

## **Decision to conduct a review of National House-Building Council undertakings relating to the supply of structural warranties for new homes in the UK (the NHBC undertakings)**

### **Introduction**

1. The Competition and Markets Authority (CMA) has decided to conduct a review of undertakings given by the National House-Building Council (NHBC) in December 1995 following an investigation by the Monopolies and Mergers Commission (MMC).<sup>1</sup>
2. NHBC currently provides structural warranty and insurance for over 1.6 million homes in the UK.<sup>2</sup> It provides an insurance scheme, Buildmark, it sets minimum standards for builders and it monitors compliance through inspections. NHBC estimates that it provides warranty schemes covering around 80% of new homes.<sup>3</sup>
3. The CMA has a statutory duty by virtue of Schedule 24 to the Enterprise Act 2002 as amended by the Enterprise and Regulatory Reform Act 2013 to keep under review undertakings, such as the NHBC undertakings, that were made under section 88 of the Fair Trading Act 1973. From time to time, the CMA must consider whether, by reason of any change of circumstances:
  - (a) undertakings are no longer appropriate and need to be varied, superseded or released; or
  - (b) an order is no longer appropriate and needs to be varied or revoked.
4. The CMA has set out in its published guidance<sup>4</sup> that, in launching a review, it will consider the case for doing so against its published prioritisation principles and whether there is a realistic prospect of finding a change of circumstances.

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<sup>1</sup> See [NHBC undertakings to Secretary of State \(pdf\)](#)

<sup>2</sup> See [NHBC website](#)

<sup>3</sup> *ibid*

<sup>4</sup> See CMA guidance: [Remedies: Guidance on the CMA's approach to the variation and termination of merger, monopoly and market undertakings and orders.](#)

5. In 2015, the NHBC undertakings were part of a CMA invitation to comment on 13 sets of market remedies.<sup>5</sup> NHBC has since requested a review of its undertakings and the CMA has now decided that this should take place.

## **MMC recommendations and NHBC undertakings**

6. In 1990 the MMC investigated whether a monopoly situation existed in the supply of structural warranty services for new homes in the United Kingdom.<sup>6</sup> The MMC concluded that a monopoly position existed in favour of NHBC. At that time the NHBC supplied over 90% of structural warranty services and had only one competitor, Municipal Mutual Insurance Ltd.
7. The MMC further concluded that certain NHBC rules<sup>7</sup> had the effect of restricting competition because they were acting as barriers to entry for NHBC's potential competitors by making it more costly for them to offer alternative warranty schemes of a comparable standard.
8. The MMC found that the effect of NHBC's (then) rule 12 was broadly to require its members to pre-notify to it all the homes they proposed to build and thus trigger the process of inspection, insurance and payment of associated fees. If an NHBC member wished to submit new homes to another warranty scheme, then this would result in a virtual doubling of its unit warranty costs as these would be incurred in both schemes. The MMC found that Rule 12 operated against the public interest because it prevented housebuilders, without incurring a financial penalty, from dual sourcing and sampling alternative schemes and that, as such, it restricted competition.
9. Furthermore, the MMC found that the ability of an NHBC member to cancel its membership in order to be able to place new homes to be built in the future in another scheme was restricted by NHBC's (then) rules 38 and 41, and by the omission from the rules of any right for a builder cancelling membership to receive NHBC cover for homes already notified to it which were either being constructed or were completed but unsold at the date of cancellation.
10. The MMC found that the rules contained no provision for protection by a terminating member of its period of membership in the event of it returning to NHBC after period spent using other schemes. The MMC found that these

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<sup>5</sup> See [CMA: Review of monopoly remedies put in place before 1 January 2005](#).

<sup>6</sup> See [MMC report: Structural warranty services in relation to new homes](#).

<sup>7</sup> See [NHBC rules for builders and developers registered under the NHBC scheme](#)

omissions, and rule 41 itself, operated against the public interest and restricted competition.

11. Detailed changes were recommended by the MMC to rules 12 and 41 and additions were recommended to the rules. In particular the MMC recommended that NHBC members should be able to sample or dual source broadly comparable schemes.
12. NHBC amended its rules in line with the recommendations and gave undertakings not to make any amendment or addition to the rules, that has or may have the result that it ceases to comply with, or complies to a lesser extent with, the MMC recommendations, without the written consent of the Director General of Fair Trading (now the CMA).

## **Change of circumstances**

13. In considering whether to launch a review, the CMA has assessed whether or not there is a realistic prospect of finding a change of circumstances such that the undertakings may no longer be required or may need to be varied.
14. In its submission to the CMA, NHBC has identified a number of potential changes of circumstances.<sup>8</sup> A summary of these is set out below.

### ***(1) Change to the competitive nature of the structural warranty market***

15. **More competition:** NHBC has stated that there are several other companies providing similar home warranties and so there is now greater competitive pressure on it. As a result, it has stated that it is losing market share. The CMA will examine the extent to which the competitive restraint on NHBC has changed as a result. While, as stated in paragraph 2, NHBC's market share is still very high, it does appear that there are now more providers of warranty services than in 1990.
16. **Lower barriers to entry:** NHBC has stated that barriers to entry are now lower, given the following changes:
  - (a) *Greater use of the agency/broker model by entrants:* NHBC has stated that the bundling of home warranty insurance, bought on a block basis, with other insurance products and then sold to home builders is now commonly used by other warranty providers.

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<sup>8</sup> See [NHBC submission to the CMA](#) (NHBC case page)

(b) *Mortgage lenders' requirements no longer favour NHBC.* The MMC report concluded that mortgage lenders' requirements were a barrier to entry in the structural warranties market. NHBC has submitted that this is no longer the case, noting that the Council of Mortgage lenders expressly states on its website that it is up to individual lenders to decide which schemes they are prepared to accept.

The CMA will examine the implications of these developments and whether there are other significant barriers to entry or expansion.

17. **Increased buyer power:** NHBC has submitted that the home building industry has become more concentrated amongst fewer, larger firms and that these are increasingly using sophisticated procurement strategies to get better deals on warranty schemes. In addition, NHBC has submitted that home builders are now increasingly switching or dual-sourcing new home warranties. The CMA will examine whether buyer power has increased materially and the extent to which this now acts as a constraint on NHBC.

## **(2) Changes to regulation**

18. **NHBC's Buildmark scheme is no longer the benchmark for structural warranties.** The MMC recommended that NHBC should allow builders to source from other schemes providing "broadly comparable standards" to the NHBC scheme. NHBC's rule 8 now enables this and the rules include a definition of "other home warranty". NHBC has submitted that this results in NHBC needing to ensure compliance of other home warranty schemes used by those on its register and so acting as a quasi-regulator. It has submitted that financial regulations now cover this requirement, together with building regulations which prescribe minimum standards for construction, as well as the assessment of individual mortgage lenders of whether a warranty scheme is acceptable to them. For these reasons, NHBC has submitted that rule 8 and its definition of "other home warranty schemes" have now become obsolete. The CMA will consider whether this is the case in the review.
19. **Consumer protection:** NHBC has submitted that the regulations described above are designed to protect consumers and so have superseded that aspect of its role. The CMA will consider the extent to which changes in regulation represent a change in circumstance in relation to the role of NHBC as reflected in the NHBC undertakings.

## **Prioritisation principles**

20. In order to make the best use of its resources, the CMA needs to ensure that it makes appropriate decisions about which projects and programmes to

undertake across its areas of responsibility. The CMA has selected the NHBC undertakings for review at this time in the light of its published prioritisation principles. These principles are impact, strategic significance, risk and resources. We consider each of these in turn.

- (a) **Impact:** New home building is an important part of the UK's economy and buying a house is one of the largest financial decisions a consumer takes. A well-functioning market for structural warranties is important so that new home buyers have the confidence that they will be covered against any structural problems that arise within the first few years of buying a new home. The market for new homes appears to be changing with a greater variety of home types and NHBC has argued that the undertakings are preventing it from making changes to its rules which would enable it to be more flexible in covering different types of new homes.
- (b) **Strategic significance:** This review reflects the CMA's statutory duty to keep under review orders and undertakings, together with its 2015/16 Annual Plan commitment to review existing merger, market and monopoly remedies. The NHBC has requested a review and has identified possible evidence of a change of circumstances. The remedies relate to an important aspect of the housing market, a strategically important sector in which there is significant public interest.
- (c) **Risks:** Given the importance of the market and the public interest in housing in general it is possible that stakeholders will raise issues with the CMA which fall outside the scope of the review. The scope of the review will therefore need to be clearly defined although information gathered as part of this exercise may provide background for other work.
- (d) **Resources:** The CMA has sufficient resources to conduct a review of this scope in a timely manner.

## Decision to review the undertakings

21. The evidence currently available to the CMA indicates that there are grounds for a realistic prospect of finding a change in circumstances relevant to the NHBC undertakings. The CMA has considered this case against its prioritisation criteria and has decided to launch a review.

## Stakeholder views

22. The CMA is inviting views from interested parties on whether it should remove or vary these undertakings. The CMA would welcome comments from affected parties such as providers of structural warranties, home builders,

insurance providers and bodies representing these sectors and new home buyers on the following issues:

- The emergence and growth of comparable structural warranty providers, and the extent to which they provide a competitive restraint on NHBC.
- Ease of entry and expansion into the supply of structural warranties and any significant barriers to entry or expansion that currently exist.
- The extent to which home builders have switched or dual-sourced their structural warranty requirements, and any barriers to further switching or dual sourcing.
- The importance of the NHBC in setting the benchmark standards in the industry, relative to the role now played by financial regulations, building standards and mortgage lender requirements.
- The practical impact of the MMC undertakings on competition in the provision of structural warranties.
- Any other changes of circumstances in this market which the CMA should consider.

23. Those responding should provide their views, supported with relevant evidence where possible, in writing to the CMA either by email or by post as set out below:

Email: [structural.warranties@cma.gsi.gov.uk](mailto:structural.warranties@cma.gsi.gov.uk)

Structural Warranties Review  
Competition and Markets Authority  
Victoria House  
37 Southampton Row  
London WC1B 4AD

24. Responses should be sent to the CMA by 5pm on Thursday 20 April 2017.