FCAI Submission to the Productivity Commission Issues Paper

Right to Repair

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1. Executive Summary

The Federal Chamber of Automotive Industries (FCAI) is the peak industry body representing the interests of the Australian importers and distributors of passenger motor vehicles, light commercials, motorcycles and ATVs. The FCAI members are listed on our website www.fcai.com.au.

The Productivity Commission (PC) Issues Paper on the topic of Right to Repair raises some interesting questions from a new motor vehicle perspective. This PC inquiry coincides with the closely related Treasury work on a proposed regulatory regime for provision of motor vehicle service and repair information to the independent repair market. Whilst this is somewhat confusing for industry, the thrust of the PC Issues Paper does provide the opportunity for a more considered analysis of the market.

The FCAI members are, collectively, the providers of advanced mobility solutions for Australian consumers having demonstrated considerable investment in environmental, safety and congestion improvements for all Australians. The PC notes that there are two different approaches to the consideration of the regulatory drivers for market intervention, a consumer and competition approach or, alternatively, an environmental driver aimed at minimising waste in resources through repairability built into the product design process. Interestingly, both these approaches are considered in the motor vehicle industry in Australia, and the FCAI does not find them, as principles, mutually exclusive. FCAI does, however, find that the consumer and competition arguments behind the Government rhetoric around access to service and repair information in Australia lacks foundation. That said, our position is to support the Governmental process that is currently underway and mentioned above.

Consumers generally make few large purchases in their lifetime and a new motor vehicle is often considered the second largest investment. This segregates the purchasing considerations apart from the general, run-of-the-mill, consumer products that are often mentioned when discussing repairability, for example mobile phones or small electrical appliances. Importantly, the other major differentiator for new motor vehicles is that while many products rely on establishing their liability through reference to the consumer guarantees under the ACL, new motor vehicle suppliers have an added warranty provided by the manufacturer or their agent which adds significant value to the product and warrants the service and repair should an issue arise in service. Given that the suppliers are warranting that they will repair the vehicles, clearly this refutes any arguments about non-repairability for these advanced machines.

The PC often refers to the ACCC 2017 Market Study of the new motor vehicle repair sector in the issues paper. FCAI notes that that study, based on information that is now dated, did not conduct any cost-benefit analysis in reaching the conclusions. Nor in fact did the study make any findings of fact, rather a series of hypothesise that the FCAI believes lack a detailed understanding of the market. While not suggesting that the PC intends to rely on that previous work in their findings, we urge a fresh consideration of the competition and consumer aspects of the market and provide more comment on this later in this submission.

FCAI would also welcome a fuller discussion on the alternative approach to product obsolescence, based on environmental perspectives and end of life treatments. The pace of change in technology in automotive has increased significantly over the last ten years with some observing that the

change over the last ten years has been more significant than the changes seen in the previous fifty years.

1. **Information Request 1**

What would a 'right to repair' entail in an Australian context? How should it be defined?

In Australia, the term "right to repair" is used in much the same way it is used in the United States: that is, it look at matters such as access to necessary spare parts, tools and information for consumers and independent repairers. It is not used in the European sense of the phrase - i.e. matters such as product design and resource management and the ability to maximise a consumer's opportunity to repair the goods and avoid creating additional waste.

2. **Information Request 2**

What types of products and repair markets should the Commission focus on?

The Australian motor vehicle market is characterised by a very large number of repairers, both authorised by the OEM and independent, that are indicative of a healthy availability of options for consumers. Of equal relevance is that fact that the majority of service and repairs in Australia are carried out by the aftermarket sector. While this does make the motor vehicle sector different from other sectors where the availability of authorised and independent service and repairs is not so prominent, the FCAI suggests that the PC continue to consider the automotive sector which will provide an independent assessment from which related Government policies may be better informed.

3. **information request 3**

   (a) **Do the consumer guarantees under the ACL provide adequate access to repair remedies for defective goods? If not, what changes could be made to improve access to repair remedies? Are there barriers to repairing products purchased using new forms of payment technologies, such as 'buy now pay later'?**

Yes, consumer guarantees under the ACL provide adequate access to repair remedies for defective goods. Section 58 of the ACL provides a specific guarantee as to the availability of repairs and spare parts. In addition, section 259 of the ACL provides that if there is a failure of one of the consumer guarantees which is not a major failure and the supplier cannot remedy the failure within a reasonable time, the consumer may, among other things, reject the goods and obtain a refund or replacement. There is therefore, a real incentive on suppliers and OEMs to ensure that goods are repaired as quickly as possible.

In addition to the ACL requirements, the Australian new vehicle market is characterised by one of the highest levels of competition in the world, with over 60 brands competing for around one million sales annually. This has in turn aided the development of significant voluntary warranties over, and above the ACL requirements, to the benefit of consumers.

'Buy now pay later' has no direct impact on the automotive sector.

(b) Is the guarantee of available repair facilities and spare parts effective in providing access to repair services and parts? Or is the opt out clause being widely used, making the guarantee ineffective?

Yes, the guarantee of available repair facilities and spare parts is effective in providing access to repair services and parts in the Australian automotive market. Additionally, and perhaps a more definitive driver of service and repairability, is the fact that vehicle OEMs and their dealers take this obligation extremely seriously and invest substantial amounts of money to ensure that their vehicles can be properly and conveniently repaired in one of the most competitive markets in the world. It should also be noted that there is a significant volume of aftermarket parts, often reverse engineered from genuine parts, that are available and routinely used by the independent repair sector. The provisions of the Designs Act are relevant in this respect.

The opt-out clause is rarely, if ever used.

(c) Should consumer guarantees seek to balance the broader societal costs of remedy choices (such as the environmental impacts of replacements) with consumer rights, and if so how? For example, should repairs be favoured as a remedy?

If a consumer has a failure in their motor vehicle, they will invariably return the vehicle and ask for a repair, or if considered a major failure or multiple minor failures, a replacement or a full refund (which they will presumably use to buy another new vehicle) rather than allowing the supplier the opportunity to repair their vehicle. The current regulatory regime is lacking precision as to the ability of the supplier to repair, as opposed to a deemed obligation to replace or refund the consumer. While this is not a topic the subject of this inquiry, FCAI suggests improvements to the ACL that clarify that in the case of a major failure or multiple minor failures the consumers right to refund or replacement must take into account the good use of the vehicle up until this occurrence.

FCAI recalls that the ACCC market study identified a “culture of repair” within the motor vehicle industry in the negative. This observation, wrongly developed in the eyes of the FCAI, is a little bewildering when the value (commercial, environmental and personal) of the product and the benefits of an extended life are considered.

While hard data on the rate of recycling for motor vehicles is difficult to gather, FCAI understands that it is extremely high, with many valuable metals and other products reclaimed and applied in secondary lives.

This significant environmental impact would be reduced if the supplier/manufacturer was given a greater opportunity to repair defective motor vehicles. Of course, should the vehicle be off the road for a long period of time the consumer should not be disadvantaged, but this could be addressed by ensuring that the consumer is provided with an equivalent replacement loan while the repair was being carried out.

(d) Are consumers sufficiently aware of the remedies that are available to them, including the option to repair faulty products, under the ACL's consumer guarantees? If not, would more information and education be a cost effective measure to assist consumers understand and enforce guarantees? What would be the best way to deliver this information? What other measures would be more effective.

At the time a consumer purchases a new motor vehicle, the dealer provides the consumer with a brochure prepared by the ACCC explaining the consumer's rights under the ACL. It is called 'Just bought a new car? Know your consumer rights.' In addition, most if not all vehicle handbooks include references to the consumers rights.

4. INFORMATION REQUEST 4

(a) The Commission is seeking information on the nature of repair markets in Australia, including detailed data on the repair markets for specific products, covering:

- **market size — by employment, revenue, number of businesses, profit margins**
- **market composition — such as market share between authorised, independent and DIY repairers Is there any evidence of a difference in quality, safety or data security between authorised repair networks and independent repairers? Are there ways to address concerns around quality, safety or data security while promoting a vibrant independent repair market?**

In terms of market size it is difficult to accurately determine the revenue as this would require a contemporary survey of a large number of participants, which is not possible within this submission deadline. In terms of the market share held by authorised dealers and the independent repairers it is widely held that vehicles leave the dealer network and move to the independent sector for servicing when the warranty period expires. Under the current warranty offerings this would mean vehicles begin to move to the independent sector from about 5 years of age. However, the car parc consists of 17 million light vehicles of varying age and varying warranty periods including a range of vehicles that were and perhaps still are sold with 3 year warranty periods.

In terms of quality of repair there are two relevant factors: genuine parts and training of technicians. In respect of parts, authorised repairers will use genuine parts where they are available. FCAI is of the view this improves the residual value of the vehicle and also ensures that the underlying design and engineering within the vehicle remains compliant with the Australian Design Rules and that the vehicle is maintained to factory standard.

In respect of training, the modern vehicles are highly complex and specialisation through the authorised repair route, along with a significant and on-going investment in training of technicians, will ensure the highest quality of repairs. Anecdotally much of the time an independent repairer spends in diagnosing a fault with a vehicle is due to the need to familiarise themselves with the operating systems of a wide range of different vehicles. This does not signal an inefficiency in provision of information to repair the vehicle, nor the development of a needlessly complex machine. It simply reflects the widely acknowledged principle of the value of specialisation.

(b) Is there any evidence of a difference in quality, safety or data security between authorised repair networks and independent repairers? Are there ways to address concerns around quality, safety or data security while promoting a vibrant independent repair market?

In the absence of any Australia-wide registration and certification system for repairers it is not possible to generalise about the capabilities of independent repairers. Authorised repairers on the other hand have to satisfy the exacting standards and requirements of the OEM.

In terms of safety, the new technologies coming to the market pose significant injury risk should a technician or other party without a high degree of specific technical knowledge and training, approach a service or repair task in an uninformed manner. In the case of an electrified vehicle or a hydrogen vehicle, these risks are extremely high particularly as they relate to the technician. With the addition of Advanced Driver Assistance (ADAS) functions such as Lane Keep Assist (LKS), Pre Collision Systems (PCS) and Radar Cruise Control (RCC) systems to name but a few, these systems use a combination of RADAR, Cameras and other advanced range detection systems to monitor the vehicles environment. All of these systems must be accurately initiated and aimed after vehicle repairs for them to operate correctly. Uninformed repairers while innocuously undertaking even minor repairs can alter these systems, resulting in incorrect operation with consequent safety implications for vehicle operators. The independent repair sector must, like any other workplace, ensure that they and their staff are aware of these risks.

With respect to data security FCAI recently updated our data and privacy code. A copy can be found at https://www.fcai.com.au/news/codes-of-practice/view/publication/172.

(c) Are there available examples of the contracts between OEMs and authorised repairers? Do these contracts limit effective competition in repair markets (such as by limiting the number and reach of authorised repairers or requiring authorised repairers to not be authorised by a competing brand)?

Dealers are authorised repairers and are party to a dealer agreement with their OEM. Some OEMs, especially those selling prestige vehicles, have agreements with authorised crash repairers.

Dealers are generally allocated an area within which they are encouraged to market their services. They are also generally prevented from establishing premises in another authorised dealer's prime market area. However, they are able to sell vehicles and genuine parts, provide associated financial and insurance agency services as well as service customers regardless of where they may reside. Authorised crash repairers generally do not have areas allocated to them.

In reality many new vehicle dealerships are multi-brand sites with service and repair facilities for a range of brands. Authorised dealers may also, depending on their location, service and repair vehicles for consumers well outside their prime market area. For example, a CBD based dealership may service commuter vehicles.

- **What is the process to become authorised? Is it open and competitive?**

Most new dealers come about through buying an existing dealership. An OEM has to consent to the new dealer and cannot withhold their consent unreasonably. FCAI understands that it is rare for a new dealer to come from a background that has no experience in operating an automotive sales, service and repair facility.

(d) Are there specific examples or other evidence of practices by OEMs or their authorised repairers that create barriers to competition in repair markets?

OEMs require that vehicles being repaired under either an OEM warranty or a consumer guarantee are repaired by an authorised repairer, who has demonstrated their investment in the tools, technology and staff to enable quality service repairs to be undertaken. Given that the OEM is paying for this work, it is reasonable that the OEM can select who it wants to do the work.

- **Do other factors also create barriers to competition in repair markets, such as short sighted consumer behaviours, switching costs, poor information availability or consumer lock in?**

The motor vehicle sector is one subject to:

- Increasing sophistication of product;
- Increasing range of models;
- An incredibly competitive market in Australia;
- An increased need to specialise in particular brands or components, even for technicians with authorised dealerships.

Even when taking this into account it should be noted that the bulk of servicing does not require access to additional and highly complex information. Basic maintenance such as replacing filters, oil, brake pads etc are taking place around the country every day and the majority of this work is carried out by the independent repair sector. Over and above this there is a range of repair and some service work carried out by the authorised dealer network under warranty at no cost to the consumer. The residual service and repair work, which is a much lesser component of the overall service and repair market, may require some form of product specialisation or specific information. This evolution in the market is not a barrier to competition, but in fact a reflection of increased consumer value and decreasing price (see page 14 of Appendix A).

(e) What is the relationship between the intensity of competition in the primary product market and the risk of consumer harm from a lack of competition in repair markets? Can competitive primary markets compensate for non competitive repair markets?

- **Is an absence of effective competition in the primary market a necessary condition for consumer harm from non-competitive repair markets?**

The primary and secondary markets for motor vehicles and repairs in Australia reflect high degrees of competition with resulting positive consumer outcomes. As previously touched on there are over

60 brands fighting for a slice of the approximately 1 million sales in the primary market every year. In addition, the service and repair market is well serviced with both authorised and independent repairers competing for business. The bulk of the service and repair work is in fact carried out by the independent repair sector.

FCAI have also provided further economic comment on this in Appendix A.

- **To what extent would measures that enhance competition in the primary market address concerns about a lack of competition in repair markets?**

See Appendix A. FCAI also notes that the current regulatory environment in Australia has encouraged an extremely competitive primary market.

(f) Are the restrictive trade practices provisions of the CCA (such as the provisions on misuse of market power, exclusive dealing or anti-competitive contracts) sufficient to deal with any anti competitive behaviours in repair markets?

In the automotive market, there is no anticompetitive behaviour, at least insofar as the OEMs are concerned. To the extent that there could be, the existing provisions are more than adequate to deal with it.

The restrictive trade practice provisions of the CCA have been relatively recently reviewed by Professor Harper and his committee. As a result of that review a number of amendments were made – including introducing the prohibition on concerted practices.

The concepts dealt with by these provisions are complex and significant amounts of jurisprudence have been developed over the years. Any further amendments would require a separate detailed analysis.

(g) What policy changes could be introduced if there is a need to increase competition in repair markets and improve consumer access to, and affordability of, repairs?

- **What are the costs and benefits of any such proposal to the community as a whole? How does it balance the rights of manufacturers and suppliers, with those of consumers and repairers?**

There is no need to increase competition in repair markets or improve consumer access to, and affordability of, repairs. FCAI questions what need there is for regulatory interference to "balance the rights" of any parties?

5. INFORMATION REQUEST 5

(a) To what extent do current IP laws already facilitate repairs by consumers or independent third parties (e.g. the spare parts defence under the Design Act)?

The current IP laws adequately facilitate repairs by consumers and independent third parties.

(b) Are there any aspects of IP laws where consumers' rights with respect to repairs are uncertain?

No.

(c) Do current IP protections (e.g. intellectual property rights, technological protection measures, end user licencing agreements) pose a significant barrier to repair in Australia?

No, they do not. This is demonstrated by the recent experience of Toyota Australia which, at considerable expense, set up a portal through which repairers could access all of Toyota's technical information. The number of requests for information was and continues to be extremely small.

If yes, please comment on any or all of the following:

- **the specific IP protections that prevent consumers from sourcing competitive repairs and/or inhibit competition in repair markets**
- **the types of products or repair markets these barriers mainly affect**
- **the prevalence of these barriers**
- **the impacts of these barriers on third party repairers and consumers (e.g. financial cost, poorer quality repairs)**
- **options for reducing these barriers and their associated benefits, costs and risks (including potential impact on market offerings).**

(d) In what ways might government facilitate legal access to embedded software in consumer and other goods for the purpose of repairs? What are the pros and cons of these approaches.

From an automotive perspective this is being dealt with through the Treasury consultations on Access to Service and Repair Information.

6. INFORMATION REQUEST 6

(a) What evidence is there of planned obsolescence in Australian product markets? Do concerns about planned obsolescence principally relate to premature failure of devices or in them being discarded still working when more attractive products enter the market?

There is no evidence of planned obsolescence in the Australian automotive market. FCAI has observed over the past few years a step change in the rate of increase in technological advances. This has also been commented upon by long-time industry members. As the automated and connected vehicles, along with low and zero emission vehicles, continue to be developed the rate of technological change will continue to grow. This is far from a state of planned obsolescence, particularly given that the existing vehicle fleet is maintained and serviced by a range of providers to ensure the product is not obsolete ahead of time. In fact, it is estimated that over 70% of the vehicle

fleet is serviced by the independent repairers. Given the fleet average age is 10.5 years, there is clearly no argument to support "planned obsolescence" in the motor vehicle market.

A further indicator of the longevity of motor vehicles is the practice of over the wire updates of software to ensure that the vehicle is up-to-date from a range of perspectives. With the evolution of autonomous driving systems and the responsibility the supplier takes for these vehicles the regularity of software updates will increase significantly to ensure that the consumers vehicles are far from obsolete.

(b) How can the Commission distinguish between planned product obsolescence and the natural evolution of products due to technological change and consumer demand?

A good way to distinguish this is by considering the warranty and parts that the supplier/manufacturer makes available for their product. In the case of automotive there is an extensive service and repair network and a full range of genuine and aftermarket parts.

(c) How does planned obsolescence affect repairers, consumers and the broader community in Australia?

Not relevant to automotive.

(d) What measures do governments currently use to prevent planned obsolescence or mitigate its effects (in Australia and overseas)? How effective are these measures?

No comments.

(e) What are the benefits, costs and risks of Australia adopting measures similar to those currently used overseas, such as product design standards and reparability ratings?

In the case of Australia any move toward regulation for new motor vehicles in this vein would be a significant increase in red tape without any additional consumer or community benefit.

(f) Do consumers have access to good information about durability and reparability when making purchases? If not, how could access to information be improved.

There are many sources of information available to a potential purchaser of a motor vehicle, including information about durability, reparability and maintenance costs. In addition, consumers are well protected by the consumer guarantees in the ACL and manufacturers warranty. These give consumers significant protections in the event that a motor vehicle is not as durable or repairable as a 'reasonable consumer' would expect.

The Australian automotive clubs such as RACQ (https://www.racq.com.au/cars-and-driving/cars/owning-and-maintaining-a-car/car-running-costs) often publish information to assist consumers to better understand the whole of life costs for motor vehicles which includes the potential or likely service costs. All of this information, together with private reviews and motoring journal reviews, provide the consumer with substantial information from which to make a purchasing decision.

7. INFORMATION REQUEST 8

(a) What policy reforms or suite of policies (if any) are necessary to facilitate a 'right to repair' in Australia?

(b) Are there any other barriers to repair and/or policy responses that the Commission should consider?

No. There is no need to introduce any policy reforms to facilitate the 'right to repair' for motor vehicles.

Closely related to this question, the Commonwealth Government has recently released an Exposure Draft of the 'Competition and Consumer Amendment (Motor Vehicle Service and Repair Information Sharing Scheme) Bill 2020, with an accompanying Exposure Draft Explanatory Memorandum. This Bill has been developed without the benefit of a cost-benefit analysis nor a rigorous regulatory impact assessment. The FCAI has prepared a submission which demonstrates the significant costs that will be imposed on the vehicle distributors (which will flow to consumers) and the limited if any benefit that could be expected *(copy of final submission to be provided).*

While the FCAI has taken a position that supports sensible industry led regulation of the supply of service and repair information we would take this opportunity to submit that in the absence of anyone making a serious case of a gap in the existing restrictive trade practices provisions of the CCA as they relate to access to service and repair information, this leaves the distinct possibility that the regulatory solution is being pursued at the behest of special interest groups. This would in turn suggest that access to service and repair regulation, including the proposed Part IVE of the CCA (motor vehicle service and repair information sharing scheme), is being pursued in order to protect certain competitors rather competition. This is further explored in Appendix A.

(c) What are the costs and the benefits of the various policy responses that have been proposed to facilitate repair (such as those outlined in table 1)?

See the FCAI's submission to the Exposure Draft of the 'Competition and Consumer Amendment (Motor Vehicle Service and Repair Information Sharing Scheme) Bill 2020.

(d) Are there other international policy measures or proposals that the Commission should consider as part of this inquiry?

No.

APPENDIX A

Durable Goods and Aftermarkets

Durable goods are purchased with the expectation of using them and obtaining associated benefits over an extended period of time (MacKie-Mason & Metzler, 2009, p. 559).

Aftermarkets are markets for goods and services used in combination with durable goods but purchased after the consumer has invested in the equipment (Borenstein, MacKie-Mason, & Netz, 1995, p. 455). Aftermarkets comprise markets for complementary goods and services that are often purchased subsequent to the purchase of the durable goods (Gundlach, 2007, p. 18). The market in the durable good is known as the primary market.

An example of a primary market is for new cars that has aftermarkets in repair parts and servicing. Demand for repair services is composed entirely of consumers of the primary market. Consumers don't demand vehicle repair unless they own a car in the first instance.

Once a durable good is purchased, consumers are required to buy aftermarket products or services that are compatible with that primary product (Organisation for Economic Co-operation and Development, 2017, p. 5). The primary good manufacturer, who has the technology, know-how, information and incentives to produce high quality secondary products, is often a major supplier in the aftermarket (Organisation for Economic Co-operation and Development, 2017, p. 5).

Products sold in aftermarkets, together with the primary product to which they relate, are components of a product system (Gundlach, 2007, p. 18). Like individual products that compete in various ways against one another, product systems also can compete against other product systems in various ways (Gundlach, 2007, p. 19). Referred to as *systems competition*, competition involving product systems can include *intrasystem* competition as well as *intersystem* competition. Intersystem competition occurs where primary and aftermarket product providers compete against other product systems (Gundlach & Foer, 2007, pp. 1-2). Intrasystem competition occurs where providers in the primary market and aftermarkets compete against each other in relation to the sale of same product and in the provision of aftermarket services.

Motor Vehicle Repair

Once a consumer buys a new car they require a range of ongoing aftermarket services and parts to ensure the car is maintained and repaired (Australian Competition and Consumer Commission, 2017, p. 38). Manufacturer car servicing requirements, including the replacement of certain high wear service parts, are set out in the logbook and service manual.

New car logbooks and service manuals detail the car manufacturer's service requirements typically up to the first 200,000km (Australian Competition and Consumer Commission, 2017, p. 40). The logbook tells the consumer when a service is required and what needs to be done.

A consumer can choose to have their car serviced by two main groups:

- Authorised repairers that are aligned with a motor vehicle manufacturer (or new vehicle importer) (Commonwealth Consumer Affairs Advisory Council, 2011, p. vi).[1] *Authorised* means a manufacturer has authorised the supply of a good and/or service to the Australian market under their brand name (Australian Competition and Consumer Commission, 2017, p. 25).
- Independent repairers that are not authorised or affiliated with car manufacturers (Australian Competition and Consumer Commission, 2017, p. 2).

Authorised Repairers

Authorised repairers are part of an authorised new car dealer network. A dealer agreement is typically required to sell a car manufacturer's models in Australia (Australian Competition and Consumer Commission, 2017, p. 32). The agreement is a legal contract which establishes the terms and conditions the manufacturer and authorised dealer are required to meet for the period of the contract. Dealer agreements typically have a duration of one to five years and expire unless a new agreement is reached. Dealer agreements are deemed by the Franchising Code of Conduct to also be franchise agreements (Australian Competition and Consumer Commission, 2017, p. 9).

The pro-competitive rationales for vertical restraints in the new motor vehicle market are numerous and varied and intrabrand restraints initiated by manufacturers acting without coercion from their dealers are almost certain to be competitive (Hovenkamp, 2005, pp. 184-185). The most commonly cited one is the *free-rider* problem. A free rider is someone who enjoys the benefits of someone else's investment without having to pay compensation (Elzinga & Mills, 2008, p. 1842).

In the case of intrabrand competition, the free rider's business policy uses discounted retail prices to attract shoppers whose demands are enhanced by the influence of the full-service retailer even though the free rider does not itself provide the retail service in question and so can undercut the full-service retailer's prices (Elzinga & Mills, 2010, p. 357). This is unsustainable as the full-service retailer cannot incur the extra expense of these services and still match the discounter's low price, and must cut back on their marketing efforts. This reduction in retail service reduces demand for the manufacturer's product and this produces detrimental consequences for consumers as well as for the manufacturer. Even in the absence of free riding, retailers may not be inclined to make the level of investments in service that would maximize the overall competitiveness of a manufacturer's products (Baumol, et al., 2006).

Imposing service requirements is one means through which car manufacturers seek to address the free riding problem and ensure the quality of service associated with a vehicle's branding is maintained to a particular standard. In relation to car servicing, the Australian Automotive Dealer Association (AADA) (2011, p. 1), representing new car dealers, has observed:

> *Manufacturers / suppliers provide strict guidelines and procedures for the equipping, tooling and operations of workshops; the training and development of technicians, and; the methodologies and responsibilities for accessing information at cost to the dealer. The options available to manufacturers / suppliers for any breaches of these requirements can be cause for the termination of a dealer's franchise agreement.*

[1] Other parties engaged in the business of distribution of new motor vehicles supplied by manufacturers overseas will also be referred to manufacturers.

As part of their dealership agreement, authorised dealers are required to undertake ongoing investment in training of their service personnel, to acquire expensive special tools and to maintain equipment and relevant campaign and repair parts inventories (Australian Automotive Dealer Association, 2016a, p. 32).

The imposition of service requirements also ensure that service and repair shops are part of authorised dealers, thereby fulfilling the obligations of manufacturers under Australian Consumer Law (ACL) to take reasonable action to ensure that facilities for the repair of motor vehicles are reasonably available for a reasonable period after the vehicle was supplied.[2]

Authorised new car dealerships across the country typically operate a repair and service centre which aims to service their manufacturer's cars within the geographical area defined in their dealer agreements (Australian Competition and Consumer Commission, 2017, p. 38).

There are around 1,500 authorised new car dealers in Australia operating from approximately 3,135 dealerships (Australian Automotive Dealer Association, 2020, pp. 3-4). Authorised new car dealers employ more than 55,000 people including almost 4,500 apprentices, and have a total turnover/sales of more than $55 billion and generate more than $2 billion in tax revenue.

Independent Repairers

Most independent repairers are small businesses operating as sole proprietors, partnerships or family businesses servicing cars in their local area (Australian Competition and Consumer Commission, 2017, p. 38). It has been estimated that there are some 30,000 independent car repair businesses operating in Australia (Australian Automotive Aftermarket Association, 2020).

There are a small number of branded repairers consisting of franchise repairers (e.g. Midas, Ultra Tune and mycar Tyre & Auto), repairers with supported relationships (e.g. Repco Authorised Service and Bosch Authorised Service), and motoring club affiliated repairers (NRMA MotorServe and RAC Auto Services in Western Australia), although these control only a small share of the overall national repair and service market (Australian Competition and Consumer Commission, 2017, p. 38). In addition, some independent repairers are approved repairers for the motoring clubs.

Competition between Authorised and Independent Repairers

From a systems perspective, one could view each car manufacturers and its authorised dealer network as firms within a single system that manufactures and supports cars (Hawker, 2011, p. 60). The car manufacturer supply interface in the form of new cars as well as the hardware and software components that dealers connect to the cars in the service aftermarket. However, intersystem rivalry in the primary market is not the only form of competition.

There is intrasystem rivalry among authorised dealers of a specific car manufacturer from sales of cars to consumers (Hawker, 2011, p. 60). The integrated product system assembled by car manufacturers also faces further intrasystem competition from third party alternatives to its original equipment manufacturer (OEM) parts as well as competition to its authorised repairers from independent repairers.

[2] Part 3-2 Division 1 s. 58, Schedule 2 of the *Competition and Consumer Act 2010.*

Authorised dealer service centres and independent repairers compete on a range of factors including the price of servicing, repairs and replacement parts, the quality and speed of their work, geographical convenience for consumers, the provision of loan cars, guarantees and other complementary services (Australian Competition and Consumer Commission, 2017, p. 41).

The nature of technical information to repair and service new cars is rapidly changing, with digital files and codes and appropriate diagnostic tools now often necessary to complete a car repair or service (Australian Competition and Consumer Commission, 2017, p. 124).

In Australia independent repairers have complained in experiencing problems in relation to being denied access to specific technical information or proprietary diagnostic tools.

Car manufacturers have participated in several initiatives through the FCAI to address the concerns expressed by independent repairers. The *Agreement on Access to Service and Repair Information for Motor Vehicles* between the FCAI, AADA, the Australian Automotive Aftermarket Association (AAAA), and the Australian Motor Industry Association (AMIA) that was signed in December 2014. The *Agreement on Access to Service and Repair Information for Motor Vehicles* ensures that service and repair information is available in a timely manner to the consumer's repairer of choice at a fair and reasonable cost. In February 2015 the FCAI established the *Voluntary Code of Practice – Access to Service and Repair Information for Motor Vehicles* to provide for an information pathway and a means of access to repair information for parties outside the authorised dealer network.

The Australian Competition and Consumer Commission (ACCC) (2017, p. 3) has found "that some car manufacturers provide independent repairers with access to most of the technical information they need to repair and service new cars" and that some car manufacturers are providing a good level of access to technical information. Despite this, the ACCC (2017, p. 122) has found that problems continue to be experienced by independent repairers in accessing technical information, and to some degree proprietary diagnostic tools, for the repair and servicing of new cars.

Competition Issues in New Car Servicing

ACCC Conclusions on New Car Servicing

It has been claimed that barriers to accessing technical information is resulting in a reduction in competition in car repair and servicing markets because independent repairers cannot compete with authorised dealers and preferred repairer networks on an even playing field (Australian Competition and Consumer Commission, 2017, p. 114). In turn, the ACCC (2017, p. 128) has come to the view that the competitive discipline imposed by independent repairers on competition in aftermarkets remains valuable and of benefit to consumers. To ensure that this competitive discipline continues, the ACCC (2017, p. 133) has recommended that a mandatory scheme should be introduced for car manufacturers to share technical information with independent repairers, on commercially fair and reasonable terms.

In reaching its conclusion, the ACCC has drawn very narrowly and selectively on the available economic and competition law (antitrust) literature that exists in relation to aftermarkets. For instance, the ACCC (2017, p. 143n) has drawn on the work of economic consultant Dr Lorenzo Coppi (2007, pp. 70-71) who has asserted:

> *There is an emerging consensus in economics that the potential for anticompetitive effects exists whenever customers are locked in, that is, they can purchase only those aftermarket products produced by the manufacturer of the primary product. … Most commentators now agree that:*
>
> 1. *The potential for harm from aftermarket monopolization is present under fairly general circumstances, even when the primary market is quite competitive and consumers are fully informed about the product lifecycle costs.*

It is submitted that if the ACCC had conducted a more thorough review of the available literature then it would have found that the circumstances in which producers can exploit consumers in aftermarkets is actually very narrow indeed and that Dr Coppi's assertions are not accurate. According to Professor Emeritus Joseph P Bauer (2007, p. 39) of Notre Dame Law School:

> *Many instances in which firms attempt to retain or expand their market shares in the aftermarket sector of a systems industry will not harm consumers. Indeed, those firms may offer a wide variety of explanations for this behavior, arguing that the use of these techniques either is efficiency-enhancing and thus has procompetitive results or, at worst, is competitively neutral.*

Tying

Precluding access for independent repairers to vehicle service and repair information could constitute an attempt on the part of car manufacturers to engage in a tying arrangement. The Commonwealth Consumer Affairs Advisory Council (CCAAC) (2012, p. 24) commented that it "would be concerned if manufacturers were engaging in conduct that effectively 'tied' or 'bundled' the supply of a new car with servicing by a dealership if this impacted on competition in the supply of automotive repair services."

Tying refers to conditioning the sale of one good on the purchase of another (Church & Ware, 2000, p. 168). In this case, a car manufacturer would condition the sale of a motor vehicle on the purchase of spare parts and servicing from the car manufacturer or their agent.

There are three potential reasons why firms seek to engage in tying behaviour:

- preservation of quality
- price discrimination or metering
- leveraging market power (Nalebuff, 2003, p. 70).

These reasons are examined further below.

Preservation of Quality

Firms may be motivated to tie for reasons related to quality (Nalebuff, 2003, p. 70). For example, if a car breaks down, then the manufacturer could suffer from a loss of reputation. Quality standards lower consumer search and information costs which tends to enhance competition (Cohen, 1996, p. 548).

Car manufacturers seek to maintain their quality standards through trade marks. A trade mark is a word, symbol, or other signifier used to distinguish a good or service produced by one firm from the goods or services of other firms (Landes & Posner, 1987, p. 268).

Trade marks promote economic efficiency through reducing consumer search costs (Landes & Posner, 1988, p. 270). Trade marks lower consumer search costs by providing consumers with a means for distinguishing between products that differ in quality but that, absent a brand name, would be difficult to distinguish at the point of purchase (Blair & Cotter, 1999, p. 13). Trade marks accomplish this goal by conferring upon the trade mark owner the right to exclude others from using the same or a similar mark on the same or related products or services, in cases in which such use would be likely to cause confusion as to source, sponsorship, or affiliation (Blair & Cotter, 1999, p. 13).

The benefits of trade marks in reducing consumer search costs require that the producer of a trade marked good maintain a consistent quality over time and across consumers (Landes & Posner, 1988, p. 271). In this way, trade mark protection encourages expenditures on quality. Rather than investigating the attributes of all goods, the consumer may find it less costly to search by identifying the relevant trade mark and purchasing the corresponding brand. For this strategy to be efficient, however, not only must it be cheaper for the consumer to search for the right trade mark than for the desired attributes of the good, but past experience must be a good predictor of the likely outcome of current consumption choices. Thus, the brand must exhibit consistent quality through time.

In turn, a firm's incentive to invest resources in developing and maintaining a strong trade mark, such as through advertising, depends on its ability to maintain consistent product quality (Landes & Posner, 1987, p. 270). Trade marks are valuable because they denote consistent quality, and a firm has an incentive to develop a trade mark only if it is able to maintain consistent quality. If a brand's quality is inconsistent, then consumers will learn that the trade mark does not enable them to relate their past to future consumption experiences and the branded product will then be like a good without a trade mark; the trade mark will not lower search costs, so consumers will be unwilling to pay more for the branded than for the unbranded good (Landes & Posner, 1988, pp. 271-272). As a result, the firm will not earn a sufficient return on its expenditures promoting the trade mark to justify the expenditures. Similarly, a firm with a valuable trade mark would be reluctant to lower the quality of its brand because it would suffer a capital loss on its investment in the trade mark.

Price Discrimination

Firms may also be motivated to tie in order to engage in price discrimination or metering. Price discrimination occurs when like goods or services are provided to different persons at different prices, the difference in price being unrelated to the cost of providing the goods or services (Dawson, Segal, & Rendall, 2003, p. 89).

If a customer’s value for a product is positively related to their intensity of use, then it will typically be possible to extract more consumer surplus through a two-part pricing scheme (Nalebuff, 2003, p. 70). The consumer pays some reduced initial price for the product plus a per-use fee (Nalebuff, 2003, pp. 70-71). This allows a firm to charge more to high-value customers, while still making sales at lower prices to low-value customers (Nalebuff, 2003, p. 71).

In what has been described as a *razor/razor blade* strategy, a manufacturer will sell the durable good in the primary market relatively cheaply, earning the bulk of its profits from sales in the aftermarket (Glick & Cameron, 1999, p. 357). This has been characterised as second-degree price discrimination

whereby the producer sells different units of output for different prices, but every individual who buys the same amount of the good pays the same price.

Economic theory provides no general guidance as to whether price discrimination increases or decreases overall efficiency, consumer surplus or total output (Shapiro, 1995, p. 499).

The objective of any monopolist or participant in a tacitly collusive agreement is to reduce output and raise prices to increase profits. For this reason, Professor Hal Varian (1996) of the University of California at Berkeley has commented in regard to the welfare effects of price discrimination that:

> *… if price differentiation allows more consumers to be served it will generally increase welfare... Market segmentation that allows markets to be served that would otherwise be neglected is also a case where overall welfare can be expected to be enhanced.*
>
> *On the other hand, price differentiation that merely shuffles prices paid by pre-existing customer groups and that does not result in an increase in the number of customers served, or the amount that they consume, will tend to reduce overall welfare.*
>
> *...*
>
> *The key concern in examining the welfare consequences of differential pricing is whether or not such pricing increases or decreases total output.*

According to Commissioner Dr Stephen King (2011) of the Productivity Commission:

> *Price discrimination may not be a bad thing. To the degree that it puts a wedge between consumers' marginal valuations for the same product (in other words, different consumers face different prices) price discrimination leads to a loss in economic surplus. But price discrimination also changes the quantity of product sold. To the degree that total sales rise with price discrimination, there may be an overall economic benefit.*

In its 2008 grocery inquiry, the ACCC made the following observations in regard to price discrimination:

> *The ACCC considers that there can be significant economic efficiency and competition benefits resulting from price discrimination … (Australian Competition and Consumer Commission, 2008, p. 552)*
>
> *The ACCC recognises that there can be genuine economic efficiency reasons for price discrimination. (Australian Competition and Consumer Commission, 2008, p. 553)*

According to distinguished American economist William Baumol Baumol (2005, p. 31):

> *... it should be noted that the market's imposition of discriminatory pricing in a wide range of circumstances is not necessarily to be deplored. It has long been known ... that discriminatory prices can enhance output and increase economic welfare.*

Professor Varian (1996) has observed that price discrimination is ubiquitous in industries that exhibit large fixed costs. Where fixed costs are high, pricing at short-run marginal cost would prevent firms

being able to fully recover their fixed costs which would have a detrimental impact on future investment decisions as well as product provision. Under these circumstances, price discrimination that enables firms to recover their fixed costs can be beneficial. According to Professor Damien Geradin and Nicolas Petit of the University of Liege (2006, pp. 484-485):

> *A key insight of economics is that price discrimination is most likely to expand output where the seller has declining average total costs. Expanding output through price discrimination is an essential strategy for firms facing problems of fixed cost recovery. Price discrimination allows firms facing large fixed costs (in practice all firms that make substantial investments) to expand their output and thus spread fixed costs over a large number of units. When marginal costs are low … any positive price allows the firm to contribute to its fixed costs. Prohibiting price discrimination would thus prevent efficient recovery of fixed costs and would, in the long run, have a negative impact on investments.*

In relation to fixed costs in car manufacturing, the Productivity Commission (2014, p. 50) has observed:

> *There are large fixed costs involved in manufacturing vehicles, starting with the design of new platforms and models, and new powertrains, as well as in general market research and advertising. These costs are usually incurred by motor vehicle producers at a global level, particularly with the move toward global platforms (discussed below). There are also large fixed costs associated with establishing infrastructure and equipment at the plant level (and retooling for upgrades and new car models).*

According to Professor Mark Glick of the University of Utah and economic consultant Duncan J Cameron (1999, pp. 358-359):

> *We think that the razor/razor blade strategy frequently, if not generally, benefits rather than harms consumers. … the strategy of pricing the initial product low and earning profits on aftermarket sales tends to succeed only with good product quality and aftermarket support. As a result, the pricing strategy itself providers important consumer information about product quality and continued support. This pricing strategy also makes the products accessible to a larger base of users. In addition, the razor/razor blade strategy typically will increase manufacturer profits and incentives for innovation, and consumer welfare. Our ultimate conclusion is that the razor/razor blade strategy is more likely to benefit competition and that the antitrust laws should more explicitly allow for the protection of proprietary aftermarkets when it does.*

Leveraging Market Power

Leveraging occurs where market power in one market is leveraged to obtain a competitive advantage in a second market (Chang, 2009, p. 328).[3] Traditionally, leveraging was viewed as a threat to competition under the assumption that a firm with market power could reap additional profits by leveraging their power into a second market. The ability to leverage market power across from one market into another market would see market power exercised in two markets and thus increase the overall level of profitability.

[3] A firm possesses market power when it can behave persistently in a manner different from the behaviour that a competitive market would enforce on a firm facing otherwise similar cost and demand conditions. (Kaysen & Turner, 1959, p. 75).

The theory of leveraging has been a controversial topic in the field of competition law and economics. The so-called *Chicago* school of antitrust has queried the ability of firms to leverage market power from one market across to another market and thereby increase the overall level of profits. According to this line of reasoning, a firm with pre-existing market power in one market will not be able to leverage this market power over to another market and thereby extend its overall level of market power and increase the overall level of profits (Bork, 1978, p. 372).

While the Chicago school view on leveraging has not gone unchallenged (Kaplow, 1985; Clarke-Smith, 2002), Professor Barry Nalebuff (2003, p. 88) of the Yale School of Management has observed:

> *This idea of leveraging power is a commonly told story, but it is not one that has a solid theoretical or empirical basis.*

The notion of car manufacturers leveraging their market power presupposes the existence of any meaningful market power on their part in the first instance. The available evidence suggests that new car manufacturing worldwide as well as new car retailing in Australia is extremely competitive, with the Productivity Commission observing:

> *Competition within the global automotive industry is intense…*
>
> *As a result of this competition, especially amongst the lower-priced, high-volume vehicle models, there is limited ability for producers to raise their prices …*
>
> *The limited scope for producers to raise their selling prices within particular vehicle market segments has resulted in cost pressures throughout the automotive supply chain. (Productivity Commission, 2014, pp. 48-49)*

and

> *The highly competitive Australian automotive market limits the scope for all sellers of cars in Australia to increase the selling price of their vehicles. (Productivity Commission, 2014, p. 67)*

Aftermarket Tying – Competition or Contracting Failure?

In its 1992 decision in the matter of *Eastman Kodak Co. v. Image Technical Services Inc.* (*Kodak*), the US Supreme Court found that a nondominant firm could abuse its market power with respect to "locked in" purchasers of the primary product in the aftermarket.[4] Kodak sold high speed photocopiers (Hovenkamp, 2005, p. 98). The largest firm in the market was Xerox, and Kodak's share of the copier market was only 23 per cent. However, consumers who already owned a Kodak photocopier were said to be "locked in" to Kodak's replacement parts because these parts were unique in that many of them were not interchangeable with the replacement parts for Xerox or other machines.

A "lock-in" raises concerns regarding the ability of a durable goods manufacturer to charge prices above the competitive level for their aftermarket parts and/or services (Goldfine & Vorrasi, 2004, p. 212). In this case, it has been suggested that a consumer could be "locked-in" to paying a higher price for aftermarket goods and services by virtue of their original investment in a durable good.

[4] 504 U.S. 451 (1992).

Tying customers in an aftermarket does not pose a problem if customers are reasonably well informed and are able to engage in life-cycle pricing. Life cycle costing refers to a buyer's contemplation at the time of purchase of not only the initial purchase price, but also expected future costs including any subsequent maintenance, repairs, parts, or services purchased over the expected duration of the product's use (Gundlach, 2007, p. 25).

However, the US Supreme Court raised concerns that there might be a group of myopic, or uniformed buyers who could be duped because they lacked the information to engage in life-cycle cost calculations (Hovenkamp, 2005, p. 98).[5] These buyers would not discover that aftermarket price were too high until after they had made their purchase in the primary market.

Customers who invest in a proprietary durable good are vulnerable to hold-ups. An investment in a specialised asset creates quasi-rents which provide the potential scope for opportunistic behaviour.[6] A quasi-rent value of an asset has been defined as the excess of its value over its salvage or its value in its next best use to another renter (Klein, Crawford, & Alchian, 1978, p. 298). The potentially appropriable specialised portion of the quasi-rent is that portion, if any, in excess of its value to the second highest-valuing user (Klein, Crawford, & Alchian, 1978, p. 298).

Asset specificity creates the scope for opportunistic behaviour that leads to the hold-up problem as outlined by former Industry Commission economist Jim Rose (1999, pp. 81-82):

> *Asset specialisation creates openings for opportunistic behaviour in which one party to the relationship manoeuvres to extract wealth from the other; and that wealth is wealth that could not be extracted in the absence of the interdependence. Specialised assets are vulnerable to hold-ups.*

The ACCC has previously recognised the possibility of a hold up occurring in a matter before the Australian Competition Tribunal:

> *... a contracting problem that can arise where (a) incomplete or otherwise limited contracts exist between two or more parties who can engage in a mutually beneficial activity, and (b) prior to the parties engaging in the mutually beneficial activity, one of the parties must make an investment that is substantially sunk and, as such, the recoverable value of the investment for the investor is significantly below the initial investment cost. 'Hold up' occurs in this situation when the party making the relevant investment cannot, through the contracting process and prior to making his or her investment, be guaranteed to receive an adequate share of the returns from the mutually beneficial activity after the investment is made and the activity occurs.*[7]

Professor Emeritus Benjamin Klein (1993, pp. 50-51) of the University of California Los Angeles has characterised the potential for hold-ups in durable good aftermarkets as a failure to contract:

> *Buyers aware of a "hold-up" potential will protect themselves either by dealing with sellers that possess sufficiently large reputations for fair dealing and, therefore, who have more to lose than they could gain by a "hold-up" policy or*

[5] 504 U.S. 451 (1992) at 473-475.
[6] Opportunism has been described as a variety of self-interest seeking but extends simple self-interest seeking to include self-interest seeking with guile (Williamson, 1979, p. 234).
[7] Re VFF Chicken Meat Growers' Boycott Authorisation [2006] ACompT 2, para. 103.

> *they will write contract terms that prevent "hold-ups" by limiting what the seller can do.*

Klein (1993, p. 52) suggests that in order to protect themselves from hold-ups in aftermarkets, all consumers need to do is to contract with durable good manufacturers:

> *The important general point that can be made from what we know about "hold-up" problems is that ... buyers need not be fully knowledgeable, and, in particular, need not know all future aftermarket prices at the time they make their equipment purchase, in order to avoid a "hold-up." Buyers need only know that switching costs are present and, therefore, that a "hold-up" potential exists. This will motivate buyers ... to take the relevant precautions, namely demanding sufficient reputation capital and/or contract protection.*

According to distinguish competition law scholar Professor Herbert Hovenkamp (2005, p. 99) of the University of Pennsylvania, the *Kodak* decision risks turning competition law into a free-ranging engine for repair of any contract that either deceives or has not taken every possible contingency into account.

Initiatives by car manufacturers in relation to aftermarket contracting of new car buyers are outlined further below.

Other Anticompetitive Detriments with Aftermarket Tying

According to the US Supreme Court in its *Kodak* decision:

> *If the cost of switching is high, consumers who already have purchased the equipment, and are thus "locked in," will tolerate some level of service-price increases before changing equipment brands. Under this scenario, a seller profitably could maintain supracompetitive prices in the aftermarket if the switching costs were high relative to the increase in service prices, and the number of locked-in customers were high relative to the number of new purchasers.*[8]

Switching costs are the additional costs over the market price that consumers incur if they elect to abandon their investment and switch to another product (Goldfine & Vorrasi, 2004, p. 213). The costs of switching increase when consumers are unable to recover the useful life of their investment in a product if they choose to shift to another brand. Large switching costs lock in a consumer once they have made an initial product purchase, so they are effectively buying a series of goods and services (Farrell & Klemperer, 2007, p. 1972).

The reasoning outlined by the US Supreme Court in its *Kodak* decision is consistent with the ACCC's view that customer switching between new car brands is unlikely to impose any competitive constraint on car manufacturers:

> *Consumer switching in the new car market is unlikely to provide strong competitive discipline on manufacturers and dealers in aftermarkets … (Australian Competition and Consumer Commission, 2017, p. 129)*

The FCAI concurs with the ACCC that because switching costs are high, that consumer switching in turn provides no short-term competitive constraint on the behaviour of producers and related

[8] 504 U.S. 451 (1992) at 476.

entities in aftermarkets. However, the available literature suggests the situation is far more complicated and nuanced than the ACCC is suggesting and that there are other mechanisms available to protect consumers in aftermarkets and discipline producers.

According to Professors Carl Shapiro and David Teece from the University of California at Berkeley (1994, p. 148):

> *... aftermarket power is most likely to be significant if switching costs are high and long lived, if customers lack the protection of long-term contracts, and if information costs prevent most customers from engaging in life-cycle costing.*

According to Professor Shapiro (1995, pp. 487-488), there are four theories of consumer exploitation in aftermarkets:

1. *The Surprise Theory*. The durable goods manufacturer can engage in exploitation of locked-in consumers in aftermarkets by making unexpected changes in policies that exclude aftermarket rivals and thus allow the manufacturer to extract more money from consumers who have already purchased the good.
2. *The "Costly Information" Theory*. There are a large number of myopic or poorly informed consumers who fail to account for aftermarket costs when purchasing the durable good. Since these consumers are not frightened away by monopolistic aftermarket prices, it creates incentives for manufacturers to extract the greatest profits possible from these locked-in consumers.
3. *The "Limited Manufacturer Commitment" Theory*. The durable good manufacturer has limited ability, at the time a consumer purchases the durable good to make credible and binding price and quality commitments for aftermarket service. As a result, the manufacturer inevitably takes advantage of customers in the aftermarket, at least to some degree, if not prevented from doing so by aftermarket competition.
4. *The "Price Discrimination" Theory*. A firm with market power in the overall interbrand market for the durable good as well as associated aftermarket goods and services can price discriminate more effectively if it can separately control the prices of parts and service for its durable good. Exclusion of aftermarket rivals can therefore be profitable by permitting enhanced price discrimination by the manufacturer.

The first three theories are discussed further below. As price discrimination as already been considered above, it will not be discussed further.

The Surprise Theory

In relation to the Surprise Theory, Shapiro (1995, p. 488) notes that any consumer injury would likely be short-lived, and typically confined to those consumers who already owned the durable good by the time the manufacturer made its policies more restrictive or less favourable to consumers and aftermarket rivals. Shapiro (1995, pp. 488-489) suggests that consumers will have strong incentives to obtain contractual protections to prevent their exploitation in aftermarkets through various mechanisms including:

1. Warranty Coverage. By obtaining warranty coverage, the consumer contracts for some service when the durable good is purchased before any lock-in occurs.
2. Long-Term Service Contracts. Buyers frequently obtain long-term service contracts concurrently with the purchase of durable goods.

These types of contractual arrangements all serve the function of shifting the consumer's purchases from the aftermarkets to the durable goods market (Shapiro, 1995, p. 489). It should be noted that such contractual arrangements are now widely available with the sale of new cars in Australia and likely to continue to expand in scope and coverage. According to the AADA (2015, p. 5):

> *The intense competition in the Australian motor vehicle retail market has led to a situation where manufacturers … , distributors and dealers augment the consumer guarantees under the ACL by offering additional consumer benefits including warranting a vehicle for longer than required by the ACL guarantees, or providing free or capped price servicing. Such offers have obvious public benefits.*

Hyundai introduced five-year warranty coverage back in 1999 with Mitsubishi following in 2004 (Dowling, 2020). In recent years most car manufacturers have moved to extend their new car warranties from three years to five years (Jeremic, 2019a). In 2014 Kia offered its 7-7-7 deal (seven years warranty, roadside assist and capped-price servicing). In July 2017 Honda rolled out a five-year and unlimited kilometre warranty on all vehicles (Costello, 2017).

In 2018 Holden, Ford, Mazda and Volkswagen all increased their coverage from three to five years, with Toyota and Subaru following suit in the first week of 2019. In April 2019, Nissan became the last of the top selling brands to offer a 5 year warranty (Jeremic, 2019b). In September 2020 Mitsubishi began offering a 10 year or 200 000km (whichever occurs first) warranty to purchasers of new Mitsubishi vehicles on the condition that those consumers acquire aftermarket servicing for their new vehicle exclusively from a Mitsubishi dealer or service centre (Australian Competition and Consumer Commission, 2020, p. 1).

Basically every car manufacturer operating in Australia has introduced capped-price servicing on its vehicles in recent times (Jeremic, 2019). Capped price servicing is used to give transparency of the cost of each scheduled service ahead of time instead of revealing the cost at the end (Camden Haven Courier, 2019). In some cases the capped-price servicing plans are built into the purchase of the car. Capped-price servicing sets a maximum price that a dealer can charge for a particular service (Fung, 2020).

Luxury car makers have by-and-large opted to offer pre-paid servicing schemes instead (Fung, 2020). Pre-paid service plans are popular overseas and lock in pricing years in advance. Pre-paid servicing can be bought at the same time as the car, or at any time prior to a car's first scheduled service.

Additional consumer protection is afforded by damage to the reputation of a manufacturer if they seek to exploit their customers in aftermarkets. This is because the damage done to a manufacturer's reputation through consumer exploitation in aftermarkets may not be limited to the product market in question, but undermine the consumer's trust in the firm, or alter the consumer's expectations on how that manufacturer will behave in the future, thereby undermining the brand in general (Shapiro, 1995).

The "Costly Information" Theory

In relation to the Costly Information Theory, if most buyers are ignorant of aftermarket costs when buying a durable good, then a competitive durable good market might do little in assisting in protecting them in ensuring competitive aftermarkets (Shapiro, 1995, p. 492). However, Shapiro

(1995, p. 492) observes that competitive durable goods markets still offer substantial protections to consumers even if they are poorly informed or myopic.

According to Shapiro (1995, p. 493), information costs are lowered by:

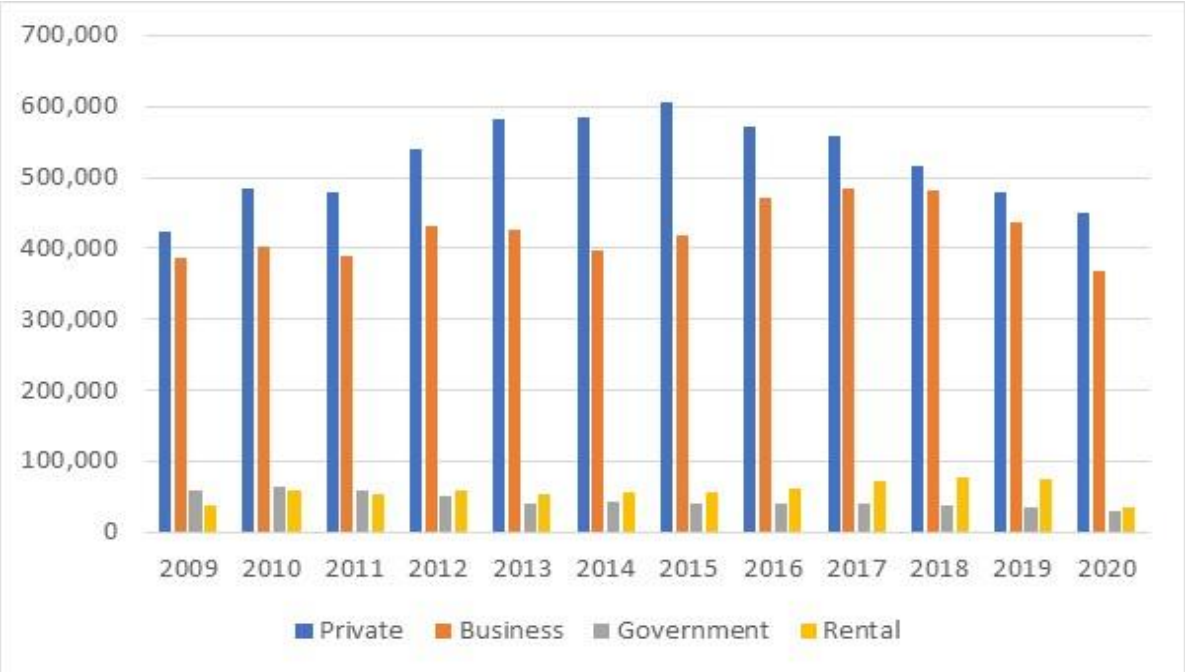
1. third party sources of information such as consultants, brokers and publications
2. buyers' ability to spread information costs over multiple units
3. repeat buyers who have experience with life cycle costs.

Thus Shapiro (1995, p. 493) observes the Costly Information Theory is unlikely to apply for expensive equipment and very difficult to sustain where buyers are large and/or experienced. The Costly Information Theory is only viable if customers are unable to evaluate equipment on a life-cycle basis, which is difficult to argue if the equipment is expensive and the buyers are businesses (Shapiro, 1995, p. 501).

In any event it is not necessary for all consumers to have good information in order for aftermarket prices to be disciplined by durable good market competition (Shapiro, 1995, p. 493). Instead, poorly informed buyers can be protected by informed buyers, whose presence forces durable goods manufacturers to compete on a total cost of ownership basis, especially as it may be difficult for sellers to identify poorly informed buyers so as to price discriminate against them.

The evidence for Australia suggests the Costly Information Theory is unlikely to be applicable to the new car market given that new car sales are fairly evenly split between private buyers and sophisticated purchasers (including fleet, rental and government purchasers) who are presumably well informed consumers (even if one makes the rather large assumption that most private buyers are ill-informed). This is outlined in Figure 1 below.

*Figure 1: New Car Sales by Buyer Type – 2009 to 2020**



Source: VFACTS database.

* Includes sales of passenger motor vehicles, sports utility vehicles and light commercial vehicles.

Even if consumers were to suffer from exploitation in aftermarkets due to the Costly Information Theory, Shapiro (1995) argues the welfare implications would be limited and reduced as consumers would be compensated by discounting in the durable good market once exploitation in the aftermarkets was taken into account by the manufacturers.

The "Limited Manufacturer Commitment" Theory

The notion behind the Limited Manufacturer Commitment Theory is that because manufacturers cannot commit to aftermarket prices due to imperfections in the contracting process, they will inevitably be tempted to raise their aftermarket prices to consumers to above the competitive level and thus exploit their locked-in customers (Shapiro, 1995, p. 495). In this instance, reputation does provide some constraint on the conduct of the manufacturer. It may not be profitable for a manufacturer to charge above-competitive aftermarket prices to locked-in service customers if the information easily spreads, inducing potential new consumers to purchase other brands (Borenstein, MacKie-Mason, & Netz, 2000, pp. 162-163).

According to Shapiro (1995, p. 496) the Limited Manufacturer Commitment Theory implies that each manufacturer has the incentive to try to offer stronger commitments to consumers than other manufacturers in order to gain market share that in turn will offer additional consumer protection and reduce the level of exploitation. The proliferation of extended warranties and capped price servicing packages being offered to new car purchasers through authorised dealers at the instigation of manufacturers is a pertinent example of stronger commitments being provided to new car purchasers. According to the AADA (2016, p. 4):

> *Consumers are also additionally protected by the issue of an express warranty to the purchaser of any new vehicles which entitles a consumer to various contractual remedies, such as repair and replacement of parts at no cost to a consumer for a period which may be up to 7 years.*

In any event, Shapiro (1995, p. 497) has expressed scepticism as to whether competition law is appropriate mechanism to responding to the anticompetitive detriment posed by the Limited Manufacturer Commitment Theory:

> *I am not convinced that this type of consumer injury is worthy of the attention of antitrust laws. This injury tends to be far smaller than traditional monopoly overcharges and deadweight losses. I am sceptical that good antitrust policy requires the courts to be involved in regulating the conduct of businesses unless significant consumer injury or inefficiency is involved.*

Like the Costly Information Theory, the Limited Manufacturers Commitment Theory also suffers from the fact that any consumer detriment will be diminished by competition and discounting in the durable good market (Shapiro, 1995, p. 501).

Electronic Logbooks

Some car manufacturers have replaced traditional manual based logbooks with online logbooks operated in a secure database through their authorised dealer network.

When a consumer brings their vehicle into an authorised service provider for servicing, the authorised service provider can log into the database and bring up the vehicle's records contained in the online logbook. This assists in identifying what services are required. Once the authorised service

provider has completed the service, they will update the online logbook and provide a printout of the service for the consumer.

Unlike manual logbooks, the online logbooks provides a complete service history for vehicles serviced within the authorised dealer network. Manual logbooks typically only contain very limited details on services, and usually only involves a stamp from the service provider certifying the service was completed and a record of whether brake fluid was replaced.

Consumers are able to access the information contained in online logbooks either through logging in on a personalised online account, or through requesting a copy of the service information through an authorised dealer.

The provision of online logbooks is a means through which authorised dealers can provide a differentiated and qualitatively superior record keeping service to customers.

While independent repairers cannot access online logbooks, there is absolutely no attempt to foreclose service and repair markets and exclude independent repairers. This is because consumers still have the freedom to choose servicing from independent repairers if they wish to do so, and can provide independent repairers with access to the information contained in an online logbook.

While independent repairers are not able to update an online logbook, it also does not preclude a consumer from maintaining their own manual logbook of servicing for the purposes of increasing the resale value of a vehicle.

An inability on the part of independent repairers to access an online logbook only raises competition issues in the event that it results in an input foreclosure. Input foreclosure occurs where the upstream division of a vertically integrated entity by denying (i.e. refusing to sell) its input, degrading the quality of the input sold, or discriminating by raising the input price to one or more downstream firms (Salop & Culley, 2014, p. 13). Foreclosure of sources of supply of inputs can affect competition adversely, although the conditions necessary for such harm are stringent (Areeda, Hovenkamp, & Solow, 2006, p. 166). However, according to the authoritative *Antitrust Law*:

> *It cannot be emphasised too strongly that "small" foreclosures cannot impair competition. (Areeda, Hovenkamp, & Solow, 2006, p. 167)*

Application of Existing Competition Law

Competition Law and the Rule of Reason Approach

Where OEMs seek to control repair markets and this substantially reduces competition and harms consumers, there are remedies already available under the *Competition and Consumer Act 2010* (CCA) (Productivity Commission, 2020, p. 11). Relevant provisions contained in Part IV of the CCA relating to restrictive trade practices include:

- s. 45 that prohibits making or giving effect to contracts, arrangements or understandings containing a provision which has the purpose, effect or likely effect of substantially lessening competition
- s. 46 where a corporation with a substantial degree of power in a market is not allowed to take advantage of this power by engaging in conduct that has the purpose, effect, or likely effect of substantially lessening competition in a market

- s. 47 prohibits various forms of exclusive dealing where the restriction has the purpose, effect, or likely effect of substantially lessening competition.

In discussing these provisions, the Productivity Commission (2020, p. 11) observes:

> *In principle, these provisions cover competition issues in repair markets, although their application in repair markets is challenging and requires demonstration that the conduct has the purpose, effect or likely effect of substantially lessening competition.*

The above statement appears to amount to almost a tacit admission that existing problems that independent repairers may encounter in relation to accessing information and data to repair new cars are not actually likely to raise compliance issues in relation to Part IV of the CCA under a rule of reason approach.

Where a statute imposes severe sanctions for violations, society generally holds that the costs of false positives exceed those of false negative (Arthur, 2000, p. 340). Judge Frank F. Easterbrook (1984, p. 17) of the US Court of Appeals for the Seventh Circuit has declared the challenge for competition law is to create simple rules that filter the category of probably-beneficial practices out of the legal system, leaving to assessment under a rule of reason approach only those with significant risks of competitive injury. The rule of reason requires an assessment and balancing of a restraint's harms, benefits and alternatives (Areeda & Hovenhamp, 2003, p. 391). Under the rule of reason approach, a practice is only condemned if it is found to interfere with competition unreasonably (Posner, 2001, p. 39). According to Judge Easterbrook (1984, pp. 39-40):

> *Each filter should be designed to screen out beneficent conduct and pass only practices that are likely to reduce output and increase price…*
>
> *The filters deal with the ingredients of anti-competitive practices. If there is no market power, if the defendant cannot profit by reducing output, or if the conduct fails any of the other tests, there is no substantial competitive problem.*

In order to ameliorate the risk of false positives, it is absolutely critical there are appropriate filters to help separate pro-competitive conduct from anti-competitive conduct.

Protecting Competition or Certain Competitors?

Parties are able to obtain legal protection to engage in exclusive dealing conduct that might otherwise breach s. 47 of the CCA through lodging an exclusive dealing notification with the ACCC.

In September 2020 Mitsubishi lodged an exclusive dealing notification with the ACCC (2020) to offer a 10 year or 200,000km (whichever occurs first) warranty to purchasers of new Mitsubishi vehicles on the condition that those consumers acquire aftermarket servicing for their new vehicle exclusively from a Mitsubishi dealer or service centre.[9] The ACCC came to the conclusion that the Notified Conduct was unlikely to have the purpose, effect or likely effect of substantially lessening competition.

When push came to shove on the competitive merits of right to repair and exclusive dealing, and the ACCC faced the prospect of review of its decision making by the Australian Competition Tribunal, the

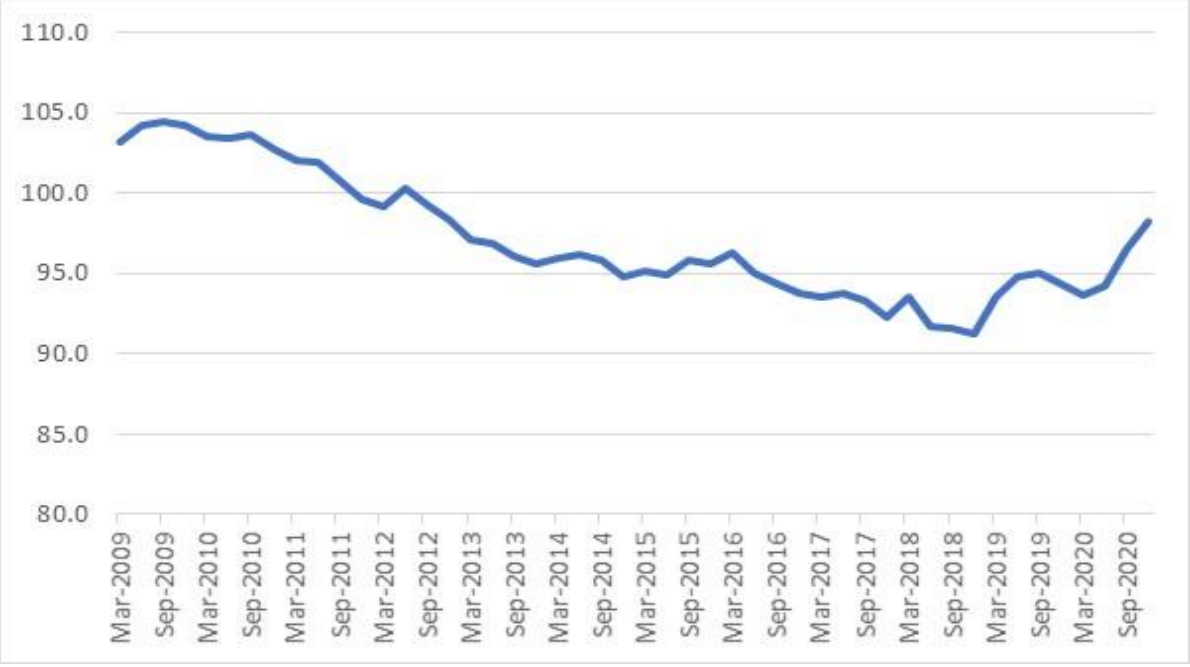
[9] Under s. 93 of the CCA, a business can obtain legal protection to engage in exclusive dealing conduct that might other breach s. 47 of the CCA by lodging an exclusive dealing notification.

ACCC was forced to acknowledged that such exclusive dealing conduct was unlikely to raise compliance issues under s. 47 of the CCA.[10]

Under the existing competition law, a manufacturer has no duty to aid an aftermarket entrant. While a manufacturer has no duty to aid a competitor, a manufacturer does not have unfettered discretion to impede a competitor through technological innovation (Glick & Cameron, 1999, p. 380). Provided that design changes can be justified by either improvements in quality or reductions in costs, then it is arguably the case that a car manufacturer faces no compliance issues in relation to Part IV of the CCA. This is highly unlikely to raise issues for car manufacturers.

In measuring rises in the consumer price index (CPI), so that it can measure 'like' products with 'like' products, the Australian Bureau of Statistics (ABS) makes adjustments to prices when there has been changes in the quality of a product. For motor vehicles, the ABS (2018, p. 32) makes adjustments for quality in relation to safety and fuel efficiency. Because there is a continuing increase in the number of features added to new cars, the ABS has continually adjusted the price of motor vehicles down to take in account the ongoing improvements in the quality of the vehicles.[11] This means that while the cost of vehicles can increase over time, the motor vehicle purchase component of the CPI (CPIMV) has gone through extended periods of decline. This can be seen in Figure 2 below that reveals the quality adjusted cost of motor vehicles in December 2020 was actually lower than it was March 2009.

Figure 2: Quarterly index numbers for the motor vehicle purchase component of the consumer price index – March 2009 to December 2020



Source: ABS (Australian Bureau of Statistics, 2021)

[10] The giving of a final notice to revoke a notification by the ACCC is subject to review by the Australian Competition Tribunal under s. 101A of the CCA.

[11] Although the CPIMV does include the sale of used cars, this relates only on the transfer of ex-government and ex-business to the household sector (Australian Bureau of Statistics, 2018, p. 38), which would be reasonably close substitutes for new cars because they wouldn't be that old.

If no car manufacturer is likely to face compliance issues under the CCA for withholding servicing and repair information from independent repairers, this raises two distinct possibilities: either there is a gap in the existing restrictive trade practices provisions of the CCA; or the policy intent of right to repair regulation serves some other policy intention.

In arriving at a list of attributes for the application of a workable competition (antitrust) policy, Judge Easterbrook (1986, pp. 1700-1701) has warned:

> *No antitrust policy should be based on a belief that courts and other institutions of government can identify the "best" structure of a market. The history of regulation demonstrates that intervention in pursuit of such goals will be unsuccessful or the playground of special interest groups.*

In the absence of anyone making a serious case of a gap in the existing restrictive trade practices provisions of the CCA as they relate to right to repair, this leaves the distinct possibility that right to repair is being pursued at the behest of special interest groups. This would in turn suggest that right to repair regulation, including the proposed Part IVE of the CCA (motor vehicle service and repair information sharing scheme), is being pursued in order to protect certain competitors rather competition.

The High Court has clearly articulated on a number of occasions that the purpose of the CCA (formerly the *Trade Practice Act 1974*) is to protect the competitive process rather than individual competitors. According to the former Chief Justice Gleeson and former Justice Callinan of the High Court in the *Boral* judgement:

> *The purpose of the Act is to promote competition, not to protect the private interests of particular persons or corporations. Competition damages competitors. If the damage is sufficiently serious, competition may eliminate a competitor.*[12]

According to former Justices Gaudron, Gummow and Hayne in the *Boral* judgement:

> *The structure of Pt IV of the Act does, despite the considerable textual differences, reflect three propositions found in the United States antitrust decisions. The first is that these laws are concerned with "the protection of competition, not competitors". The second … is that "[e]ven an act of pure malice by one business competitor against another does not, without more, state a claim under the federal antitrust laws; those laws do not create a federal law of unfair competition or 'purport to afford remedies for all torts committed by or against persons engaged in interstate commerce'." The third … is that it is in the interest of competition to permit firms with substantial degrees of power in the market (or, in the United States, a dominant position) to engage in vigorous price competition and that it would be a perverse result to render illegal the cutting of prices in order to maintain or increase market share.*[13]

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[12] *Boral Besser Masonry Limited (now Boral Masonry Ltd) v Australian Competition and Consumer Commission* [2003] HCA 5 at 87.
[13] [2003] HCA 5 at 160.

Intellectual Property Protection

Repair and service information and data is knowledge created by vehicle manufacturers during the development of new cars and is their intellectual property. Property rights refers to an owner's right to use a good or asset for consumption and/or income generation (referred to as use rights) (Besley and Ghatak, 2010, p. 4526). A property right includes the right to exclude others.

Intellectual property refers to creations of the mind: inventions; literary and artistic works; and symbols, names and images used in commerce (World Intellectual Property Organization, 2012a, p. 2). Intellectual property rights are like any other property right in that they allow creators, or owners, to benefit from their own work or investment in a creation.

Repair and service information and data is the intellectual property of vehicle manufacturers that is usually referred to as trade secrets. A trade secret is any proprietary knowledge or any confidential information that has value for a company (IP Australia). As a signatory to the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), Australia must have a legal system for protecting trade secrets from unfair disclosure (Article 39.2).

It has been contended that exclusionary practices in aftermarkets by durable goods manufacturers enhances the returns they receive from exploiting their intellectual property. According to Associate Professor Boylston Herndon (2002, p. 326):

> *… the extension of a "parts monopoly" to a "service monopoly" may serve as an efficient means for the manufacturer to capture the returns from its investment in intellectual property.*

Similarly, According to the OECD (Organisation for Economic Co-operation and Development, 2017, p. 2):

> *Such conduct (often of an exclusionary nature) can be objectively justified by IP and efficiency considerations.*

The promotion of aftermarket competition through the right to repair regulation places an undue emphasis on allocative efficiency and price competition over dynamic efficiency that in turn risks undermining innovation and intellectual property protection.

Efficiency in competition economics is multifaceted encompassing several different concepts. Allocative along with productive efficiency are static concepts of efficiency. Static efficiency refers to holding society's technological know-how constant (Kolasky & Dick, 2003, p. 247). On the other hand, dynamic efficiency refers to the efficiency benefits achieved through research, development, and innovation, including the diffusion of technology to produce new products and processes (Fox, 2008). Dynamic efficiency brings benefits to consumers either through the introduction of improved new products that buyers value more highly ("product innovations"), or through the use of new, lower cost ways of producing existing products ("process innovations") (Commerce Commission, 2003a, p. X)

Competition law is often directed toward the preservation of allocation efficiency. For example, the ACCC (2002, p. 226) has previously stated that the theoretical case for competition laws has been traditionally founded on the need to protect allocative efficiency.

Sometimes there are trade-offs between the different concepts of efficiency. For example, the 2009 Nobel Laureate for economics, Oliver Williamson (1968), postulated a trade-off model to assess the societal benefits and detriments of mergers. Under Williamson's *naïve trade-off model*, it is possible for the improved productive efficiency achieved through the creation of a merged firm to outweigh the detrimental consequences through the loss of allocative efficiency from allowing the merger to proceed.

In terms of trade-offs, economists generally place greater emphasis on dynamic efficiency because it is the main driver of economic growth over the longer term. The reason why economies continue to grow despite the diminishing marginal product of capital is due to the cumulative improvements in technique (Romer, 1994). While capital investments by individual firms remain subject to diminishing returns, improvements in the techniques of production through innovation ensure that there is no decline in the marginal product of capital at the aggregate level.

Both economic arguments and empirical studies of the literature have confirmed that dynamic efficiency gains are more important for social welfare than static efficiency gains (Evans & Hughes, 2003, p. 12).

Regulation that delays investment and innovation may delay beneficial effects on future surpluses that can arise from such things as lower costs and new products. In turn, regulation that results in a missing market will result in the loss of the entire consumer and producer surplus (Evans & Hahn, 2010, p. 5). Similarly, a delay induced by regulation will see the total surplus of that market missing for the period of the delay. The entire combined consumer and producer surplus in a market usually dwarfs a traditional deadweight loss triangle (Goolsbee, 2006).

Information can be like any other commodity in that it can be costly to obtain (Productivity Commission, 2005, p. 48). The costs of obtaining information may not just be financial – they may also include the opportunity cost devoting time and effort that could be spent elsewhere (Productivity Commission, 2005, p. 48). Cost of obtaining information can be considered as a transaction cost.

On the other hand, information can have some characteristics of a public good (Productivity Commission, 2005, p. 49). A pure public good has the characteristics of non-rivalry in consumption and being non-excludable. Non-rivalry is where the consumption of one individual does not diminish the amount of product available for other consumers. Non-excludability means that it is not possible to exclude anyone from consuming the product. Information can be used many times over without reducing what is available to others, and it can sometimes be difficult to exclude its use by others.

Information that is easy to replicate has the property of non-rivalry (Shapiro & Varian, 1997, p. 9). However, the question as to whether information has the property of non-excludability is more problematic. Because some forms of information are or can be made excludable and because the returns from some forms of information can be appropriated (there is some degree of excludability), information can be considered an impure public good (Stiglitz, 1999). A public good that becomes excludable is a club good (McNutt, 2000, p. 928).

Because repair and service information and data is information that is potentially easy to replicate on the hand, and potentially excludable on the other, it has the characteristic of a club good. The

thrust of club theory is that the competitive market will function efficiently to provide club goods, so there is no reason that such goods should be publicly provided at all (Scotchmer, 2002, p. 1999). Through excludability individuals who do not contribute to the financing of the club can be prevented, at relatively low cost, of gaining access to the benefits of club membership (Anderson, Shughart II, & Tollison, 2004, p. 176). Essentially, clubs exist to confer benefits on members and to exclude free riders.

Because information, unlike a tangible good, can be used without being used up and can be sold without being given up, it means that information will generally be sold on condition that it must not be shared with others in order to maintain its excludability from free riders.[14] Otherwise, an inability on the part of information creators to protect their information in this manner will act as a disincentive to information creation and deterrent towards innovation, the main driver of economic growth in the long term.

Because repair and service information and data is expensive to create for car manufacturers, excludable and thus marketable to vehicle repairers, it is not a free good and should be used so as to make a contribution towards covering the substantial fixed costs expended in its creation during the vehicle development process.

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[14] The one exception to this is when parties are licensed to distribute the information to other parties on a subscription basis.

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