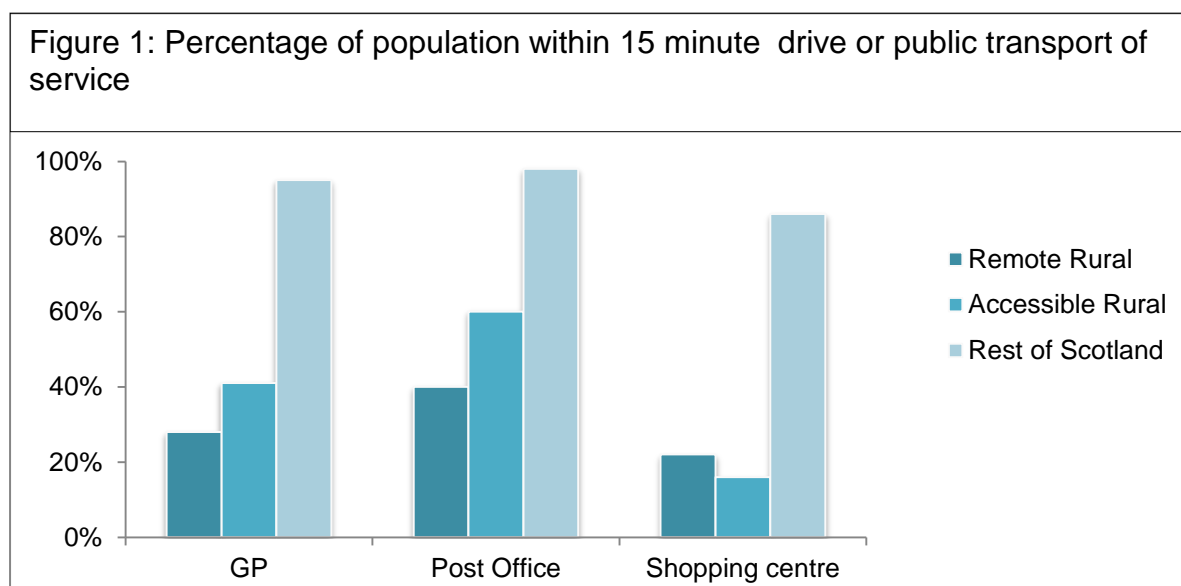
⁷ Scottish Government, [Businesses in Scotland](#), March 2015 figures released on 3 November 2015

⁸ UK Government, [Business population estimate for the UK and regions: 2015 statistical release](#), released 14 October 2015

Geographic Context

Rural Scotland accounts for 98 per cent of the land mass of Scotland but only 18 per cent of the population; the rest of Scotland accounts for 82 per cent of the population and only two per cent of the land mass. Over recent years, the population of rural Scotland has continued to grow at a faster rate than the rest of Scotland, driven by the increase in accessible rural areas, mainly due to inward migration.⁹

There are significant benefits to living in rural Scotland. A higher proportion of residents of rural Scotland, compared to the rest of Scotland, rate their neighbourhood as a 'very good' place to live. However, rural consumers face a number of challenges. In terms access to services, more people in rural areas are outwith a reasonable drive time to key services compared with the rest of Scotland. Figure 1 shows that the percentage of rural consumers that have to drive over 15 minutes to reach essential services is considerable.



In general, a lower percentage of people in rural areas find key services convenient when compared to the rest of Scotland. This is particularly noticeable for essential services such as hospitals, dentists, chemists, public transport and banking services. For example, 58 per cent of residents of remote rural areas find public transport convenient compared to 89 per cent of residents in the rest of Scotland.

Residents in rural areas are, in general, less likely to be satisfied with public transport with 29 per cent of remote rural residents dissatisfied with the quality of public transport, compared with 12 per cent in the rest of Scotland.

⁹ Scottish Government, [Rural Scotland Key Facts 2015](#)

Residents in rural areas are also more likely to be in fuel poverty¹⁰. The proportion of households in remote rural Scotland which are classed as extreme 'fuel poor' is more than double that of the proportion in the rest of Scotland (22 per cent compared to 9 per cent). Almost two thirds of households in remote rural Scotland are classed as 'fuel poor', while nearly half of households in accessible rural Scotland are in fuel poverty. In contrast, in the rest of Scotland 64 per cent of households have been classed as 'not fuel poor'.

Social Context

The population of the United Kingdom in 2014 was 64.6 million with the population of Scotland representing 8 per cent of the total population (5.3 million people).¹¹ Between 2004 and 2014 the percentage of the population in Scotland aged between 60-74 has increased by 17 per cent as has the percentage of the population over the age of 75.¹² The ageing of the Scottish population means that there is an increasing number of potentially vulnerable consumers who need effective protection when purchasing goods and services.

Ensuring that the benefits of economic growth are equally shared across society is important to boost the overall growth. Of the 34 OECD countries, the UK ranked 6th worst in terms of income inequality, while Scotland ranked 16th.

The social make up of Scotland is different to that of the rest of the UK. In Scotland, the cost of living is lower than elsewhere in the UK: the average weekly household expenditure in Scotland between 2010-12 was £427.30 compared with £491 in England¹³. However, this corresponds to a significantly lower median household wealth in Scotland compared to the rest of the UK. In 2014 the median household wealth was £186,600 in Scotland compared with £225,100 across Great Britain.¹⁴

Deprivation may also impact on consumer experiences. In 2013-14, 15 per cent of people in Scotland were in absolute poverty, with 20 per cent in absolute poverty after housing costs.¹⁵ For these consumers, essential services reflect a significant proportion of their income and so it is essential to ensure that competition is working well. For example, in the energy market a person is said to be living in fuel poverty if, in order to maintain a satisfactory heating regime, they would need to spend more than ten per cent of their household income. The estimated rate of fuel poverty in Scotland in 2014 was 34.9 per cent.¹⁶

Spending on essential services, therefore, can represent a significant proportion of consumers' household expenditure, especially for vulnerable consumers. Figure 2

¹⁰ A household is defined as being in fuel poverty if it would be required to spend more than 10 per cent of its income on all household fuel use. 'Extreme fuel poverty' is defined as a household having to spend more than 20 per cent of its income on household fuel.

¹¹ ONS, [Annual Mid-year Population Estimates: 2014](#), June 2015

¹² National Records of Scotland, [Scotland's Population: The Registrar General's Annual Review of Demographic Trends 2014](#)

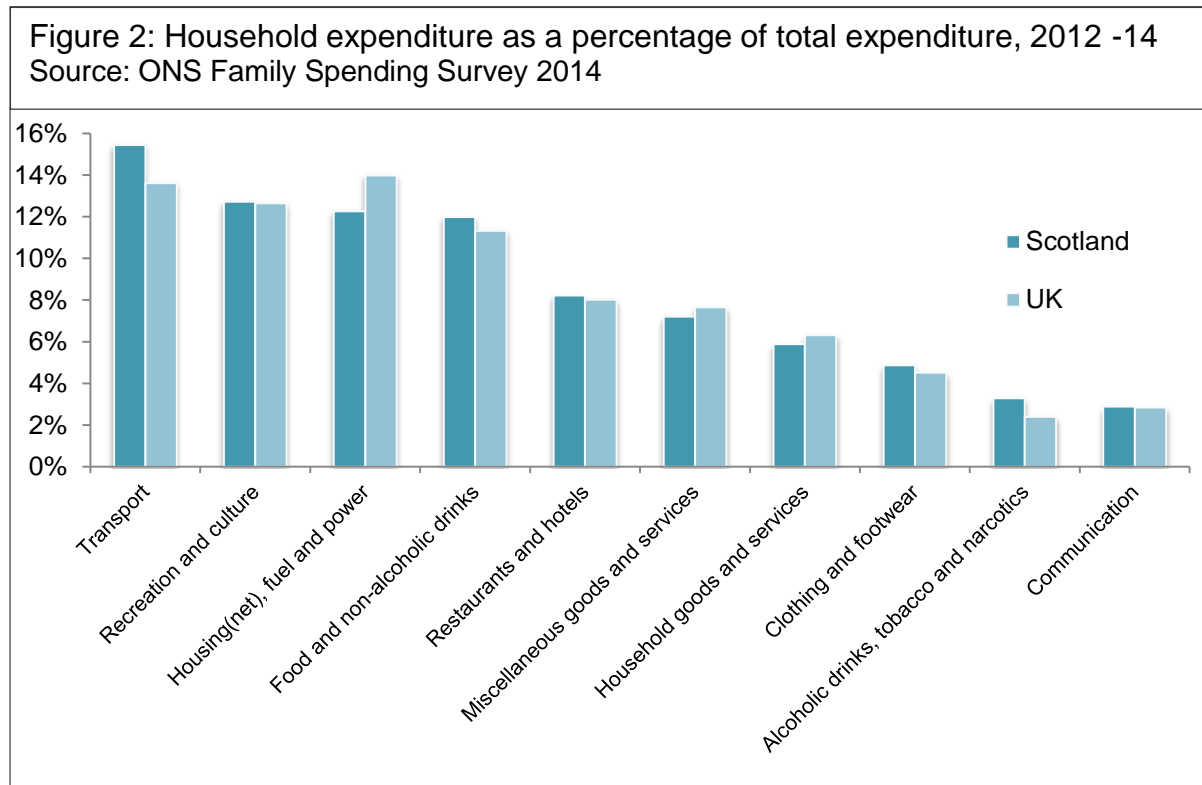
¹³ ONS, [Compendium of UK Statistics Social Indicators](#)

¹⁴ ONS, [Wealth and Assets Survey 2014](#)

¹⁵ Scottish Government, [Relative Poverty in Scotland 2013-2014](#)

¹⁶ Scottish Government, [Fuel Poverty](#)

below shows the expenditure of Scottish households on different goods and services. Expenditure on transport represents a large percentage of consumers' expenditure, with housing costs also representing a significant proportion of household spending.



Household expenditure varies significantly between income groups. Across the UK in 2014, lower income households spent a higher proportion of their total expenditure on food and drink than higher income households: on average, households with the lowest ten per cent of incomes spent 17 per cent of total expenditure on food and non-alcoholic drink, compared with seven per cent for the highest ten per cent of incomes. Similarly, low earning households spent nine per cent of total expenditure on electricity, gas and other housing fuels compared with three per cent for the highest income households.¹⁷

Household expenditure in rural areas (£567.80) was significantly higher than in urban areas (£498.40). The biggest difference in expenditure was in transport where the average weekly expenditure in rural areas was £89.20 compared with £64.70 in urban areas. This is of particular importance given Scotland's geographic landscape and likely reflects lower availability of public transport in rural areas and longer journeys to access services and amenities.¹⁸

¹⁷ONS, [Family Spending 2015: A Report on the Living Costs and Food Survey 2014](#), Chapter 3

¹⁸ONS, [Family Spending 2015: A Report on the Living Costs and Food Survey 2014](#), Chapter 1

ACTION: Currently, evidence on the variation of expenditure by income, age and area is only available for the UK as a whole. The Scottish Government will seek to gain a better understanding in the variation in consumer spending based on an individual's social, geographic and economic circumstances.

EVIDENCE GATHERED FROM STAKEHOLDERS

Our evidence gathering highlighted several markets which might not be working well for Scottish consumers. The following section highlights some of the key issues that have been raised that we will now consider in more detail. We will work closely with key stakeholders and Scottish Government colleagues in order to address the areas identified in the assessment through our action plan.

CONSUMERS AND BUSINESSES IN SCOTLAND

Businesses

Open and competitive markets together with effective competition policy have the ability to drive economic growth. In a well-functioning market, consumers give businesses a clear indication of their preferences. As a result, businesses that provide products that consumers want will prosper while others will not.

Competition puts businesses under pressure to offer the best products at the best possible price. This provides firms with strong incentives to improve productivity, reduce prices and to innovate. As a consequence, consumers should have a wider choice, lower prices and higher quality goods. The aim of competition policy is to address areas where markets are not necessarily delivering the best outcomes for consumers.

The CMA reviewed evidence and found that competition drives productivity in three ways:

- competition acts as a disciplining device, placing pressure on managers of firms to become more efficient;
- competition ensures that more productive firms increase their market share at the expense of the less productive; and
- competition drives firms to innovate, coming up with new products and processes which can lead to increases in efficiency.¹⁹

ACTION: The Scottish Government will seek to gain a better understanding of the links between productivity and competition with the aim of developing metrics to measure this relationship.

Businesses' Awareness of Competition Policy and Law

During 2015, the CMA undertook both quantitative and qualitative research into businesses' awareness of competition law.²⁰ This research found that the majority (77 per cent) of businesses either did not know competition law very well or hadn't heard of it at all, with awareness particularly low amongst small and medium enterprises. Whilst the proportion of Scottish businesses with a strong awareness of

¹⁹ CMA, [Productivity and Competition – A Summary of Evidence](#), July 2015

²⁰ CMA, [SMEs & Competition Law – Qualitative Research Report](#) (Prepared by BDRG Continental for the CMA), May 2015

competition law (27 per cent) was higher than the UK average (23 per cent), this low level of awareness highlights that further work is needed.²¹

The CMA has launched a campaign to increase awareness of competition amongst businesses.²² However, the Scottish Government believes that more can be done at a Scottish level to increase businesses' engagement with competition law and policy.

ACTION: The Scottish Government will work with business organisations to carry out research into Scottish businesses' attitudes to competition and competition issues and will consider how to engage businesses more in competition matters.

Disruptive Technologies and the Sharing Economy

Technology changes the way we do things and disruptive technologies transform markets by innovating and allowing for the more efficient use of resources. Whilst disruptive technologies (or innovation) and the sharing economy are not the same, the impact that these alternative business models will have on markets are similar.

'Disruptive Innovation' has been defined as 'the phenomenon by which an innovation transforms an existing market or sector by introducing simplicity, convenience, accessibility, and affordability where complication and high cost are the status quo.'²³ Whilst the sharing economy – where individuals share human and physical resources – allows people to utilise unused or underused assets, allowing individuals to make money by sharing resources, time and skills across online platforms.²⁴

As access to technology, in particular mobile technology, has rapidly increased, the development of disruptive technology and the sharing economy has become more prominent in many sectors of the economy, changing the way consumers purchase goods and services. A key characteristic of disruptive technologies is the speed with which they transform markets. This is particularly important when compared with the speed of legislation and changes to regulations. This means that Government and regulators need to be agile in their response to changes to markets. As shown in Figure 3, disruptive technologies have had a significant impact across sectors and are likely to continue to do so.

²¹ CMA, [UK Businesses' Understanding of Competition Law](#) (Prepared for the CMA by IFF Research) March 2015

²² CMA, [Competing fairly in business: at-a-glance guide to competition law](#)

²³ Professor Clayton M Christensen, *The Innovator's Dilemma*, 1997

²⁴ UK Government, [Unlocking the sharing economy – an independent review by Debbie Wosskow](#), November 2014

Figure 3: Examples of Disruptive Technologies

Source: IBM

Uber: The world's largest taxi company owns no taxis**Airbnb:** The largest accommodation provider owns no real estate**Skype:** The largest phone company owns no telecoms infrastructure**Facebook:** The most popular media owner creates no content**Netflix:** The world's largest movie house owns no cinemas**Apple & Google:** The largest software vendors do not write the apps

Disruptive technologies bring significant benefits to consumers, competition and the economy through lower prices, greater choice and better service. PwC has calculated that, on a global basis, the sharing economy is currently worth £9 billion and this is set to rise to £230 billion by 2025.²⁵ Furthermore, disruptive technologies allow for a more efficient use of underused resources by allowing people to share their resources through online platforms. This also allows individuals to benefit from more flexible working arrangements as well as new ways of supplementing their incomes.²⁶

However, these benefits must be balanced with the need for regulation and for these new businesses and traditional operators to be treated fairly with no unfair competitive advantage. A key element of debate surrounding disruptive technologies is the degree to which they should be regulated. Often, market structures and regulation can create barriers to new entrants. Where there are such barriers to entering a market, these regulations and structures should be reviewed to ensure that they encourage competition and, consequently, increase consumer choice. It is important that consideration is also given to regulation which may have become obsolete or may discourage innovation in the market. Regulation must be proportionate, encourage innovation and provide a favourable business environment in which all companies can grow and flourish.

On the other hand, new businesses are often competing with existing providers but are not necessarily bound by the same rules and regulations. The existence of a regulatory gap between new and incumbent operators can lead to an issue of market fairness. It is also likely that new technologies may disrupt a market and quickly become the dominant firm in this market. Key examples of this include Google and Facebook. Dominance in itself is not an issue, but firms must be monitored closely to ensure that there is no abuse of this dominant position.

Disruptive technologies bring significant benefits for consumers through greater choice and lower prices. However, these benefits must be balanced with the need to protect consumers. In particular, it is important to ensure that health and safety

²⁵ PwC, [Five key sharing economy sectors could generate £9 billion of UK revenues by 2025](#), August 2014

²⁶ Institute of Economic Affairs, [Regulatory Approaches to the Sharing Economy](#), 2016

standards are in place and that consumers are given sufficient information to make an informed choice in these markets.

Further analysis is needed to understand where the balance is between encouraging competition and ensuring regulation is appropriate to ensure there is no competitive advantage nor unintended consequences. The Scottish Government will be looking at the issues around disruptive technologies in detail in the coming months. Specifically on regulation, the independent Regulatory Review Group is also undertaking a review of the regulatory environment within Scotland for key sectors affected by digital disruption to ensure that it remains appropriate to encourage and support innovation while maintaining a level playing field.

Disruptive technologies transform current business models. In Scotland, we must ensure that Scottish businesses are able to capitalise on these disruptions and have the necessary tools and ability to enter these markets should they wish to. It is also important to ensure that market structures and features are not unnecessarily restricting the entry of new disruptive business models.

ACTION: As part of a wider package of work considering the balance between competition and regulation, the Scottish Government will carry out research to consider how to ensure Scottish businesses are able to make the most of the arrival of disruptive technologies and that market structures do not unnecessarily restrict the entry of new disruptive business models.

Consumers

Our stakeholders in the consumer landscape have provided a wealth of data on the experiences of Scottish consumers, particularly in relation to how Scottish consumers fare in comparison to those in the rest of the UK. Whilst not all consumer issues will be the consequence of competition concerns, understanding those areas where Scottish consumers face detriment and suffer harm will be key to ensuring markets work well in the interests of consumers, businesses and the Scottish economy. Empowered consumers drive firms to compete. Consumers help increase competition by purchasing goods from the business that offers them the best combination of price, features and quality. Businesses that do not meet the needs of consumers will be forced to change their product or leave the market.

Scottish Consumers' Experiences

Insight from consumer stakeholders shows that essential services, such as energy, transport and banking are those which consumers experience the most issues with, reflecting both the importance of these services to everyday life of Scottish consumers and ensuring that the Scotland's economic, geographic and social make-up does not result in gaps in access to or choices in these sectors.

Data from Ombudsman Services, an ombudsman service that provides dispute resolution across a number of sectors, found that²⁷:

- There were 5.1 million consumer complaints in Scotland in 2015.

²⁷ Ombudsman Services, [Consumer Action Report - Scotland](#), 2016

- The number of consumer complaints varied considerably by region in Scotland from 3.05 complaints per head in the West of Scotland to 2.34 in the South of Scotland (Figure 4).
- The most common sectors for complaints in Scotland were retail (35 per cent of complaints), telecommunications (17 per cent), energy (11 per cent) and banking (7 per cent). As Figure 5 shows, this differs slightly from consumer experiences in the UK as a whole.

Figure 4: Complaints by region, Scotland (2015)
Source: Consumer Action Monitor, Ombudsman Services

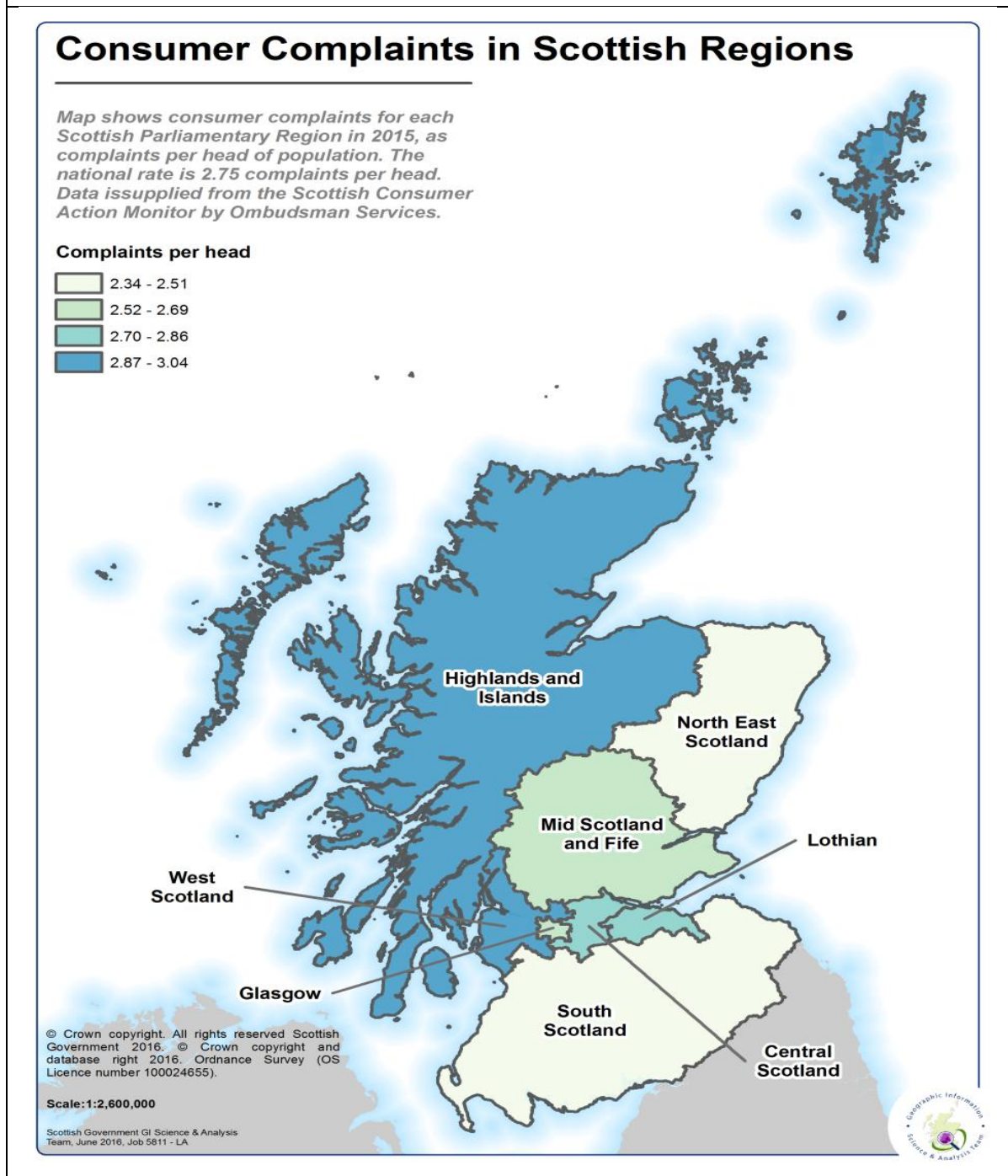
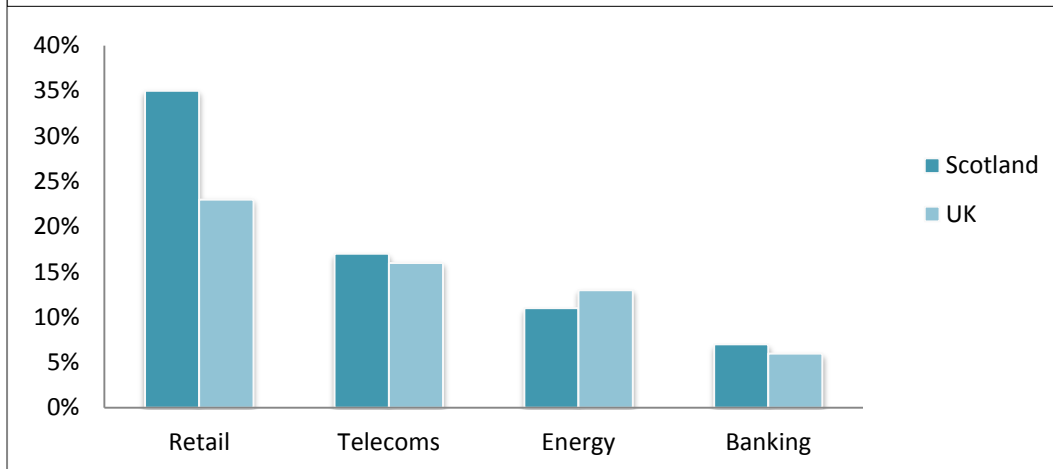


Figure 5: Complaints by sector, Scotland and the UK (2015)
 Source: Consumer Action Monitor, Ombudsman Services



In order to develop a strategy for consumer protection and competition that ensures that informed and empowered consumers make the most of competitive markets and encourages and rewards businesses which are innovative, efficient and fair, the Scottish Government needs to develop knowledge and understanding of the thinking and influences of Scottish businesses and consumers. There is a perception that Scottish consumers tend to behave differently to consumers in other parts of the UK. In particular, it is believed that Scottish consumers are more likely to be loyal to a particular brand. For example the findings of the CMA energy market investigation found that Scotland and Wales appeared to show higher degrees of incumbent brand loyalty.²⁸

ACTION: The Scottish Government will consider whether the demographic and geographic circumstances of Scottish consumers have an impact on their behaviour or whether there is a cultural tendency for Scottish consumers to be more loyal to Scottish brands, particularly in the regulated sectors.

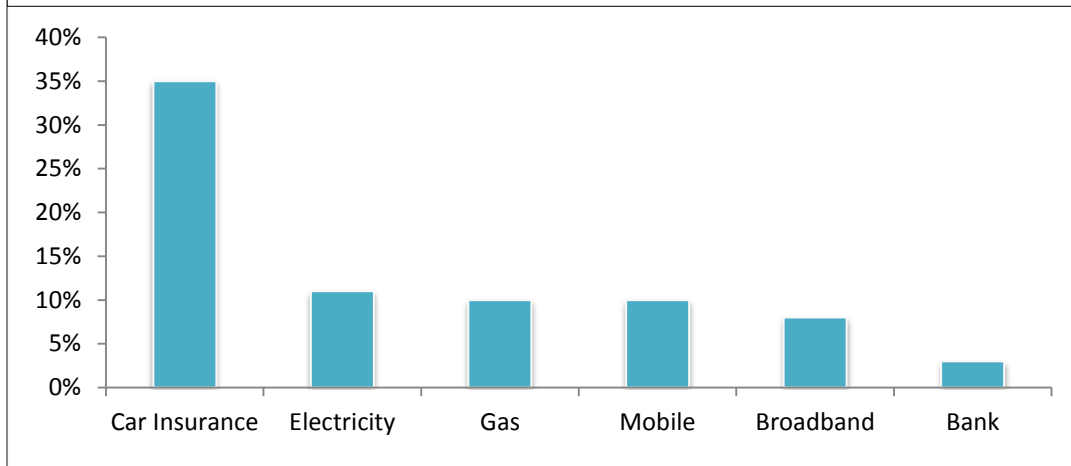
Consumer Switching in the Regulated Sectors

In order for competitive markets to function effectively, consumers need to be actively engaged in markets in order to place competitive pressure on businesses. Across sectors, consumer switching remains relatively low, particularly in the regulated sectors of energy, telecoms and banking. Figure 6 below shows the proportion of consumers that switched utility supplier in the last 12 months.

²⁸ CMA, [Energy Market Investigation: Summary of Final Report](#), June 2016, page 29

Figure 6: Proportion of UK consumers who have switched utility supplier in the last 12 months (2015)

Source: Ofcom, The Consumer Experience 2015



The Scottish Government held a stakeholder event in July 2015 which considered whether there is a need for a specific Scottish approach to consumer switching. There was consensus amongst participants that consumer switching appears to be a particular issue in Scotland. For example, the findings of the CMA energy market investigation found that there were lower levels of consumer engagement in the market in Scotland than in England.²⁹ This may, in part, be due to a higher rate of incumbent brand loyalty in Scotland. However, we are keen to gain a better understanding of why levels of engagement appear to be lower in Scotland in the regulated sectors than in England.

A key underlying principle is that not all consumers are the same and that different consumer characteristics lead to different switching behaviour. Therefore, different policy responses will be needed for different types of consumer. While price comparison websites provide a useful service for most consumers, for example, vulnerable consumers often do not have access to them and so may lose out.

We want to gain a better understanding of the barriers that consumers in Scotland face when switching and how better provision of information might encourage greater switching.

ACTION: The Scottish Government will undertake a survey to establish the extent of switching and the barriers that consumers face. We will use the results from this survey to identify the characteristics of different types of switchers with the aim of developing targeted policy interventions.

Vulnerable Consumers and Rural Issues in the Regulated Sectors

While competitive markets bring significant benefits to consumers, in certain sectors network effects or economies of scales cause circumstances such as natural monopolies (typically with high fixed costs and lower marginal costs) which limit the prospects for effective competition and so there is a need for regulation.³⁰ In such

²⁹ CMA, [Energy Market Investigation: Summary of Final Report](#), June 2016, page 29

³⁰ Department for Business Innovation and Skills, [Principles for Economic Regulation](#), April 2011

circumstances, it is essential to have effective, independent economic regulation which will promote effective competition, where possible, but will also promote the interests of consumers through the provision of good quality, good value, reliable services.

The Scottish Government defines a consumer as ‘anyone who buys goods or digital content, or uses goods or services either in the private or public sector, now or in the future.’³¹ It is important to note that a consumer’s circumstances can change rapidly and any consumer can, temporarily, become a vulnerable consumer. For example, a customer may face a bereavement or illness that puts them in a vulnerable position for only a short period of time. A vulnerable consumer, therefore, is a consumer whose personal circumstances or characteristics mean that they are especially likely to face detriment or face greater detriment than other consumers. A vulnerable consumer is also less likely to be able to protect their own interests when purchasing goods or services. In Scotland, a greater number of these consumers face detriment due to higher levels of deprivation and rurality.

In the regulated sectors, there are various competition issues that cause significant detriment to consumers, particularly vulnerable consumers, as seen in the CMA’s current investigations into the retail banking and energy markets. However, even in areas where competition may be working well at a UK level, our evidence shows that there are specific market failures in Scotland due to its demographic and geographic landscape. These specific challenges can be seen in the different sectors discussed below.

Telecommunications

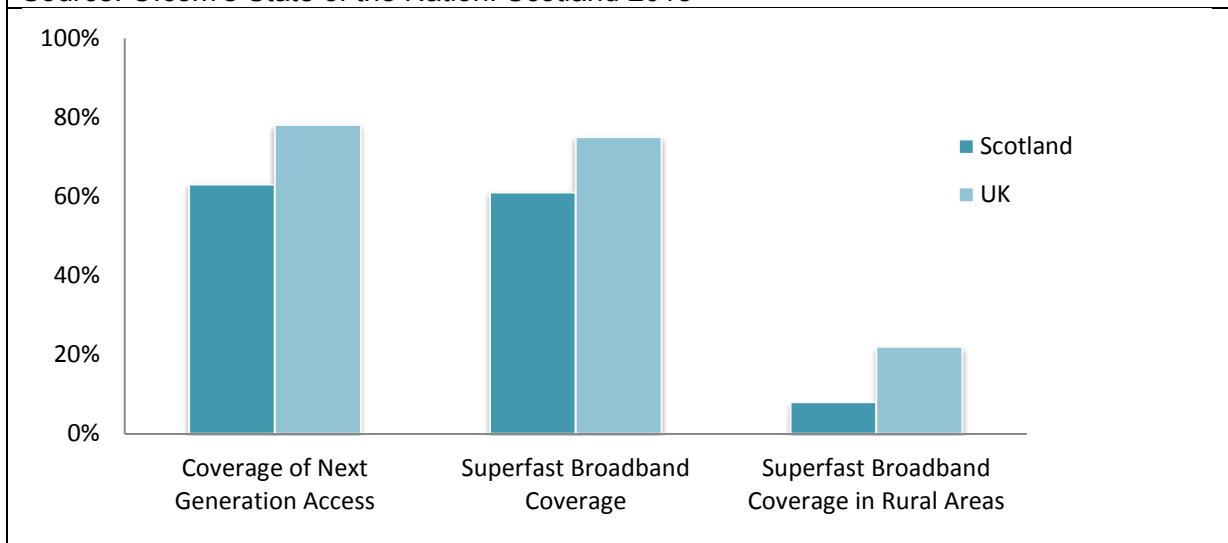
The focus of the UK’s regulatory approach in recent years has been to promote effective and sustainable competition. This has proved successful in large parts of the UK; but not in others. In areas where there is limited competition – a definition that could apply to large areas of Scotland – good consumer outcomes have often been lacking and the regulatory environment has not been able to incentivise or ensure the necessary investment to maintain or upgrade network infrastructure. As a result, an infrastructure deficit has been created over time, which has resulted in variable availability and quality of service across the country leading to a lack of consumer choice in some areas.

The Next Generation Access (NGA) broadband market in Scotland provides a useful illustration of the lack of competition in Scotland (as seen in Figure 7) and shows the lower levels of coverage in Scotland compared to the rest of the UK. There are effectively two commercial suppliers – BT Openreach and Virgin Media. Ofcom’s 2015 Communication Market Report for Scotland suggests that 75 per cent of premises in Scotland are able to receive Openreach fibre broadband services and 36 per cent are able to receive Virgin Media cable services. Very few areas have a choice between the two with no competition outside of the major cities and nothing north of Dundee.

³¹ Scottish Government, [Definition of a Consumer](#)

Although investment from the Scottish Government, and other public sector partners, is helping to extend coverage, this demonstrates that the market does not operate in the same way across the whole of the UK. Ofcom recently undertook a Strategic Review of Digital Communication and published their initial conclusions in February 2016. These include proposals to reform the UK telecoms market by encouraging more competition, reforming Openreach, imposing tougher performance targets and improving quality of service. It remains to be seen whether these measures will address market failure in areas where there is little or no competition at both the infrastructure and services layer.

Figure 7: Broadband coverage in Scotland and UK, 2015
Source: Ofcom's State of the Nation: Scotland 2015



Energy

The CMA's energy market investigation has identified a number of features of the market (in both generation and retail supply) that give rise to an adverse effect on competition and has proposed a number of remedies to address these features. The CMA's final report³² identified overall consumer detriment of £2 billion in 2015.

The issues faced by Scottish consumers in the retail energy market are similar to those faced by consumers in other parts of Great Britain. However, Scottish Government analysis has highlighted that the retail energy supply market in Scotland is relatively more concentrated than in Great Britain as a whole and exhibits a number of characteristics which may mean that suppliers are able to segment the market and offer different terms to certain groups for both behavioural and structural reasons. For example:

In Scotland, 20 per cent of electricity consumers are on prepayment meters compared with 16 per cent nationwide.³³ The figure below shows the average unit costs for different types of payment methods. The average unit cost for domestic standard electricity in the North of Scotland is higher across all three methods of payment than that of South of Scotland and UK average.

³² CMA, [Energy Market Investigation: Modernising the Energy Market](#), June 2016, page 6

³³ [DECC Quarterly Energy Prices March 2016](#), Table 2.4.2

Figure 8: Average Annual Domestic Standard Electricity Bills 2015
 Source: DECC Quarterly Energy Prices December 2015, Table 2.2.3

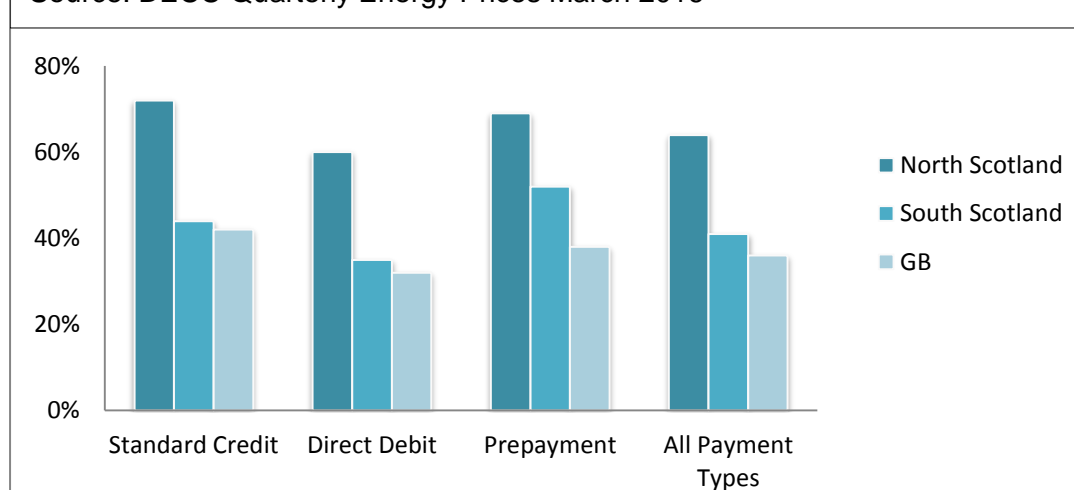
Average Unit Cost	Standard Credit	Direct Debit	Prepayment
North Scotland	17.5	16.1	17.5
South Scotland	15.9	14.4	15.8
UK	16.2	14.7	16.3

Prepayment meter customers face bills that are 10.5 per cent higher than direct debt payments. These issues are exacerbated by the fact that average consumption is higher in the North of Scotland. Consumers with dynamically teleswitched meters operating in dynamic mode, all of which are located in Scotland, are not able to participate fully in the retail energy market and face particularly strong barriers to switching supplier and/or tariff.³⁴

The CMA also found that consumers in Scotland are less likely to have been active in the market against key indicators of engagement than those in England.

Department of Energy and Climate Change data shows that electricity consumers in Scotland are more likely to be with their home supplier (the original supplier in a given area) compared with other British consumers, as shown in the figure below. However, gas consumers in the North of Scotland are less likely to be with their home supplier than the GB average.

Figure 9: Percentage of Customers on Home Electricity Supplier
 Source: DECC Quarterly Energy Prices March 2016



The remedies proposed by the CMA need to continue to be assessed in the Scottish context to determine their potential impacts. The extent to which Scottish consumers respond to changes in the market is a critical factor in assessing how successfully the package of interventions will tackle consumer detriment in the Scottish context.

³⁴ CMA, [Energy Market Investigation: Provisional Decision on Remedies: Appendix 3.1: Restricted Meters](#), March 2016

It is important to understand whether there are characteristics of Scottish consumers that make them inherently less likely to switch and therefore which policy interventions could increase the likelihood of switching. Our proposed research on switching will go some way to addressing this but further action may be necessary in the complex energy market.

Delivery Charges

The OFT's 2012 report, *Price and Choice in Remote Communities*, highlighted the issues of poor service and high charges for delivery, especially to the Highlands and Islands of Scotland, with concerns about the cost of delivery, suppliers refusing to deliver to remote locations, delivery times, misleading use of the term 'Free Mainland Delivery' and the unnecessary use of delivery services other than Royal Mail or alternative delivery hubs which might be cheaper.

In response to these and similar concerns, the Statement of Principles for parcel deliveries was launched by the Minister for Business, Energy and Tourism in November 2013. It sets out best practice principles for retailers to provide delivery services that meet the needs of their customers.³⁵ Although voluntary, the principles will help to support businesses, and lead to improvements in the number of customers abandoning purchases that they would otherwise have made.

In Citizens Advice Scotland's (CAS's) report, *The Postcode Penalty: The Distance Travelled*³⁶, published in September 2015, they reviewed the extent to which retailers' practice has improved since CAS's previous survey in 2012. The report looked at surcharges, exclusions and the variance between different retailers in their practice. While some improvements were noted, it still found that customers were facing disproportionate restrictions when it came to the delivery of their purchases.

ACTION: The Scottish Government will continue its discussions with stakeholders to explore a range of sustainable solutions for rural communities.

Current Investigations

The CMA is currently undertaking market investigations into the energy and banking markets and has recently published proposals for competition in rail, while Ofcom has recently undertaken a review of digital communications. Many of these investigations may address the competition issues faced by Scottish consumers, and the Scottish Government will work closely with economic regulators and the CMA to implement and recommended changes to the market.

ACTION: The Scottish Government will continue to ensure on-going competition and regulatory investigations and studies take sufficient account of Scottish issues.

Potential Competition Issues in Areas of the Scottish Economy

³⁵ Scottish Government, [Parcel Delivery in Remote and Rural Areas](#)

³⁶ Citizens Advice Scotland, [The Postcode Penalty: The Distance Travelled](#), 2015

Scottish Legal Framework

The distinct nature of the Scottish legal system means that related market failures in Scotland and detriment faced by Scottish consumers may be different from other UK jurisdictions. Therefore, it is important that these issues are highlighted in order to ensure that there is no undue detriment to Scottish consumers.

Property Market

Tenement housing is a far greater component of the Scottish property market than in the rest of the UK with 34 per cent of households living in purpose-built blocks of flats or tenements³⁷ compared to 16 per cent in England and Wales.³⁸

In 2009, the OFT carried out a market investigation of property managers in Scotland.³⁹ It found that although 70 per cent of those surveyed were happy with their property manager, a significant minority were not. It found issues in three main areas:

Switching

The OFT found very low levels of switching in the market; even when compared with sectors like banking where switching has typically been low. The switching of a property factor requires collective agreement from home-owners. The majority of consumers believed that they did not have sufficient knowledge of the switching process and one-third of consumers felt that the service they received from their property manager was not good value for money.

Barriers to Switching

Secondly, there were situations where it was particularly difficult for consumers to switch:

- Owner occupiers in ex-local authority properties within a predominantly social housing development are required to use the social housing landlord's property manager.
- A property manager is appointed by a developer on the completion of a new development to manage that site for a number of years.
- More generally title deeds (and deeds of conditions) may make it difficult to dismiss the incumbent property manager. However, the Title Conditions (Scotland) Act 2003 contains an overriding power for a two-thirds majority of owners to dismiss the factor.⁴⁰

Complaints Mechanism

Thirdly, the OFT found that owners with a complaint had limited scope for redress. When using the property manager's own complaints system, many were left with the issue either unresolved or with an unsatisfactory response. The absence of advice

³⁷ Scotland's Census 2011, [Key Results on Households and Families, and Method of Travel to Work or Study in Scotland](#)

³⁸ ONS, [2011 Census: Key Statistics for England and Wales](#), March 2011

³⁹ OFT, [Property Managers in Scotland – A Market Study](#), February 2009

⁴⁰ [Title Conditions \(Scotland\) Act 2003](#) s64

and information and an effective system of redress meant that there was inadequate protection for consumers.⁴¹

Changes in the Property Factors Market

The Property Factors (Scotland) Act 2011 established a system of redress in the form of the Homeowner Housing Panel and a code of conduct for property factors which sets out minimum standards of practice. The code of conduct requires property factors to give all homeowners for whom they act a written statement of services including information as to the services to be provided, the fee to be charged and, importantly, clear information on how to change or terminate the service contract.⁴²

Current Issues in the Market

Although the introduction of an effective system of redress is a significant improvement in the property factors market, problems still exist. There are still very low levels of awareness and engagement with the market which also means that there is a lack of competitive pressure on property factors which could lead to higher prices and lower service levels.

ACTION: In order to counter this, we have planned a public facing guidance on the provisions of the Title Conditions (Scotland) Act 2003 on the dismissal and replacement of property factors. This will ensure that consumers are better informed of their choice.

Legal Services

The CMA is currently carrying out a market study into legal services in England and Wales and it will be important to see how their findings may also apply to the Scottish market. The CMA plans to examine three key issues:

- whether consumers can drive effective competition by making informed purchasing decisions;
- whether consumers are adequately protected from potential harm or can obtain satisfactory redress if legal services go wrong; and
- how regulation and the regulatory framework impact on competition for the supply of legal services.⁴³

The Scottish Government is currently considering the provision of consumer advocacy and redress for legal services and will examine similar issues to those of the CMA as well as considering how their findings may apply to the Scottish market.

In particular, there are concerns regarding consumers' awareness of the provision of unregulated legal services. Certain areas of the law are reserved to solicitors who must be regulated by the Law Society of Scotland. Other areas, however, are not reserved meaning that advice and representation can be handled by unregulated firms or a person who is not qualified to provide the service. Unregulated areas of the law include employment law, family law, personal injury and consumer matters. Consumers who purchase legal services in the unregulated legal sector are not

⁴¹ OFT, [Property Managers in Scotland – A Market Study](#), February 2009, page 63

⁴² Professor Kenneth G C Reid and Professor George L Gretton, *Conveyancing 2011*, page 114

⁴³ CMA, [Legal Services Market Study](#)

offered the same protection as those in the regulated sector and are not covered by the Law Society's Indemnity Policy or Client Protection Fund nor by the Scottish Legal Complaints Commission.

Consumers, therefore, may be exposing themselves to potential harm, should something go wrong. In order for the legal market to function effectively, consumers should be empowered to make informed decision on the best product for them. However, the majority of consumers do not realise that not all legal services are regulated and so these consumers are not able to make an informed choice of service.⁴⁴

ACTION: The Scottish Government will ensure that consumers are sufficiently informed about the difference between regulated and unregulated legal services.

Localised Markets

In determining markets in which there may be specific detriment to Scottish consumers, one of the key consideration is whether or not the market is local to Scotland. It is key for the Scottish Government to gain an understanding of the features of these markets in order to be able to identify any competition concerns that are specific to Scotland. Examples of markets that are likely to be localised include perishables, heavy, low value, uneconomic to transport long distances or areas that are devolved to Scotland.

ACTION: The Scottish Government will work with key partners to undertake scoping research to establish the features of localised markets.

Empowering Consumers in Public and Private Markets

Well-informed consumers are a critical part of a functioning market. In both public and private markets, consumers often face complex decisions without clear information about prices and services available. Asymmetric information can act as a barrier to the effective functioning of a market. An important element of empowering consumers and ensuring that markets function effectively is making sure that they have sufficient information about the product they are buying and are able to use this information to compare between firms and products. However, in many markets the information may be complex or difficult to find, making it hard for consumers to make informed decisions.

Similarly, although choice can be used in public service markets as a way of improving performance and increasing the say that individuals have over the services they access, consumers often face complex decisions. In making decisions, consumers are faced with certain barriers: there is low awareness about the ability to choose, low ability to assess the information and make an informed choice and lack of capability to act.⁴⁵ There are also instances where it is inappropriate for consumers to have a choice in public services. For example, consumers are not in a

⁴⁴ The Law Society of Scotland, [The Solicitors \(Scotland\) Act 1980: The Case for Change](#)

⁴⁵ OFT, [Choice and Competition in Public Services – a Guide for Policymakers](#) (prepared by Frontier Economics for OFT)

position to make an informed decision about the medical treatment they require. GPs, therefore, are necessary to act on behalf of the patient to ensure they get the appropriate care.⁴⁶ A balance, therefore, is needed between providing consumers with a choice and ensuring that they are protected.

ACTION: The Scottish Government will consider how best to provide consumers with the information needed to make informed decisions in complex and difficult markets such as health and social care.

Transport

The provision of public transport is an area where competition, regulation and public provision must be carefully balanced. Public transport is an essential service for many consumers in their daily life. In particular in rural areas, access to affordable and reliable public transport is needed in order to provide people with access to services such as health, education and work.

Competition in transport services can bring benefits to consumers. Greater competition typically gives consumers greater choice of service at lower prices. However, competition can also lead to a lack of supply in rural areas or unprofitable, but necessary, routes. Some forms of transport, such as rail, have characteristics which raise issues that need to be addressed for competition to be feasible. In such cases, competition for the market in the form of franchise agreements ensures that consumers get a good quality service at a reasonable price.

As markets for transport in Scotland are complex and often involve lifeline services, it is important that consumers receive an affordable and reliable services. As the issues in these markets are so complex, detailed work is needed to assess whether there are any that may cause detriment to consumers. The Scottish Government will carry out further research in to transport services in order to consider whether markets are working effectively for consumers.

In all transport markets, whether there is public provision or competition (for or in the market), it is important to ensure the services are working well for consumers and that consumers are confident and knowledgeable. In order to protect and empower consumers, their views must be represented through effective advocacy and there must be clear routes to redress. Effective redress helps to inform competition policy as complaints data, when properly harnessed and aggregated, can identify problem areas within markets, or even specific areas of detriment.

ACTION: The Scottish Government will consider whether there is adequate provision of consumer advocacy and redress as the first stage of our in depth research into transport services in Scotland.

⁴⁶ City University London, [Public Service Markets: Their Economics, Oversight and Regulation](#), December 2014

CONCLUSIONS

The devolution of certain competition powers gives the Scottish Government the opportunity to ensure that Scotland's markets are competitive and fair to consumers and to highlight where markets are not working well for consumers. The Scottish Government will work closely with stakeholders to ensure that areas of current or potential detriment to Scottish consumers are highlighted and that solutions are found.

The Strategic Assessment of Markets in Scotland is our first step in highlighting markets where there may be detriment to Scottish consumers. Specifically, the Assessment identifies areas of specific detriment to Scottish consumers due to our distinct economic, geographic and social circumstances which may mean that problems faced by Scottish consumers are different to other parts of the UK.

The findings of the Strategic Assessment of Markets in Scotland will inform the Scottish Government's work in the short to medium term. This Assessment contains actions that the Scottish Government will take forward in order to address market failures in Scotland. In taking action on these issues, the Scottish Government will work in close partnership with stakeholders to address the detriment to Scottish consumers.



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