Forbidden conversations: Trade Practices Act implications for Alliances

Snap Shot

Alliances carry serious risks of breaching the competition provisions of the Trade Practices Act and the consequences of a breach can be significant. They may involve the imposition of significant financial penalties, banning orders for individuals, and orders for civil damages and legal costs. They may also involve reputational damage and the need to devote substantial resources to responding to investigations by the Australian Competition and Consumer Commission.

The competition provisions in the Trade Practices Act

The competition provisions in the Trade Practices Act broadly prohibit two types of conduct. Firstly, conduct that has the purpose or likely effect of substantially lessening competition in a market. And secondly, conduct involving market sharing, bid rigging, price fixing, and some types of tying arrangements. This second type of conduct may result in a breach even where there is no appreciable effect on competition.

Common situations where this conduct may arise are:

- non compete clauses,
- pricing agreements between competitors,
- resale pricing agreements,
- tying, and
- forbidden conversations.

Non-compete clauses

Sometimes, alliance participants wish to commit exclusively to an alliance by agreeing to only undertake certain activities within the alliance. They will also refrain from competing against the alliance.

Reducing risk

The simplest way to reduce risk with non-compete clauses is to avoid agreements restricting activities outside the alliance and agreements not to compete against the alliance.

If the members want the comfort of an agreement not to compete against the alliance, it may still be possible to lawfully include a non-compete clause in the alliance documents. However to minimise risk, the non-compete clause must be carefully drafted to show two important points:

- it must accurately reflect the members' sole purpose in seeking that commitment is pro-competitive (to foster the success of the alliance), and

- it should only extend to prevent the members from engaging in activities that are reasonably necessary to protect the legitimate business interests of the alliance.

A good example of a situation where a non-compete clause may be unlawful is where it applies to activities not engaged in by the alliance, or has an unduly lengthy duration.

Of course, if the members of the alliance are merely seeking to implement an ulterior purpose of limiting the extent to which they might otherwise compete against each other, that would pose a significant Trade practices risk.

Pricing agreements between competitors

In some cases, the participants of an alliance may wish to agree the price at which goods and services will be supplied by the alliance, or acquired by the alliance. They may also wish to agree the price at which goods or services produced by the alliance will be re-supplied to third parties.

It is important to ensure that these types of pricing agreements do not result in a breach of the price fixing provisions.

Reducing risk

Complementarity

Pricing agreements should not result in a breach of the price fixing provisions if the alliance members would not otherwise (in the absence of the alliance) supply or acquire the goods or services. This will typically occur where the alliance members contribute complementary expertise to the alliance such as a distribution channel and sales and marketing expertise on the one hand and manufacturing expertise on the other hand.

Collective acquisition exemption

Where 2 or more of the members of the alliance would (in the absence of the alliance) supply or acquire goods or services, great care must be taken to avoid a breach of the price fixing provisions. Any agreement on the price of the goods or services needs to be structured to ensure it falls within the exemption for collective acquisitions.

To meet this exemption, alliance members would need to:

- acquire those services collectively, not individually, and

- ensure that the collective acquisition has neither the purpose, or the likely effect, of substantially lessening competition.

Complete defence for joint ventures

The complete defence for joint ventures is wider in scope than the collective acquisition exemption. Therefore, if the services cannot be acquired collectively, it may be possible to structure the agreement so that it comes within the complete defence for joint ventures.

The complete defence potentially applies to agreements about:

- the price at which members of an alliance will **acquire** things from third parties,

- the price at which members of the alliance will **supply** things to third parties, and
- some non-compete agreements.

The complete defence for joint ventures will be available where the members of the alliance can demonstrate that the purpose of the conduct is for the sole purpose of a joint venture; and does not have the purpose, and will not have the likely effect, of substantially lessening competition in a market.

The complete defence is only available for joint ventures. A joint venture may be incorporated or unincorporated, but it must involve a joint endeavour.

The complete defence is not available where the members of the alliance expressly agree that their alliance will not constitute a joint venture.

Resale pricing agreements

Appoint resellers as agents

If the members of the alliance wish to agree the resale price of products produced by the alliance, in order to avoid a breach of the resale price maintenance provisions, the members of the alliance may appoint legal agents to resell the products.

Merely recommend the resale price

Alternatively, it may be possible not to breach the Act by using a system of recommended retail prices. However, the recommendation should be accompanied by a written communication which makes it clear that the resellers are free to sell the products at prices other than the recommended price.

Tying conduct

Tying is where alliance participants may wish to structure their arrangements so customers have to acquire products from more than one member of the alliance.

Third line forcing

Third line forcing is a particular type of 'tying' conduct which is prohibited by the Trade Practices Act. It involves an offer to supply goods or services on condition that the customer will acquire other, perhaps unwanted, goods or services from a third party. This would happen, for example where one member of the alliance offered to supply haulage services on the condition that the customer would agree to acquire components for a crushing plant from another member of the alliance.

Reducing risk

It is usually possible to restructure tying conduct so that it will not result in a breach of the third line forcing provisions. The commonest way to do so is by bundling the services together. This can be done where one member of the alliance acquires goods or services from another member and offers both to the customer in a bundle. For example, the member would acquire the components for the crushing plant from the other member and offer the haulage services and crushing plant components as a bundle.

Forbidden conversations

Sometimes, the members of an alliance use the alliance as a forum to exchange strategic or commercially sensitive information which is outside the mandate of the alliance. Many cartel cases have involved those situations.

Reducing risk

In situations where the members of an alliance compete against each other in any area, it is advisable to conduct all meetings of members of the alliance in accordance with a written protocol. The written protocol should list the topics that can, and cannot, be discussed at the meeting. Generally, discussions about future sales and marketing strategies, pricing, or other commercially sensitive information should be avoided.

It is also advisable to conduct any meetings of members of the alliance strictly in accordance with a written agenda. In some cases, it may be advisable to have a lawyer present and for the members of the alliance to agree that the lawyer may intervene to terminate a discussion.

The importance of seeking advice

Due to the potentially significant penalties for breaching the Trade Practices Act it is important to ensure both the structure and operation of your alliance minimises Trade Practices risk.

If you are involved in alliancing, the best way of determining how to approach your alliance is to seek advice from your lawyer.

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