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Submission to the Regulation Impact Statement on dealing with Franchise relationships between car manufacturers and new car



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1. Executive Summary

- 1.1. The Motor Trades Association of Australia Limited (MTAA) and its members, the State and Territory Motor Trade Associations and Automobile Chambers of Commerce, welcome the Department of Industry, Innovation and Science's consideration, through the Draft Regulatory Impact Statement released on 20 December 2018, of the relationship between Car Manufacturers; and New Car Franchised Dealerships, in particular the long standing concerns of significant power imbalances towards Manufacturers.
- 1.2. MTAA believes Industry Department investigations goes some way to addressing matters raised in the ACCC New Car Retailing Market Study (2017); and importantly Recommendation 16 of the 2013 Wein Review¹ into the Franchising Code of Conduct, which called for an analysis of the impact of a minimum term and standard contractual terms for motor vehicle agreements to be undertaken prior to a future review of the Franchising Code.
- 1.3. Before and since the introduction of the Franchising Code of Conduct, MTAA and its Members have advocated relentlessly that the Franchising Code of Conduct is ineffective and unsuitable for the purpose of resolving the serious detriments resulting from the significant power imbalances in the relationship between vehicle manufacturers, who are the beneficiaries of these imbalances, at the expense of new car dealers.
- 1.4. While understanding the need for the Franchising Code of Conduct and other regulatory tools are designed to meet requirements of the broader economy, MTAA and Member representations have stressed that the automotive market is complex, with complex products in modern motor vehicles. The failure of the current Franchising Code of Conduct to provide suitable remedies, or indeed provide a basis for action for the highly specific problems arising from the Dealership/Manufacturer relationship.
- 1.5. The urgent need for action in regards to these matters has been reinforced by the MTAA's and Member advocacy and business owner testimony to the Wein Review of the Franchising Code of Conduct, ACCC Market Study into New Car Retailing, the Joint Parliamentary Inquiry into the Effectiveness of the Franchising Code, and investigations into Unfair Contract Term protections. MTAA in all has been consistent in calling for a significant rebalancing in the Dealer/Manufacturer relationship, through the use of government instruments to ensure fairness.

¹ Wein Review 2013 Review of The Franchising Code of Conduct Recommendation 18 Pg. xi

- 1.6. MTAA and Members believe it important to note that concerns and problems arising from power imbalances from manufacturers and retail franchised dealers are not uniform or applicable to every relationship. There are good examples of relationships that work well, where conflicts are the exception rather than the norm, and can usually be traced back to commitments to negotiate in good faith. Generally market leading manufacturers demonstrate greater collaboration, communication, negotiation happier in their dealership networks that significantly contributes to market leadership and profitability.
- 1.7. This observation has been confirmed by MTAA Members through dealer surveys and workshops including two dealer surveys conducted by VACC in 2018². It is important also to note that market leading manufacturers also do not participate in cyber car practices and support their dealership and consumer network when faced with warranty or Australian Consumer Law (ACL) claims.
- 1.8. However, there is evidence that as pressures mount and market share reduces then dealers can and have experienced changes in behaviour by manufacturers where previously sound relationships, built up over years, can evaporate seemingly overnight.
- 1.9. MTAA Member dealer constituents do not want conflict and would prefer a harmonious and profitable collaboration.
- 1.10. MTAA notes the Department indicates in the RIS discussion paper that it is intended to apply '*only the arrangements between new car dealers and manufacturers are being considered in this Regulation Impact Statement (RIS)*'.³ While the concerns of new car retailers are of critical importance and should be addressed as a matter of priority, MTAA strongly recommends that any solutions must equally apply to motorcycle and farm machinery franchised retailers who invariably experience the concerns that are materially consistent, albeit with some minor nuances.
- 1.11. MTAA welcomes the observation that this power imbalance is causing detriment warranting potential regulatory intervention. The RIS categorises the effects of this power imbalance into three groupings:
- *End of term arrangements* – dealers are being provided insufficient time to prepare when an agreement is not renewed.
 - *Capital expenditure* – dealers are not being provided meaningful or precise disclosure.
 - *Dispute resolution* – it can be difficult for car dealers to undertake multi-party dispute resolution.

² VACC Cyber car survey & VACC Franchise and Oil Code Survey 2018.

³ Regulation Impact Statement - Franchise relationships between car manufacturers and new car dealers Para 2, Pg. 6

- 1.12. MTAA agrees that these principle groupings are of considerable concern to dealerships and cause substantial detriment; however, we contend that there remain other areas which require of deeper examination and inclusion in any regulatory intervention.
- 1.13. One such area is consumer guarantees and warranties and the obligations of the product manufacturer for these areas of Australian Consumer Law and the Competition and Consumer Act.
- 1.14. The RIS stipulates that other sections of the Treasury Department, as well as other government portfolios and agencies, are engaged in investigations into associated policy matters including effectiveness of the franchising. It is imperative that any regulatory intervention is cognisant of the findings and recommendations of these other investigations and those solutions are coordinated and connected.

2. Recommendations

The MTAA recommends:

1. **Regulatory intervention in the form of a specific mandated and prescribed Automotive Code of Conduct, including deterrent financial penalties for non-compliance, to provide a fair and balanced relationship between New Car Franchised dealers and Vehicle Manufacturers. A voluntary Code is not supported.**
2. **That such an Automotive Code of Conduct is developed to address new car retailing as a priority, but equally will apply to motorcycle, car rental, automotive repairers, marine powered products, and farm machinery franchised retailers who invariably experience the same concerns, albeit with some subtle differences. MTAA recommends a further consultation and implementation timeline be established once the automotive new car retailing franchising mandated solution is implemented.**
3. **Best endeavors should be made to ensure that the final Automotive Code of Conduct is consistent and cognisant of the findings and recommendations of the Parliamentary Joint Committee (PJC) Inquiry into the effectiveness of the Franchising Code of Conduct, ACCC New Car Retailing Market Study and other inquiries and investigations.**
4. **MTAA recommends that the implementation of this Code as well as other Automotive Sector Codes of Conduct be included in future reviews and reform of the Australian Consumer Law to ensure the unique aspects of vehicle products and sustainment to be regulated by a fit for purpose regulatory framework instead of relying on legislation intended for less substantial purchases.**

5. Any new automotive dealer specific franchise code includes provisions that mandate:
 - A minimum five year term and five year renewal unless otherwise negotiated and agreed in good faith by the franchisor and franchisee.
 - A bilateral 12 month notice of intention to not renew an agreement.
 - Detailed notification in writing for non-renewal or termination including data and metrics used to reach decisions and mediation and determination processes in the event of dispute.
 - Detailed notification of reasons for franchisor dissatisfaction with performance including specific data and evidence of such dissatisfaction and prescribed timeframes and methodologies to address.
 - Disclosure documentation which must:
 - Include specific detail and requirements in an documents associated with the dealer agreement, particularly where such documentation contains specific demands, requirements, expectations of monetary value or where noncompliance could be used as rationale for non-renewal.
 - Be accompanied by educational material written in plain language, that will help all parties to understand disclosure agreements, negotiating in good faith and any penalties that may apply if breaches are proven; and disseminate this information via national seminars in key metropolitan and regional areas.
 - Be direct and specific in regard to all capital expenditure requirements and provide reasonable, justified, estimates, including methodologies, for what expense/s the franchisee will incur and time requirements during the agreement term of such expenditure.
 - Factor in changes to new vehicle technologies and an estimate of associated costs that dealers will need to outlay in order to conform to requirements for new technologies.
 - Manufacturer responsibility to ensure the outgoing franchisee is not left with excess stock or parts that are of good order and not obsolete.
 - Consideration is given to inclusion of mandatory buy-back of stock if such stock is demanded by the franchisor to be carried by the franchisee during the notification period for non-renewal.
6. Any new automotive specific franchising code is clear in its edict that the pre-reporting of sold cars (cyber cars, RDA Cars, called cars) is prohibited, and that any influence or pressure applied by the manufacturer in regard to pre-reporting of sold cars constitutes a breach of the Code.

3. MTAA and Member organisations in context

- 3.1 The Automotive sector and the multiple industries within it, are undergoing unprecedented structural adjustment brought about by external global influences including automation, the rapid application of advanced technology, increasing influence of increasingly larger and consolidated market participants, and changes to consumer purchasing behaviours.
- 3.2 Modern motor vehicles are now highly complex, integrated, and increasingly inter-connected products. Increased safety, efficiency, environmental, mobility and connectivity outcomes are being achieved with increasing reliance on computerisation, often with multiple third party Original Equipment Manufacturers (OEMs) creating and supplying technologies particularly in advanced systems and sub-system integration.
- 3.3 MTAA Limited is the national association of participating State and Territory Motor Trades Associations and Automobile Chambers of Commerce Members, and discrete national industry associations that exist under the MTAA umbrella providing unparalleled coverage and access to the nation's automotive and related businesses.
- 3.4 MTAA and members represents and is the national voice of the 69,365 retail motor trades businesses which employ over 379,365 Australians that contributed \$37.1 billion to the Australian economy in 2015/16; which equates to 2.2% of Australia's GDP. ⁴ The vast majority of these businesses are small and family owned and operated enterprises.
- 3.5 MTAA member constituents include automotive retail, service, maintenance, repair, dismantling recycling and associated businesses, that provide essential services to a growing Australian fleet of vehicles fast approaching 20 million (expected by 2020) and growing annually by 2.1%⁵ that has rapidly advancing technological systems and capabilities.
- 3.6 MTAA Limited Members have almost all industries (more than 95%) of the automotive sector represented as business member constituents. This allows MTAA Limited Members the ability to understand the operations, issues, concerns and risks of participating automotive industries including but not limited to:
 - *New car retailing (including service)*
 - *Used car retailing (including some who service)*
 - *New and used motorcycle retailing (including service and recycling / dismantling)*
 - *Vehicle body repair (smash repair)*
 - *Independent automotive servicing*
 - *Service station and convenience stores (franchise and independent)*
 - *Auto recyclers, dismantlers and part suppliers*

⁴ Australian Automotive Directions Industry Report, August 2017

⁵ Australian Automotive Directions Industry Report, August 2017

- *Farm and industrial machinery retailing (including service and in some cases dismantling and recycling)*
- *Tyre retailing, retreading and recycling*
- *Towing*
- *Bus and coach*
- *Heavy vehicle*
- *Specific service professions including glass, transmission, engine replacement and reconditioning, brakes, steering, automotive electrical and air- conditioning*
- *Vehicle Rental*

3.7 Most MTAA Limited members are also automotive sector training providers and possess extensive operations and facilities in apprenticeship training and skills development and post trade qualifications. In many jurisdictions MTAA Members are the largest employers of automotive apprentices and trainees.

4. Macro observations on the Regulatory Impact Statement

Risk of uncoordinated policy response.

- 4.1. The RIS acknowledges and makes reference to numerous other inquiries, completed or underway, which may influence and / or impact the relationship between car manufacturers and dealers and the need for regulatory intervention. These include the Parliamentary Joint Committee (PJC) Inquiry, the Review of Unfair Contract Term Protections for Small Business, the ACCC Market Study, and previous Wein Review of the Franchising Code and previous reviews of the ACL and CCA. The RIS also acknowledges other areas of current inquiry which may impact including provision, through regulatory intervention, access to automotive service and repair information and data. The RIS introductory comments also outline portfolio accountabilities.
- 4.2. MTAA notes that the critically important area of the ACL and CCA obligations regarding consumer guarantees and warranty accountability were not in the terms of reference for the Industry Department specifically, but are nonetheless a significant ongoing issue in the relationship between some car manufacturers and dealers.
- 4.3. MTAA understands and is heavily involved in the machinery of government and the need for specific portfolio investigations and responses. MTAA is also aware of and appreciates current levels of inter-departmental collaboration on some current investigations and that the Industry Department is in regular communication and interfacing with the Treasury Department on such matters.

- 4.4. However, MTAA is concerned that any policy or regulatory response may ultimately be uncoordinated or lack the cohesion to address all matters requiring regulatory intervention. MTAA urges the Industry Department and others to continue to collaborate across portfolios to ensure any identified solutions to the matters currently under investigation are cohesive and coordinated and mitigate such a risk.

Clarification of some assumptions contained in the RIS

- 4.5. There are a number of assumptions or conclusions drawn by authors of the RIS which are of concern to the MTAA and its Members and constituents.
- 4.6. For example the RIS includes two statements which are referenced / attributable to FCAI and presented as facts, but which MTAA disputes.
- 4.7. For example:
- a. *'New car dealers do not pay fees or royalties to car manufacturers for the use of their brand. The only payments that car dealers typically make to manufacturers are contributions to co-operative marketing funds and payments for purchasing vehicles, parts, accessories and tools'.⁶*
 - MTAA respectfully suggests this statement is in conflict with itself and at best glosses over the complexity of arrangements by being somewhat oblique in the use of definitions. MTAA does not expect FCAI to be able to necessarily understand dealer perspectives on agreements and requirements contained in them, but does not agree with such broad statements and consider it inappropriate for them to be included in a RIS.
 - Without getting into a definitions debate, MTAA is of the view that dealers pay fees to the franchisor. Fees for signage, access to service and repair information, training, training materials, and other 'subscription services'. Then there are singular payments for vehicles, parts, accessories, equipment, tools etc. that are usually prescribed, if not demanded, as conditions of the agreement and more often than not with little negotiation between the parties.
 - MTAA is not disputing these as legitimate costs of business or in terms of the franchise relationship, but cannot tolerate ongoing assertions that franchisee costs are confined to marketing funds (and these can be significant) and'; *'payments for purchasing vehicles, parts, accessories and tools'.*

⁶ FCAI 2018, p. 3 (Ibid footnote Error! Bookmark not defined.).

One dealer has provided more qualified information to demonstrate the types of fees incurred from one car manufacturer (franchisor) on a regular basis. Fees include, but are not limited to:

- \$350.00 for product training materials
- \$500.00 for training
- \$55.00 for per month for 'technology'
- \$1000.00 for training
- \$137.50 monthly charge for parts catalogue

It may be suggested these charges are small in the sense of the total operations of a car dealership but are relative to the dealership operations, size and locality; and in some smaller dealerships can be the difference between a dealership being profitable or not.

The above represents a small sample for one small dealership. Larger dealerships and particularly those with multiple franchises will have significantly greater fees on an ongoing basis.

- b. *'New car dealers typically control the location of the franchise and many own the land on which the dealership is located. In other franchise systems, it is more common for the franchisor to control the location of the franchisee'.*
- MTAA considers that the ownership of land and location is a secondary consideration to the Manufacturer determined Prime Marketing Areas. However, we note that increasingly dealers DO NOT control the location of the franchise.
 - MTAA considers the statement in the RIS is be incorrect and/or misleading as it does not reflect the singular role of the Manufacturers in materially affecting the viability of individual dealerships through control over the dealership's Prime Marketing Area.
 - In the past two years as some manufacturers have rationalized their dealer networks through termination or non-renewal, it is the OEM franchisor not the dealer that has determined location.
 - Additionally MTAA is able to substantiate allegations of where some manufacturers have deliberately adjusted Prime Market Areas to influence contract negotiations.
 - These manifests in actions that effectively remove incumbent dealerships, increase competitive pressure on dealers to 'shift' locations, or in some cases conjure circumstances that provide the opportunity for non-renewal. This occurs even though all Key Performance Indicators contained in the agreement have been met, and without explanation provided for the decision.

- Dealers contend that OEM market data and marketing strategies have a history of being reliant on out of date or incorrect information, that fails to account for local relations and market trends not recorded in national socio-economic data sets.
- It has been MTAA's experience that irrespective of this knowledge, some OEMs have used PMA changes as a key component of a dealer network rationalization program, which often results in non-renewal, despite the rationale of the PMA, which dealerships, pay for in their Franchise Agreements, being to provide a protected customer base that supports dealership sustainability and profitability.

5. Departmental Consultation Questions

5.1 As part of preparing this submission in response to the RIS, most MTAA members have provided significant input and feedback based on individual consultations with their vehicle dealer constituents. Some MTAA members have provided separate submissions and these should be read in conjunction with MTAA's submission.

5.2 In particular MTAA Member VACC through its Victorian Automotive Dealer Association division has conducted surveys with results referred to in a separate VACC / VADA submission made to the RIS Consultation.

5.3 South Australian Franchise Dealership Working Group

MTAA Member, MTA-SA undertook a significant workshop of dealer members in January 2019 to obtain direct industry feedback through a dedicated Working Group to assess the proposed Automotive Franchising Code. The Working Group consisted of a balance between Regional and Metropolitan, multi-site and single site dealerships, representing most of the OEM brands in the market place.

Key points arising from the Working Group's work include:

- Members believe multiple options should be adopted to achieve the Code's purpose
- Option 2A & 2D are the most effective of those considered and viewed the priority reforms
- In relation to 2D, it is critical to limit what OEMs can change mid-agreement
- In relation to 2C, dealers rejected the proposed negotiation commencement for buybacks taking place after non-renewal has occurred. It was agreed that a fair and reasonable formula should be developed as part of the Code so that there is no requirement for negotiation once a non-renewal letter has been issued (as this would only perpetuate the franchisor to franchisee power disparity and be counter-productive to these proposed changes).

- All Options, with the exception of the Status Quo and Voluntary proposals, were supported in varying degrees

The Working Group's deliberations were arrived at through consensus, and a more detailed summary of their work is provided in the below table:

Options considered by the RIS to have a positive net benefit	Supported by MTA-SA Dealers?	Comment
Option 2A – requiring manufacturers to provide 12 months' notice when not renewing a dealer agreement.	Y	Strong agreement. 12 months is more appropriate to allow for dealers to get affairs in order.
Option 2B – requiring manufacturers to provide a statement to a dealer whose agreement is not being renewed outlining why the agreement is not being renewed.	Y	Less urgent than Option 2D. Although, attendees recognised the importance of keeping OEMs accountable regarding the requirement to "act in good faith".
Option 2D – requiring pre-contractual disclosure of significant capital expenditure to have a greater degree of specificity.	Y	Critical to recognize the link between this and to limiting what OEMs can change mid-agreement. Dealers are mostly happy to invest the capital as long as unfair situations are not imposed. For example, a new dealership is opened and postcodes are subsequently "taken away" from the original dealer's PMA.
Option 2F – enabling multi franchise mediation	Y	Would have its merits both with a group of same franchise dealers meeting together, and one dealer meeting with all of its franchisors on a common issue.
Other options considered by the RIS		
Option 1 – Maintaining the status quo.	N	Clear that there needs to be change
Option 2C – Mandating that manufacturers buy back stock when an agreement is not renewed.	Y	Very strong agreement. However, members disputed the RIS's suggestion that the price of the stock "would be negotiated by the parties after the notice of non-renewal is served". It was agreed that a fair and reasonable formula should be developed as part of the Code so that there is no requirement for negotiation once a non-renewal letter has been issued (as this would only perpetuate the franchisor to franchisee power disparity and be counter-productive to these proposed changes).
Option 2E – Minimum five year terms with right of renewal.	Y	Broadly supported.
Option 3 – Voluntary Code of Conduct.	N	It is clear that this must be mandated to ensure accountability for non-compliance.

5.4 Generally the outcome of the deliberations of the MTA-SA working group reflected views of dealers nationwide and helped inform MTAA's responses to the Department's consultation questions contained in the RIS Discussion Paper.

Regulatory Intervention

Status Quo

- Under no circumstances is a 'Status quo' option acceptable. It is the longstanding position of MTAA that the recognised power imbalance of car insurers is causing detriment to car dealers in the first instance and consumers to such an extent that regulatory intervention is warranted and overdue.
- Regulatory intervention is the only solution and MTAA and Members preference is for a standalone mandated and prescribed code that attaches penalties to potential breaches to ensure enforcement capability.
- However, cognisant of other inquiries and reviews and the call by MTAA for cohesion and coordination of policy responses to a number of interrelated matters, MTAA is open to potential alternative solutions such as a separate schedule to Franchising Code of Conduct specific for automotive dealership agreements or an automotive code with schedules that satisfy current recognised concerns and problems outlined in reports and investigations.

Option 2A – 12 month notice periods

Department Questions for stakeholders and MTAA response:

- MTAA and members position is for a minimum of 12 months' notice period for termination or non-renewal.
1. ***What is standard industry practice for non-renewal, is it longer than the minimum six months required under the Franchising Code?***
 - 1.1 This is a variable. Some car manufacturer franchisors have longer terms, others shorter. It may also be dependent on who is initiating the non-renewal. For example MTAA Member VACC has provided information in regard to provisions contained in a particular Dealership Agreement (*Agreement available on request*) where it is stated '*the dealer has the obligation to advise the manufacturer at a minimum of 7-9 months of the dealer intention to seek extension*'⁷.

⁷ Manufacturer 'X' Dealership Agreement

- 1.2 However, generally almost all franchisor car manufacturers abide by six month requirements stipulated in the Franchising Code provisions for non-renewal as standard practice. What is at issue is that the complexity of the market, the complexity of arrangements and requirements in dealer agreements, including stock inventory and service and warranty requirements and requirements stipulated in operations and procedures manuals which form part of dealer agreements.
- 1.3 MTAA's position is for a notification period of a minimum of twelve months in advance of a franchisor's intention to terminate or cancel an existing agreement⁸. More information on the rationale for this position is provided under responses to Question 3.
- 1.4 12 months will also provide consumers, particularly in regional and rural markets, greater opportunity to make informed decisions about future purchases and access to accompanying automotive services including maintenance and repair options in the event that the impacted brand has vacated the market through a decision of the franchisor to not renew the dealership.
- 1.5 There are instances where manufactures have negotiated a 12 month notice of non-renewal or termination. This is of course based on the premise of a mutual decision to enforce the non-renewal.
2. ***How long does it take to negotiate new franchise arrangements with a different car manufacturer?***
- 2.1 It is the understanding of MTAA, based on advice of members that a new franchise agreement with a different manufacturer (franchisor) can be almost immediate in effect to periods of between three and six months from initial contact to agreement start up. There are many matters which may need to be addressed during agreement negotiation including capital investment required in new buildings, facilities, signage, Prime Market Area (PMA) determination, stock levels, floorplan financing, warranty and consumer guarantee arrangements and compensation , tools and equipment, access to service and repair information, training, etc.

⁸ MTAA LTD Submission to the Parliamentary Joint Committee on Corporations and Financial Services into the operation and effectiveness of the Franchising Code of Conduct May 2018 Pg. 19

- 2.2 While many dealership groups operate sophisticated business models, and are sufficiently resourced to negotiate fair and equitable terms in a timely manner, MTAA would respectfully suggest this is not the norm across the entire industry.
- 2.3 The use of the word 'negotiate' in this question is of significant importance. The question as presented seemingly presumes or implies that there are always genuine good faith negotiations at some point during discussions on a potential new franchise including the provisions and requirements of the franchisor prepared dealer agreement.
- 2.4 As outlined in MTAA's response to other inquiries including the ACCC market Study, PJC Inquiry and unfair contract term protections for small business, and testimony provided by individual business member dealers to some of these inquiries; dealer agreements are provided by the franchisor in largely pro forma format (for the entire dealer network), presented on a 'take it or leave it' basis, with only some minor variations reflecting nuances to a particular dealership and variables such as location. Invariably there is little 'negotiation' and even in circumstances where dealers have raised concerns or have sought to have terms varied, such approaches are often have been met with refusal and a 'take it or leave it' attitude from some franchisors.
- 2.5 Further difficulties arise when a reduced term is offered, unilateral alteration of Prime Market Area (PMA) are made, and disputes around breaches and the validity of those breaches issued during the previous term.
- 2.6 MTAA and Members are also aware of inappropriate behaviours by some car manufacturers toward dealers when those dealers may be negotiating a new franchise agreement with a different car manufacturer.
- 2.7 MTAA and Members have been provided material evidence from some dealers who have faced significant difficulties with an existing franchisor making threats to remove the franchise if the franchisee acquires an additional franchise; or making unreasonable monetary demands related to the existing site on which the franchise is located.

- 2.8 Dealers in this instance will trust that the franchisor will behave ethically and responsibly. This can be the case, but as witnessed with several brands when there is a change in direct report or senior executive at the franchisor - relationships can often change, and previous arrangements are not recognised.
- 2.9 Of importance is that if a dealer is seeking a new franchise arrangement to replace a brand that has been terminated or not renewed, it is often to ensure the survivability and profitability of the entire dealer business. Usually this is to ensure that personal assets including homes and individual income are not put at unnecessary risk.
- 2.10 MTAA is unaware of any official benchmarking on how long it does take to negotiate a new agreement.
3. *It has been put to us that 12 months is considered to be a more adequate length of notice for non-renewal. Is this optimal or is there a more optimal period of notice for non-renewal?*
- 3.1 As previously stated, it is MTAA's view that the formal notification should occur with 12 months remaining on the agreement term. This means that franchisor preparations for formal advice would start before the 12 month date. For example, if a current five year dealer (franchise) agreement were to end on 30 June in the fifth year of the agreement, then formal advice of the franchisor to the franchisee that they were intending not to renew or terminate should be provided on 1 July of the proceeding calendar year (or day 1 of the fifth year of the term).
- 3.2 However, MTAA strongly suggests that it is not just lengthening the notice period but providing increased mechanisms for disclosure and transparency to elements of business and transactions during that notice period. Significant problems arise during the non-renewal or termination notification period in regard to manufacturer expectations and dealer understanding in areas such stock, services, buy back and freedoms of the dealer to seek alternative franchisors and / or to sell the business without some of the restrictions and problems that MTAA has enunciated in submissions to other inquiries.
- 3.3 For example, MTAA is aware of the 'dumping' of stock on dealers who were then notified that their agreement would not be renewed. Dealers have little to no say in the stock allocated, and in some cases

the stock did not suit the location or consumer preferences for that market, yet were supplied and expected to be sold by the non-continuing dealer franchisee without adequate buy back arrangements.

4. *Would the benefit to car dealers of an extra six months' notice outweigh the costs to manufacturers of having to make business decisions further out than the prescribed six months? Why/Why not?*

- 4.1 MTAA believes the mutual benefits for both dealers and consumers outweigh any costs to manufacturers.
- 4.2 We are talking an additional six months with increased transparency and mechanisms for key elements of the agreement during the extended notification period. MTAA does not believe it to be an onerous requirement. It provides increased surety, increased capability (provided the existing franchisor does not make dealer decision making difficult).
- 4.3 While the timeframes for the application of rapid advances in technology are reducing; the design, approval for production and model launch of motor vehicles remain a relatively known quantity and can span several years. For example most car manufacturers will know today the vehicle model release arrangements well into the next decade. While MTAA accepts this timeframe may potentially shorten, there is no known 'business decisions' that would be impacted by adding six months onto current requirements for a notification of termination or non-renewal.
- 4.4 Even changes to consumer buying habits and the impacts and growth of ride sharing, vehicle ownership versus vehicle hire, individual driver licensing, autonomous vehicles, congestion and the impact of other mobility offerings, have relatively longer time horizons. None of which in the opinion of MTAA would impact an additional six months of notification and ability of dealer businesses and consumers to adapt to changes in brand and product availability in a particular location.
- 4.5 MTAA is aware of, understands, and respects manufacturers, dealers, and entrepreneurs, will investigate and implement other retailing models. For example there are increasing intersects between online purchasing. Some countries have seen the arrival of a 'vending machine' type of retail outlet directly linked

to purchase decisions being made online by consumers. Also emerging are differing versions of the traditional showroom dealership model including the Toyota 'agent model' in New Zealand as referenced in the RIS.

- 4.6 MTAA respectfully suggests that in a country such as Australia with its widely dispersed population, vast distances between regional and rural communities, ongoing reliance on road transport as the primary means of connectivity and mobility, ongoing relationship with motor vehicles, and an aging core population, the role of dealers and the services they provide are considered to be ongoing for the foreseeable future. MTAA is already aware of increasing consumer concerns in regional and rural Australia from the impacts of reduced dealerships for many brands.
- 4.7 MTAA suggests the longer timeframe will increase transparency (particularly if other matters also raised in this submission are addressed simultaneously) leading to better planning outcomes and ultimately better business decisions. It is important to also understand that car manufacturers do not have a mortgage on business innovation and decisions with many dealership groups and individual dealer businesses worldwide also identify innovative and alternative options for the retailing of motor vehicles and accompanying services.
- 4.8 The answer to this question should be also be viewed in comparative terms. The RIS recognises the power imbalance and that a dealer has the most to lose under current arrangements.
5. ***Would increased education and awareness of existing pre-disclosure and notice periods for non-renewal support dealers undertake their due diligence and highlight the risks of non-renewal?***

- 5.1 MTAA supports continuous awareness and education activities, but respectfully suggests this is not a central issue. The question could be read to imply that there is a current lack of awareness and knowledge in these areas and this MTAA believes is not the case. Indeed it is the frustration experienced by many dealers that even with knowledge of requirements and use of protections and processes; these are ultimately ineffective and do not address the behaviours and conduct being experienced.
- 5.2 This is not to say the MTAA and Members would not welcome increased education and awareness focussing on pre-disclosure or non-renewal. MTAA suggests however that car manufacturers who are now all international based companies should also be included.
- 5.3 MTAA Member, the VACC, conducted a survey of members as part of submissions to reviews of the Franchising Code in 2018. The Franchising and Oil Code Survey 2018 (the survey) indicated that 36% of respondents did not receive full disclosure of all contractual rights in their agreement. More than half (59%) of respondents to the survey reported that they were not aware of their rights at termination and a further 54% did not have a clear understanding of the rights and obligations of each party at the end of the franchise term⁹.
- 5.4 Any planned educational material should be developed in conjunction with dealer facing Industry Body's and be worded in simple terms that is understandable to the reader. Ultimately the requirement of both parties to deal in good faith is paramount.

Option 2B – Franchisors to provide reasons for non-renewal

- Dealers support this option to provide better accountability and guidance on reasons for non-renewal. However, implementation of this option should be prioritized behind Option 2 D – Buy back of Stock.

6. *Is it common practice for car manufacturers to explain to dealers why their agreements are not being renewed?*

⁹ VACC Submission to Parliamentary Inquiry into the operation and effectiveness of the Franchising Code of Conduct, 4 May 2018. Pg. 7

- 6.1 It is not common practice for car manufacturers to adequately explain why their agreements are not being renewed. The common opinion amongst new car dealers is that manufacturers will use 'non-renewal' as a more cost-effective method of achieving dealer network rationalisation.
- 6.2 MTAA has numerous examples where dealers including some who, in only the two years prior to being told their franchise would not be renewed, had been voted among the best dealers in the country by the brand. In one case a dealer was selected as 'dealer of the year' only a year before they were not renewed. There are also numerous examples where dealers have not been renewed, yet every performance indicator had been met, profitability, even in difficult trading environments, were being maintained, and high customer satisfaction levels, were still not enough for the dealer to retain the franchise.
- 6.3 Recently MTAA has brought to the attention of regulators what it believes to be unconscionable conduct of some manufacturers after notification of non-renewal, including inappropriate behaviours in deliberately thwarting dealer efforts to secure alternative dealerships or to be able to sell their dealership.
- 6.4 MTAA also refers the Department to Hansard for hearing of the PJC inquiry into franchising who heard from dealer's experiences with non-renewal behaviours. For example, it is common for car manufacturers to advise dealers feeble one or two-line excuses that the non-renewal is taking effect because of 're-structuring'¹⁰.
- 6.5 Dealers who avail themselves of dispute resolution provisions of the franchising code including mediation are completely dissatisfied and indicate the process is a waste of time money and resource and usually without any meaningful fair and reasonable outcome.

There are equally many dealers who will not 'rock the boat' with legitimate concerns or testing of the behaviour of car manufacturers because of genuine concerns over repercussions or impacts on other negotiations with other car manufacturers to secure an alternative franchise.

- 6.6 The dealer agreements generally reflect pro forma provisions from the Franchising Code which reflect a whole of franchise approach. Herein lies a considerable issue in that while technically the provisions may have been met, they do not reflect the complexity of the market of the relationship and the millions of dollars involved. This is not to say other franchisees are any less important in terms of protections and

¹⁰ Notice of non-renewal of manufacturer 2018. Available upon request.

remedies offered, but few if any match automotive dealerships in terms of size, influence of the franchisor, and capital investment. This is why MTAA is of the view that as well as an extension of the notification period there needs to be transparency on arrangements and processes during the notification period.

Option 2C – Stock buy-backs

- MTAA understands the rationale detailed in the RIS regarding difficulties in addressing stock buy backs in dealership terminations or non-renewals and potential conflicts with ensuring open processes for competition and unfettered contract negotiation. However MTAA respectfully suggests that motor vehicles are unlike any other franchise and requiring specific consideration in regard to stock buyback.
- Core to MTAA and Member arguments is the market and product complexity. Unlike other franchise operations in other industries we are talking about millions of dollars in stock combined with power and influence over those stock levels by car manufacturer franchisors.
- On top of motor vehicles, and as recognised in the RIS, there are further demanded requirements for specific and specialist tools, equipment and parts.
- MTAA does not agree with the position expressed in the RIS that regulating stock buybacks would be *'contrary to the existing policy framework for the Franchising Code, competition principles underpinning the CCA and general principles of contract law since it would be seeking to impose particular commercial terms on two parties to a contract rather than let the parties to the contract or the franchise agreement determine the terms that best suit them.'*
- MTAA argues that in situations where the franchisors demand or impose certain levels or types of stock during the period following notification of non-renewal or termination, that are **not agreed** to by the dealer through good faith negotiations, then there must be a mechanism to provide for buy backs at wholesale price charged to dealers for such imposed stock.
- While it would reduce the commercial pressure and risk on new car dealers, the RIS seemingly presumes the commercial pressure and risk was agreed to by dealers in all situations and in many examples

provided to MTAA this is not the case. Often the imposition of stock intersects with targets specified by franchisor for sales and can change during the notification period.

- MTAA does not agree with assumptions that compliance costs would 'greatly increase' for manufacturers as they will still have an ability to recoup costs through the future sale of vehicles bought back. It is not necessarily a negative either if negotiations are prolonged because it would further encourage good faith negotiations during the notification period.

Department Questions for stakeholders and MTAA response:

7. Are car dealers able to run down their stock when they know an agreement is not being renewed?

7.1 Dealers are in a precarious situation regarding running down stock. A recent non-renewed dealer advised, *"In the best of cases, dealers are given a six-month non-renewal notice and are expected to maintain stocking levels, anything from 45-60 days of stock, to be eligible for bonus programs"*.

7.2 A customer base that requires servicing and repairs dictates that stock level must be kept at adequate levels. A recent dealer who exited the dealership network commented:

*'if I knew I wasn't being renewed then I could have gone off 'auto release' from my finance company to 'manual release' so I wouldn't have to take any stock without an order on it.'*¹¹

7.3 Dealers can be in the difficult position of having negotiated a deal close to when the non-renewal term expires, only to not have that vehicle delivered or counted to be delivered, as part of its sales target. In one Dealer Agreement viewed by MTAA Member, VACC, it is stated that it is at the manufacturer's discretion to fulfil any orders placed by the dealer.

It is further stated that the dealer must reimburse the manufacturer if any loss is incurred because of a sale to a third party.¹² If that position was accepted, it would result in the dealer missing on sales bonuses and other incentives. Dealers also have customer bases of independent repairers who rely on genuine parts to facilitate the service of their customers.

¹¹ Ex dealer interview VACC January 2019

¹² Dealer Agreement available upon request

- 7.4 There may also be the downward pressure of pre-reporting cars sold ('cyber cars'). The practice is incentivised and directed by manufacturers and causes unnecessary expense and red-tape for dealers. It is a practice many dealers do not want to apply, but for reasons including pressure from the manufacturer, the need to achieve unreasonable sales targets and financial incentives, many dealers feel pressured into doing so. Many dealers have advised VACC if they do not participate they fear non- renewal or termination.
- 7.5 Dealers must register these cars with the local road's authority to be counted as being included in VFACTs and manufacturer reporting to overseas head offices. Dealers are then required to retail these vehicles as a used motor vehicle. The hidden costs associated with this practice greatly impact the dealer's bottom line.
- 7.6 Research conducted by MTAA Member, VACC in 2018 indicates that 28.9 per cent of all cars sold nationally are 'cyber cars'. Based on this figure, it is estimated that 95,433 cyber cars existed in Victoria from October 2017 to October 2018. These cars must then be sold as used cars, which mean a certificate of roadworthiness must be completed at the point of retail sale to a consumer. VACC benchmarking shows the average cost for each individual roadworthy to be \$233.33 and costs the Victorian new car franchise sector an estimated \$22.2 million per annum.¹³
- 7.7 MTAA can provide further information on this practice if it is of use to the Department. In regard to this matter, MTAA's national position is that any regulatory intervention must include provisions that the pre-reporting of sold cars is prohibited and that any influence or pressure emanating from the manufacturer constitutes a clear breach provisions of the ultimate regulatory solution.

¹³ VACC Research 'A case for removing roadworthy certification for new, low kilometre, dealer -owned cars'
October 2018

- 7.8 Dealer and manufacturer accountabilities for Consumer Guarantees and Warranty must also be considerations. While it appears this area was not considered in the RIS it can be, and is, a considerable point of dispute.
- 7.9 MTAA has numerous examples and highlighted some of them in previous submissions to the Franchising Code Review, the ACCC New Car Market Study and PJC Inquiry into franchising on the type and levels of disputation that arise from dealers being caught between consumers and manufacturers in meeting and being properly compensated for consumer guarantee and warranty work.
- 7.10 There are examples where disputes heighten during notification periods for termination and / or non-renewal where a dealer meets obligations to a customer for rectification of warranty, re-call or consumer guarantee work; but then faces significant problems being compensated for the work or for some franchisors accepting ultimate accountability for the work performed and costs associated with it.
8. *How much stock would a dealer typically have remaining when an agreement is not renewed?*
- 8.1 Ideally stock or inventory should be at levels suitable for the dealership, the prime market area and mutually agreed between the franchisor and franchisee inclusive of incentives and programs for increased sales and improvement in market share.
- 8.2 At any one-time dealers can have millions of dollars of stock holdings including vehicles, parts, tools and equipment. The reality is that dealers still have a responsibility to their customer base and obligations under Australian Consumer Law (ACL) to maintain adequate parts supply for service, repair, and to meet consumer guarantee and warranty requirements. These vehicles and parts are easily transferable to other dealers who will assume that brand presence within that area.
9. *In what circumstances do buy-back arrangements generally apply in current agreements (for example, at non-renewal, termination by agreement)?*
- 9.1 The response to this question would generally depend upon the state of the relationship between the franchisor and the franchisee and the circumstances that have led to the non-renewal. MTAA is aware of

some good car manufacturer franchisors who enjoy healthy relationships with their dealer network include buy back arrangements. Generally it is a discretionary term and varies from franchisor to franchisor.

- 9.2 A review of a recent Dealer Agreement of a car manufacturer franchisor revealed a term that stated that the manufacturer at its 'absolute discretion may within 14 business days of the Termination Date repurchase from the dealer any or all tools or equipment designed for servicing the products purchased by Dealer from the manufacturer.
- 9.3 In what may be deemed as an equitable and fair arrangement another manufacturer states that the manufacturer will pay the dealer a purchase price for unused tools, while parts and vehicles will be at landed prices (invoice price, plus unrebated duties, taxes and inland transportation costs). However if there is a model change or vehicles are not of the current year there is a 15% difference in that purchase price. Some dealers have advised that while this practice is not a standard approach, dealers can be stuck with runout models that have been supplied by the manufacturer as part of an overly ambitious sales target set by the manufacturer to clear such excess stock, irrespective of the notification to terminate or not renew.
- 9.4 The key takeaway from the research and interviews conducted by MTAA members with dealer members reveals considerable resources are dedicated by dealers to ensure they are informed of what terms they are contractually bound to.

10. *To what extent do dealerships trade stock with other dealership businesses to address the issue of excess stock upon cessation of a franchise agreement?*

- 10.1 Dealers have indicated to some MTAA members that there is no equitable position for a dealer to trade stock to another dealer to reduce its stock holding at the point of cessation of the franchise agreement.

10.2 This is largely due to the complexity of requirements between the franchisor and franchisee and obligations under laws and regulations. For example a receiving dealer would not qualify for secondary holdback and other incentives from the manufacturer on the traded stock. Compounding this practice is the consideration that some stock is undesirable and may only have suited the original receiving dealer. Overall the complex structure of margins, bonuses and holdbacks lessen the ability for a dealer to move stock to other dealers, who need to avail themselves of full margin.

11. *To what extent do manufacturers buy-back stock upon the conclusion of a dealership agreement?*

11.1 The extent to which manufacturers buy back stock upon the conclusion of a dealer agreement, as mentioned above, varies from brand to brand and the circumstances of the non-renewal or termination.

11.2 In data collected from MTAA Member dealer constituents, many advised that the franchisor would not re-purchase or provide compensation for parts or equipment beyond a specific age. In instances where the franchisor agreed to repurchase the stock it was re-purchased at below cost causing the franchisee financial loss¹⁴. The situation is again compounded by the pressure and incentives by manufactures for dealers to pre-report cars as sold (aka 'cyber cars').

11.3 Interviews with members of VACC indicated that there is no equitable position for a dealer to trade stock to another dealer to reduce its stock holding at the point of cessation of the Franchise Agreement. One prominent member advises that they have eight franchises and not one of them have a buy- back agreement²⁴ and that no other dealer would take the stock as they are all overstocked¹⁵.

11.4 However, some dealers advise it would be non-advantageous to transfer the stock as the dealer may have to transfer any bonus or holdback money that came with that car.¹⁶

¹⁴ VACC Submission to Parliamentary Inquiry into the operation and effectiveness of the Franchising Code of Conduct, 4 May 2018. Pg.12

¹⁵ VACC Survey into DIIS RIS January 2019

¹⁶ VACC Survey into DIIS RIS January 2019

11.5 MTAA Member VACC has dealer constituents contend that the receiving dealer would not qualify for secondary holdback from the manufacturer if the model is being traded. For example, this secondary holdback on a high-volume brand could amount to a figure of approximately \$400 per unit.¹⁷

12. *To what extent would mandating buy-back options deter manufacturers from signing dealership agreements?*

12.1 It is the view of MTAA and Members that there should be no deterrent, provided manufacturers were very clear and specific regarding the buyback provisions including for example that any buy-back units were in new condition, in original packaging and could be able to be redirected to another dealer as a new unit; buy-back would need to be at the dealer's original invoiced purchase price; and any other terms that were negotiated in good faith between the franchisor and franchisee dealer. As previously stated mandated buy-back written into any agreement would ensure manufactures would not 'load up' dealer's that they do not intend to renew with unacceptable or negotiated levels of stock.

Option 2D – Enhanced capital expenditure disclosure

Department Questions for stakeholders and MTAA response:

13. *Do manufacturers typically determine what significant capital expenditure will be required prior to an agreement being entered into or is this a decision that is ordinarily made during the life of the agreement?*

13.1 Initially yes, but MTAA has been presented with numerous examples where the initial disclosure make somewhat vague references to marketing and brand improvement and similar types of expenditure. For example a franchisor may determine that a refreshed brand is required as part of a new cycle of models, market research, or many other valid reasons, during the term of the agreement. What is often not disclosed is that in such circumstances the rebranding exercise may require complete new signage requiring significant change to buildings and facilities. Such requirements are usually dictated by the parent organisation and may be at odds with the dealers own marketing and business requirements.

¹⁷ Ex Victorian Dealer who was not renewed 2017

13.2 MTAA has previously reported that for dealer to meet the capital invest requirements contained in agreements, will usually necessitate finance via financial institutions, with is secured against the dealer's business and invariable in most cases the personal assets of the dealer. Whilst most dealerships can and should be expected to have security provisions attached to any finance arrangement, the exposure required when combined with the development required and lack of tenure in agreement leaves the dealer precariously placed. This becomes a paramount consideration when the dealer suddenly finds they are not being renewed even though there was no indication that the business was not meeting requirements or performance indicators or any other indication that they would not be renewed.

13.3 MTAA and dealer members have explained in detail to the PJC inquiry into the franchising code examples where dealers who otherwise would have reasonably expected to maintain the franchise relationship were terminated or not renewed. Some then experienced behaviours from some franchisors that were not acceptable placing further financial and personal duress on those dealers.

14. *Generally, what is the monetary range for expenditure disclosed to car dealers? How common are wide expenditure ranges in disclosure documents? If wide expenditure ranges are provided, why are they provided?*

14.1 There is no real universal formula as expenditure will vary considerably between franchisors and within the franchise. Terminology is often broad and monetary examples likely to be wide ranging. This is commonplace and franchisors are able to do this under the existing franchise code guidelines. Overarching franchise agreements are written to be compliant with the Code, but again MTAA and Member concerns are that a car dealership is not and bears no resemblance to a fast food or retail franchise.

- 14.2 When reviewing non-disclosure documents provided by some franchisors it was revealed that when calculating gross profit margins, the Non-Disclosure Documents offer estimates as ranging from 1.5%- 5%. The documents would be typical of what is provided to a dealer at the initial stage in that they are deliberately nonspecific in what the cost would be and are as generic as too considered as redundant. Ranges calculated with reference to day to day expenditure are bracketed in wide ranging, unhelpful ranges.
- 14.3 According to dealers surveyed by MTAA Member VACC, it is uncommon for the manufacturer to dictate the monetary value of what you need to spend. Rather they dictate the specification of the facility¹⁸. Some Manufacturers also dictate the suppliers that must be used for the supply of furniture, tiles and all corporate identity including signage and other expenditure to maintain the dealership to the manufacturer's corporate image specifications.

The following table highlights the extreme capital expenditure for showroom update costs borne by some VADA members as dictated by manufacturer.

ITEM DICTATED BY MANUFACTURER	DEALER COMMENT
Chairs \$500 per chair from France	same chair purchased from Ikea for \$100
Tiles from Italy at \$100sqm	Can be purchased locally for \$40sqm
Entry portal \$3k	Now does not fit with the manufacturer Corporate Image and must be removed.
Single letter replacement on signage cost over \$2k to replace.	Must use manufacturer contractor

Facility to build for three car showrooms over
\$1m plus \$160K

Must be updated every 2 years

15. *What level of support and education is provided to dealers when entering into franchising agreements and during the contract, regarding capital expenditure requirements?*

- 15.1 Some manufacturers go over and beyond what their current obligations are under the Franchising Code. However, the difficulty for franchisees is obtaining professional advice that is available on suitable terms. Manufacturers franchise agreements are created by leading law firms, many with high levels of skill with franchise law. The Franchisee is expected to obtain its own advice on the franchise agreement. To do so requires a law firm of equal standing. This is not only difficult but expensive. Some dealers struggle with the complexity of franchise agreements, which are not written in common language.
- 15.2 MTAA is aware that Dealers have received legal advice over time indicating that a particular terms should not be accepted within the agreement; 'or not to sign' the agreement because of the imbalance of power demonstrated in the terms and conditions. However when a dealer is unable to secure good faith negotiations to alter a particular term, where the franchisor indicates it is a take it or leave it position, or in some cases where the dealer believes there may be potential negative repercussions, they invariably will agree to the agreement, irrespective of the advice received, in order to secure short to medium term financial security, wellbeing, and business sustainability including job security for Australians employed by them.
- 15.3 Changes to capital expenditure and other requirements during the term of the agreement are largely accepted as they are either been 'alluded to' in broad definitions contained during disclosure or failure to abide is interpreted alongside a potential non-renewal or termination for failure to meet requirements.
- 15.6 The fear of such repercussions is significant. MTAA would argue that the reason why some dealers have come forward over the past 18 months after 20 years of seeking dealer participation in such inquiries and reviews to validate known misconduct and unacceptable behaviours is due to the increasing trend of treatment they received and inability to gain appropriate recourse through existing regulatory measures.

16. Are you aware of instances where dealers have expended significant capital expenditure towards the end of a dealer agreement which is in accordance with their agreement, but which they anticipate cannot be recouped? How far out from the end of the agreement are they undertaking this capital expenditure?

16.1 MTAA and members are aware of instances where dealers have expended significant capital expenditure towards the end of a Franchise Agreement at the instructions of the manufacturer. MTAA arranged for an ex-VACC dealer to present their case, in camera, to the Parliamentary Joint senate Inquiry (PJC). They raised matters put to the original Franchising Code Inquiry. The ex-dealer outlined how, with the approval of the manufacturer, they built new showrooms in regional Victoria and New south Wales only to have that Franchise Agreement non-renewed. A decision that ultimately cost the now ex-dealer millions of dollars.

16.2 The following is an extract from MTAA Member VACC 2019 RIS survey from a dealer affected by a decision of a manufacturer to not renew after having a business plan approved by the manufacturer:

'Three months prior to being handed non-renewal, our five-year business plan was approved, and we were specifically directed to begin construction of a new dealership on our current site. It was later claimed that the non-renewal decision was made after that, but I don't believe the slashing of 30 dealers from your network is a snap decision and that it was unconscionable of the manufacturer to ask us to start major works when non-renewal was on the cards. We were required to maintain staff training, pay for marketing materials, annual subscriptions (which we then had to fight for a six-month refund of), and were even billed for special tools that were automatically billed and arrived in days before the business closure'.

16.3 MTAA is prepared to ask some member dealer constituents to speak confidentially to the Department on examples experienced. MTAA and Members are aware of significant instances where dealers have expended significant capital expenditure towards the end of an agreement term, at the instructions of the manufacturer, with expectations that the franchise would be renewed as there were no indications of any dissatisfaction, nonperformance or noncompliance.

16.4 It should also be noted that dealers have, for financial reasons, needed to relocate or alter their facilities and have invested capital to satisfy their manufacturer. The manufacturer has not renewed their agreement. This has sometimes occurred within 12 months of the agreement term.

17. Can dealers undertake capital investments, for example build a showroom, so that it can be repurposed to suit another distributor's brand if their existing dealership agreement ends?

17.1 Generally yes, but this decision can be, and is heavily influenced by the requirements of the franchisor and in the case of a multi franchise site – multiple franchisors. It is important to note that most car manufacturers will have specific requirements regarding the appearance, functionality and operations of facilities including showrooms, vehicle delivery, servicing, storage and detailing areas, customer reception etc. In some cases they may be common. In others requirements may be specific to a particular brand making it difficult for a facility that can be repurposed at the end of the agreement.

17.2 From the evidence gathered via face to face interviews and review of five random Dealer Agreements¹⁹, it is the case that dealers cannot make alterations or invest in fit out of premises without the manufacturer's written permission during the period of the agreement, including the non-renewal period. In one agreement it is explicitly stated that dealer must make any alterations within 30 days to that manufacturer's specific area as defined within the agreement²⁰.

17.3 Repurposing at the end of an agreement could be possible if included as mutually agreed term, negotiated in good faith, but this is not common. Even with such potential the dealer would have to gamble on the size of the facility and its service centre meeting other franchisors requirements.

¹⁹ Genuine Manufacturer Dealer agreements n.d

²⁰ Manufacturer Dealer Agreement 2007

18. *To what extent do the other provisions of the CCA, such as the unconscionable conduct provisions, provide remedies for dealers in situations where they have to outlay capital which cannot be recouped during the term of the dealership agreement?*

18.1 MTAA is aware of several dealers who have used the dispute resolution and mediation processes outlined by the Franchising Code to no avail. Franchisors concerned with these cases demonstrated the significance of the power imbalance with significant access to legal and time resources.

18.2 More recently MTAA, on behalf of some members and their dealer constituents has made representation to the regulator for investigation and potential enforcement action under various provisions of the ACA. MTAA viewed so seriously the potential unconscionable conduct of one franchisor and the clear inability of impacted dealers to have any recourse through established mechanisms that it had no choice but to bring the matter to the regulator's attention. MTAA is awaiting advice on the progress of this representation.

18.3 The apparent inability to seek relief or recourse through provisions within the CCA also underpins MTAA and Member calls for more specific action through regulatory intervention. It is the experience of MTAA that in some industries and some circumstances the necessary universal and whole of economy approach laws and regulations can provides gap that are exploited.

19. *What extent would be mandating buy-back options deter manufacturers from signing dealership agreements?*

19.1 There should be no deterrent as evidenced by some franchisors willingness to incorporate such provisions and the apparent sounder relationships they appear to enjoy with their dealer network.

20. *The Franchising Code also prohibits franchisor imposed capital outlays during the term of the franchising agreement unless specific conditions are satisfied. How are these provisions utilised within the industry?*

20.1 As previously mentioned dealer agreements are constructed legally to conform to the Codes' requirements and are generally compliant. However it is the wide ranges of financial exposure and matters specific to automotive franchises which create concerns as outlined in this response to the RIS and require greater details, mechanisms and specificity to counter the market and product complexity found in automotive retailing.

Option 2E – Minimum five year terms with right of renewal

Department Questions for stakeholders and MTAA response:

21. *How would car manufacturers respond to the introduction of minimum terms?*

21.1 In the broad, MTAA cannot respond to how manufacturers would respond. However MTAA suggests that problems identified and risks to both parties could be mitigated if specific provisions increasing transparency and the role of good faith negotiations were developed and implemented as part of regulatory intervention. Provisions could include specific and mutually agreed terms and processes for non-renewal or termination including specific, improved, and transparent causation for findings of non-performance, non-compliance, or poor satisfaction as part of disclosure.

21.2 MTAA Members report that manufacturers would generally respond negatively to the introduction of minimum terms. The arguments put forward that by having minimum terms applied could restrict the

manufacturers' ability to control the size and location of its dealer networks does not stack up. It would be better for all stakeholders if the alteration to the minimum terms was negotiated in a fair and reasonable way. This would avoid the non-renewals or terminations of 30 dealers at a time.

- 21.3 Some MTAA Members suggest that minimum terms would be more acceptable if provision for non-renewal or termination applied to non-performance, with performance criteria being clarified prior to the agreement being formalised.

22. *Would dealers and manufacturers still have flexibility to respond to developments in technology and changing consumer preferences if agreements had minimum five year terms?*

- 22.1 Yes. As previously detailed the automotive retailing industry is facing a number of challenges and external influences. MTAA suggests there is no reason why each manufacturer and their dealer network cannot seize opportunities for greater collaboration and transparent and meaningful good faith negotiation that results in mutually beneficial outcomes.

Manufacturers can still structure future agreements taking into account application of existing or emerging technology, their future model line-up, changes to service and repair and other requirements within commercial understandings. Pressure from competitors impacting on sales of a manufacturers brand would apply across the manufacturer's network and not be specifically relevant to an individual dealer.

- 22.2 The dealership network is currently repositioning well to changing consumer preferences. It is worth noting that changes to consumer preferences has in 2018 seen commercial vehicles register as three of the top seven selling models.

- 22.3 FCAI has noted 2018 as a year of continuing adjustment for motoring consumers, with the year seeing a further shift to SUV sales at the expense of passenger vehicles²¹. Dealers are already coping with the challenge of changing consumer preferences. There is no reason a future automotive specific code could not factor in degrees of flexibility that will allow for changes to agreements, whereby the agreement will

²¹ FCAI Media Release 'Sales down in challenging 2018 Environment' 4 January 2019

consider the introduction of future technology, future model line-up and changes to service and repair and other requirements with commercial implications.

22.4 This could only be achieved if minimum terms were introduced. MTAA emphasise that a five by five-year option is the only way for dealers and manufacturers to take advantage of changes in technology and changes in consumer buying habits.

22.5 The inevitable increase in sales of electric, hybrid and autonomous vehicles to a manufacturer's local line-up of vehicles will not cause great disruption to dealership operations or influence how a future agreement should look. The dealership network and manufacturers are currently handling the technology aspect of these vehicles, including infrastructure adaptations to be able to repair these vehicles.

The real issue will come in aftermarket repair, where a lagging independent network may not be sufficiently equipped to service and repair such vehicles. It would be within the manufacturers' purview to advise in the disclosure document of the capital expenditure outlay that dealer would require to be part of the sale of these vehicles.

23. *What would be the public benefits or detriment of providing minimum tenure and a right of renewal? For example, to what extent might it deter manufacturers signing agreements with dealers or accelerate consolidation of dealerships in particular regions or areas?*

23.1 As Australia fast approaches a national passenger and commercial fleet of some 20 million vehicles and ongoing reliance on road transport as primary means of mobility and connectivity, it is essential that all Australians have reasonable access to new car retailing and associated services.

23.2 Equally important is that consumers are not disadvantaged by one-off or short term decisions that undermine consumer confidence and access to associated services including maintenance and repair and recourse for consumer guarantees and warranty. In addition dealers are key elements of communities

and there are a range of tangible and intangible public benefits not the least of which includes employment and consistent level of service availability in a locality.

23.3 Consolidation is recognised as is the potential for alternative business models to address changing consumer behaviours. However this should not be a short-term decision and if restructures or rationalisation is should provide retail business and consumers with time to adapt and make their own decisions.

23.4 Manufacturers have considerable resources in global market research, trends and consumer purchasing decisions and plan accordingly. However sometimes this is driven without the benefit of local market input and knowledge off potential impacts direct and indirect to significantly differing communities and consumer groups.

On many occasions changes in policy direction by automotive franchisors has been driven by new cost and market share imperatives implemented by new (and often transient) senior management without truly understanding market dynamics unique to Australia and to Australian jurisdictions or localities. Dealers generally accept change, but struggle with illogical change based on incomplete understanding or plans drawn in isolation in distant off shore headquarters.

24. *Would a longer notice period for non-renewal achieve a similar outcome to addressing concerns about minimum tenure and the need for franchisees to have certainty when it comes to business planning?*

24.1 Yes. The objective of regulatory intervention is to address identified problems, improve transparency and behaviours and identify, develop and implement specific mechanisms. A longer notice period with accompanying mechanisms, processes and requirements will provide greater business surety and allow for more orderly transition.

25. *To what extent would minimum terms or a right of renewal prevent manufacturers from responding to changing market conditions and lock the parties into the existing business model?*

- 25.1 MTAA does not believe minimum terms would negatively impact either franchisor or franchisee from responding to changing market conditions.
- 25.2 As previously mentioned, even with rapid application of advancing technology; changes to consumer behaviours; changes to propulsion systems, ride sharing, automation and a range of other factors and influences; there is still a relatively long lead time in terms of model design, production decision and implementation taking several years at a minimum. If the historical method of retailing vehicles is to cease, it won't occur overnight, and franchisees will see it coming. Both parties will need to make informed decisions about their respective futures in the Australian market future within the confines of the agreed Code.

Option 2F – Multi-party dispute resolution

Department Questions for stakeholders and MTAA response:

26. *Would an ability to enter into multi franchise mediation make car dealers more likely to utilise mediation as a means to resolve disputes?*
- 26.1 MTAA believes not. Mediation has not been overly, if at all, successful as a means of dispute resolution to date because of the recognised power imbalance. The number and type of disputes vary from dealership to dealership and from franchisor to dealer. Mediation under the Code is rarely successful as dealers cannot hope to counter the manufacturer's financial and legal strength, in most cases succumbing to pressure exerted through the franchise agreement. Dealers are also currently unable to access unfair contract term protections like other small businesses because of thresholds to define small businesses.
- 26.2 MTAA would respectfully suggest that when Dealer Councils were more independent of the Franchisor, their ability to collectively negotiate for dealer network businesses was significantly greater than today for most franchisors. Over time franchisors have largely exerted increased control / influence over Dealer Councils to the point where it is difficult, if not impossible, for Dealer Councils to negotiate improved terms.

26.3 Central to MTAA call for regulatory intervention is the role of mandated and prescribed penalties as a deterrent, and enforcement and as an enabler to properly constructed mediation and determination outcomes. Dealer councils could be empowered as one option, so too could external independent options including mediation and dispute resolution services as a stepped alternative to litigation.

26.4 MTAA and Members respectfully suggest that collective bargaining by dealers or dealer councils for a specific brand could be successful in achieving a more balanced relationship between manufacturer and dealer. However, too often we see dealer councils dominated by manufacturer representatives, whose mere presence at dealer council meetings makes open dialogue problematic.

26.5 The experience of dealers explained through surveys and workshops and cases exercised through mediation processes under the existing franchising code indicates that the current mediation process is of no use to dealers as the power wielded by the manufacturers is too great. This is reflected in the comments of a dealer who attempted mediation with a manufacturer:

*'.....the manufacturer attended as required, wasted the day with insults and a complete unwillingness to consider any reasonable terms. They left with no agreement being reached in the knowledge that it is prohibitively expensive for a dealer to take the next steps in beginning legal action.'*²²

27. Are car dealers generally aware of the existing dispute resolution procedures in the Franchising Code?

27.1 Yes, but are mindful of the manufactures power and their relative bargaining / negotiation strength. There is a general unwillingness to 'go it alone' against a manufacturer because of the time, cost and stress of doing so and genuine fear of repercussion or retribution through eventual termination or non-renewal. There are similar problems for Dealer Councils , who may have increased strength through numbers of dealers to better balance the power of the franchisor, the problem then becomes the wide variety, locations, attributes, characteristics and relative size and composition of dealers; within the Dealer Council which may make it difficult to reach consensus for the same fears.

Voluntary Code of Conduct

Department Questions for stakeholders and MTAA response:

28. Would a voluntary code of conduct specific to the automotive industry be effective?

28.1 No.

28.2 There is strong and compelling evidence that some vehicle manufacturers fall short of genuine commitment to negotiating good faith agreements. In turn, this weakens the entire vehicle and service supply chain, which ultimately puts businesses and consumers at risk. Ironically, Australia is one of the world's highest per-capita markets for new vehicle sales, but is arguably decades behind its global counterparts when it comes to its relationships with its supply chains and the broader automotive market place in Australia.

28.3 The use of unenforceable, voluntary codes in the automotive industry has largely failed to remedy the very conditions that spurred their development. This is also the case in the application of the Franchising Code and its failure to affect unfair and, at times damaging commercial relationships between vehicle manufacturers and vehicle dealerships. MTAA and Members believes the creation of a specific, mandated code, for the automotive industry will have a significant and positive effect. It will have the capacity to rebalance the relationship between vehicle manufacturers and their supply chain partners and vehicle dealerships and thereby secure improved outcomes for consumers.

28.4 In the 2013 Wein Review into the Franchising Code, it was clearly articulated that that in 1990, a standing Committee introduced a voluntary code of practice that included wide ranging provisions. In 1994 prominent new car retailing franchising lawyer, Robert Gardini, reviewed the then voluntary code of

practice and found that only 40 to 50 per cent of franchisors had registered under the Code and that standards under the Code were ineffective²³.

- 28.5 As evidenced in other voluntary automotive codes, where there are significant power imbalances, dominant market participants appear to be able to largely circumnavigate both the intentions and letter of these codes. Cases in point include the Heads of Agreement for access to vehicle service and repair information (2014) and the voluntary smash repair and insurance industries code of conduct.
- 28.6 The voluntary code for insurers and vehicle body repairers (Motor Vehicle Insurance and Repair Industry Code of Conduct) was designed to create a fairer working relationship between vehicle body repairers and motor vehicle insurers. Again, the voluntary nature of this code has suffered the goliath effect imposed by the insurers where attempts have been made to have the code applied. While the industry has shown that the fair application of the Code can result in success for body repairers, the sheer size and scale of the motor vehicle insurers means that any attempt to use the code or remedy disputes with insurers, takes significant energy, time and commitment from small business, often resulting in a negative outcome for the small business.
- 28.7 The failings of the voluntary nature of this Code have seen it mandated through NSW jurisdiction legislation to address shortcomings. It is being considered for mandation through similar legislation in Victoria and Western Australia.
- 28.8 Similarly, the failure of the Heads of Agreement for access to service and repair information has resulted in recommendation from the ACCC for a mandated and prescribed scheme and the commitment of Government to addressing this recommendation through a mandated Code.

²³ Wein Review 2013 Review of The Franchising Code of Conduct Pg.3

28.9 Voluntary does not carry the carrot and stick of a mandated and prescribed Code which contain penalties and greater enforceability but also rewards compliance and good faith negotiations because of the threat of penalties. This is why a mandated and prescribed Code is MTAA and Member's preference.

28.10 The complexity of the automotive industry has been highlighted in recent times through focus on consumer guarantees and warranty and by reviews and changes to the ACL and CCA. It is this complexity (name another franchise operation that provides life time support for products that have a life span of 12+ years and the costs involved with associated infrastructure (showrooms, service parts and repair facilities, staff) are very different from the typical franchises covered under the code.

28.3 For the matters under consideration there must be some government oversight and enforcement otherwise regulatory intervention will be only a part solution.

Regulatory Cost Assumptions

Department Questions for stakeholders and MTAA response:

29. Are the assumptions that underpin the regulatory costs reasonable?

29.1 In the opinion of MTAA Members and generally the assumptions for regulatory costs appear reasonable with the exception of 2C where multiple factors may impact the cost assumptions and therefore MTAA is unsure whether these are reasonable or not.

30. What additional regulatory costs should be included?

30.1 The costs of mediation can discourage some dealers from seeking a mediated outcome. Costs associated with airfares, accommodation, venue and other reasonable travel and administrative expenses need to be clear. The intangible costs of attendance and anxiety factor heavily in decisions.

30.2 Any new code would need to apply punitive measures, including heavy penalties, if either party is vexatious in their claim, or ignores or disrupts the proceedings of the mediation. MTAA recommends legislated punitive measures (penalties) to be applied to any stakeholder who does not commit to mandatory mediation under a new automotive code.

Implementation

Department Questions for stakeholders and MTAA response:

31. If an automotive code is implemented, should it apply to a broader category of vehicles, rather than just new cars?

31.1 Yes, it should apply to the automotive industry as a whole. Cars, trucks, buses, motorcycles, farm machinery, marine powered products, power equipment, automotive parts and repair outlets. The issues raised during recent investigations into the car market which impact consumers are replicated in other automotive industry sectors.

31.2 Consumers will benefit from regulatory intervention for all franchised and contracted businesses where there is a power imbalance of such magnitude that other participants and consumers are facing detriment.

31.3 However motor vehicle retailing is the highest priority and proposed solutions for new car retailing should not be held up while considering other industries. The Code should be constructed so that new car retailing issues are addressed first and foremost as these will also tend to address critical issues impacting other automotive industries.

32. Are there any practical difficulties associated with only applying an automotive code to new car dealers? For example, are there franchise agreements that cover both new cars and motorcycles?

- 32.1 Motorcycle franchise agreements mirror car franchise agreements. Applying an automotive code for new car dealers only would create potential confusion in the retail market as consumers own multiple automotive products and have expectations that levels of service would be consistent across the automotive industry.
- 32.2 The solution must equally apply to motorcycle, car rental, automotive repairers, marine powered products, and farm machinery franchised retailers who invariably experience the same concerns, albeit with some subtle differences

6. Conclusion

- 6.1 MTAA welcomes the opportunity to contribute to participate in this RIS process and remains available at any time should the review team wish to pursue matters raised in this submission further, or to access other confidential information that has been provided to other inquiries. In addition MTAA extends an invitation for the Department to access business owners prepared to discuss issues raised confidentially, by contacting the MTAA who will coordinate.
- 6.2 As industries within the automotive sector continue to consolidate and changes continue to influence businesses and their operations, the bottom line remains that consumers should still feel confidence in an economy where competition is strong, new entrants are encouraged, small businesses are able to flourish, and they have the opportunities to grow, - without harmful and detrimental impacts, and with access to protections which ensure these fundamentals.

END OF SUBMISSION