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Briefing note December 2014

ACCC authorises resale price maintenance for the first time

Pursuant to a recent determination by the Australian competition enforcement authority, the Australian Competition and Consumer Commission ("ACCC"), Resale Price Maintenance ("RPM") has been "authorised" for the first time in Australian competition law history. The authorisation decision could be a valuable indicator of the limited circumstances in which RPM may be acceptable in Australia and other jurisdictions.

A green light for RPM?

In most jurisdictions, including Australia, RPM is presumed to be anticompetitive, and is therefore prohibited unless parties to an RPM arrangement can prove that it has pro-competitive effects.

The ACCC, in common with other competition authorities, has been highly reluctant to accept evidence of pro-competitive effects and, until now, has never issued an authorisation for RPM. Indeed, on 27 December 2013, the ACCC obtained orders against Mitsubishi Electric of penalties of AUD 2.2 million for engaging in RPM in relation to Mitsubishi Electric branded air conditioning products.

However, in a recent decision, the ACCC conditionally authorised Tooltechnic Systems (Aust) Pty Ltd ("Tooltechnic") to set minimum retail prices for its Festool power tool products for a period of four years.

While the per se prohibition on RPM is unchanged, the ACCC determination represents a conceptual shift from the traditional unwavering attitude of the ACCC as an enforcement agency to prohibit the practice to one that somewhat aligns with the United States' position that assesses the conduct based upon the economic rationale for its justification.

However, in our view the conditional authorisation is not to be treated by suppliers as a sign of the ACCC welcoming RPM, but rather an example of the exceptional surrounding circumstances that may warrant such an authorisation in limited conditions.

Authorisation under Australian competition law involves a balancing of the competitive detriments of the anti-competitive behaviour with any public benefits associated with the conduct and only "authorising" such conduct when the benefits outweigh the detriments.

To underline that the Tooltechnic matter is a particular set of exceptional circumstances, on 11 December 2014 the ACCC obtained court enforceable undertakings against two bicycle parts and accessories suppliers imported and wholesaling in Australia to prevent them from engaging in RPM.

Key issues

- RPM is presumed to be anticompetitive in most global jurisdictions, including Australia, unless parties can prove otherwise.
- The ACCC's authorisation decision could be a valuable indicator of the circumstances in which RPM may be acceptable in Australia and other jurisdictions.
- However, the facts of the case suggest that those circumstances will be limited to cases where the parties face strong inter–brand competition, and there is evidence that contractual mechanisms have failed to prevent free riding and to promote high quality service levels.

Background to the determination

Authorisation process

Under section 48 of the Competition and Consumer Act 2010 (Cth), RPM is prohibited regardless of any effect the relevant RPM conduct has on competition. Section 88(8A) of the CCA empowers the ACCC to authorise RPM if it is satisfied that the associated public benefits will outweigh the relevant public detriments. Tooltechnic's application for authorisation of such conduct is the first to be made since the authorisation process was first introduced in 1995.

Tooltechnic's application

Under the application, Tooltechnic, an exclusive importer and wholesaler of Festool power tools, sought to vary its supply agreements to require dealers to not re-sell Festool products below minimum price levels specified by Tooltechnic. Its reasoning was that the highly complex and differentiated nature of the product required dealers to invest in certain pre-sale and post-sale services (such as demonstrations, training and repairs) however the incentive to provide these services was being undermined by certain non-investing "free-riding" retailers who would undercut the investing dealers by offering the products at a discounted price. This would encourage customers to benefit from the full-service dealer in informing themselves of the product and then purchase the Festool product from another dealer at a considerable discount.

Tooltechnic submitted evidence that the existing contractual arrangements had been ineffective in preventing free-riding conduct, and in securing the offer of high quality services by dealers, with the consequence and that the price undercutting damaged the image and status of the Festool brand.

Authorisation

The ACCC released a draft determination on 21 October 2014 proposing to grant conditional authorisation and invited comment from relevant stakeholders (such as major competitors and power tool retailers) on the proposed determination, most of whom were generally receptive to the proposed authorisation.

On 5 December 2014 the ACCC issued its final determination to authorise the RPM for a four year period, conditional on Tooltechnic meeting reporting requirements including but not limited to the details of the RPM set, average wholesale prices and the relevant changes made to its supply agreements.

Balance of Public Benefit and Detriment

The ACCC acknowledged that the likely public detriments of authorising the RPM included the restriction on intra-brand price competition which would see some consumers face a higher retail price for Festool products. The other key public detriment was the likelihood that in fixing a minimum resale price the risk of coordinated conduct would be increased and could lead to higher prices, reduced output and diminished innovation.

Both of the identified public detriments could be counteracted, in the ACCC's view, by the fact that:

- competitive pressure from other suppliers of power tool products would constrain Tooltechnic given that Tooltechnic would have little incentive to raise prices above competitive levels for fear of losing customers to more competitive counterparts; and
- given the power tool market was characterised by a wide array of alternative power tool products, low barriers to entry and substantial innovation, it could not be said to be a market conducive to facilitating co-ordinated conduct.

Beyond counteracting the public detriments identified, the ACCC acknowledged additional public benefits that RPM would achieve including:

- encouraging retailers to invest in providing a full service and allowing customers to make more informed decisions regarding the purchase of trade-quality power tools;
- mitigating the material risks of market failure caused by free-riding of certain retailers of Festool products; and
- encouraging retailers to compete on factors beyond price including service, performance and reliability.

Insights and Implications for Business

Whilst the authorisation indicates a shift from an entirely strict prohibition on resale price maintenance, other businesses should not expect such an authorisation to be a common response by the ACCC to applications to engage in RPM. The ACCC's proposal to grant an authorisation in this case was a response to very specific circumstances, mainly the material risks of market failure caused by free-riding, and the evidence that existing contractual mechanisms had been ineffective at preventing this (prompting the ACCC to recognise that "there may be inherent difficulties in contracting for a particular level of retail service").

By the same token, the ACCC's recognition of free-riding as a market failure that may warrant regulatory intervention is an important recognition of the merit and practical application of certain economic theory to modern markets. The determination is in line with the United States and Canadian approach of recognising the pro-competitive effects of RPM however the United States and Canada have gone further to abandon per se prohibition.

In the course of the impending National Competition Policy Review report of the Australian Government, the Review Panel acknowledged that some jurisdictions had moved away from a per se prohibition but did not recommend that Australia embark on the same course. In its draft report the Review Panel recommends retaining the per se prohibition on RPM but allowing for an exemption for RPM conduct between related bodies corporate (as is currently stipulated for other forms of exclusive dealing) and allowing RPM to be notified to the ACCC under the current process for exclusive dealing. If accepted this would mean that notified RPM conduct would be permitted unless the ACCC investigates and revokes a notification within 14 days. In its submission in response to the draft report, the ACCC opposed the latter recommendation, reasoning that the current authorisation process was better equipped to screen for efficiency enhancing RPM arrangements.

The reporting conditions and limited timeframe for Tooltechnic's RPM in indicate that the ACCC may have intended this first authorisation to form somewhat of a test period for whether RPM can in fact achieve the public benefits and pro-competitive effects which advocate its permissibility.

It is quite likely that the ACCC will use the Tooltechnic matter as an example of why the authorisation approach is preferable and allows for closer monitoring than the notification regime suggested by the Review Panel.

Conclusion

It is a fair observation that the unique characteristics of the product market and Tooltechnic's very small market share carried significant weight in justifying RPM conduct. In particular, it remains to be seen whether other services such as investments in advertising and marketing a product may also be considered as a free riding issue, which would impact many smaller suppliers and internet retailers who do not engage in promotional activities. It is doubtful whether the ACCC would allow the net to be cast this wide and it appears from the rationale for the authorisation that product differentiation played a key role in demanding particular need for certain pre sale and post sale services which in turn served the purpose of better informing the consumer's choice in a technically complex product market.

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