AUSTRALIAN AUTOMOTIVE DEALER ASSOCIATION

SUBMISSION TO THE REGULATION IMPACT STATEMENT

FRANCHISE RELATIONSHIPS BETWEEN CAR MANUFACTURERS AND NEW CAR DEALERS

15 FEBRUARY 2019

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FOREWORD

AADA is pleased to respond to the Department of Industry Innovation and Science's request for comments on the Regulation Impact Statement (RIS) for Franchise relationships between distributors and new car Dealers.

We welcome this RIS and the opportunity to participate in the consultation process. For some time, the AADA has been calling for an Automotive Code of Conduct to bring a degree of balance to the relationship between franchised new car Dealers and powerful vehicle Manufactures.

Many Dealers have excellent relationships with their Manufacturer partners, but Dealers are still subject to unfortunate behaviours by some Manufacturers. The power imbalance is clear as even the biggest Dealer groups in Australia are relatively small when compared to the offshore multinational car Manufacturers, which are typically Fortune 100 companies.

Issues related to this power imbalance have been well documented in the Joint Committee on Corporations and Financial Services' Inquiry into the Franchising Code of Conduct. The issues have also been raised by the ACCC in its 2017 new car retailing study and the 2013 Wein Review of the Franchising Code of Conduct.

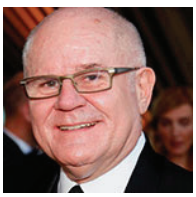
The AADA welcomes many of the options which have been supported by this RIS. Increasing non-renewal notice periods, providing reasons for non-renewal, requiring more specific pre-contractual disclosure and multi-party mediation are all options supported by the AADA.

However, we consider it is critical that the Automotive Code includes several options that have not been considered or supported by the RIS. These include:

- a mechanism which provides a link between the investment OEMs ask Dealers to make with the term of the Agreement OEMs give to Dealers,
- an end of term obligation for the buying back of stock,
- a framework for best practice in relation to Warranty and ACL obligations,
- action against the ability of OEMs to unilaterally vary aspects of the Dealer Agreement such as Prime Market Areas and KPIs.

Australia's new car Dealers will never achieve power parity with the massive corporations to which they are franchised, but an Automotive Code of Conduct which includes the above elements will go some way to providing a fairer situation.

David Blackhall
Chief Executive Officer



EXECUTIVE SUMMARY

- AADA supports regulatory intervention as the method to address the issues identified in the franchise relationships between car Manufacturers and new car Dealers.
- AADA supports the establishment of an Automotive Code separate to the Franchising Code. Our organisation is willing to discuss the merits of a schedule to the Franchising Code.
- AADA supports the increase in notice periods Manufacturers must provide to Dealers if their Dealer Agreement's will not be renewed, from six months to twelve months.
- The process of non-renewal should be accompanied by an orderly, written exit plan with relevant milestones.
- Effective and affordable dispute resolution processes should be available either to single franchisees, or for multiple franchisees.
- The AADA supports the requirement to provide a reason for non-renewal of a Dealer Agreement. Providing a reason will make it clearer whether the non-renewal has been exercised by a Manufacturer in good faith.
- The AADA maintains that the Automotive Code must contain a framework which formalises an obligation the buyback of brand-new vehicle stock, and an agreed formula for the buyback of parts and special tools.
- It is essential that the Automotive Code includes a template which provides a linkage between the investment Dealers make, the expected ROI, and the contract term they are offered.
- The Automotive Code needs to address the issue of warranty practices in franchise relationships between car Manufacturers and new car Dealers.
- Due to the power imbalance Dealers should be afforded protection from unfair contract terms. We believe unilateral variation of Prime Market Area (PMA) or certain Key Performance Indicators should be addressed in the Code.

REGULATORY INTERVENTION VS VOLUNTARY CODE OF CONDUCT

The RIS has clearly identified that there are problems in the relations between franchised new car Dealers and Manufacturers and as such the status quo is simply unsustainable.

It is also encouraging that the RIS has concluded that a Voluntary Code of Conduct is unlikely to address issues in automotive franchising. The AADA is opposed to a voluntary approach as we regard the Australian arms of the vehicle Manufacturers as merely extensions of their offshore multinational parent companies. These parent companies make decisions and issue directives on how the local arm is to operate. In short, directives are issued from abroad and it is highly unlikely that these directives would pay any attention to a voluntary code of behaviour.

A voluntary system is also concerning because it does not compel all Manufacturers to participate and even for those who do participate, it is easy to withdraw. This is particularly concerning when you consider that there is a high level of turnover of senior management at the Australia arms of Manufacturers. Often, new senior managers are dispatched to Australia from abroad. They bring with them a new approach and may use the benefit of volunteerism to withdraw from any process which they perceive to interfere with their commercial or personal career aspirations.

There are several examples within the automotive industry that have demonstrated the limits of a voluntary approach. One should look no further than the Agreement on Access to Service and Repair Information for Motor Vehicles (Heads of Agreement) signed between several stakeholders in the industry, including Manufacturers. The Agreement which was supposed to facilitate sharing of information between OEM's and independent Repairers was recently reviewed by the ACCC and found to be ineffective. The ACCC found that one of the major flaws of the Agreement was that "it is not directly binding on car Manufacturers and other industry participants".

For these reasons the AADA supports regulatory intervention as the method to address the issues identified in the RIS. In terms of implementation, the AADA supports the establishment of an Automotive Code separate from the Franchising Code. We would welcome a discussion with the Department of Industry, Innovation and Science on the option of implementation through amendments (under a separate schedule) to the Franchising Code - however, our strong preference is for an Automotive Code with dispute resolution and penalty mechanisms specifically suited to its participants.

RELATIVE SIZE AND POWER – VEHICLE MANUFACTURERS AND NEW CAR DEALERS

The AADA considers that to put our concerns in context regarding the proposed Automotive Code of Conduct and this RIS, it is essential to understand the sheer scale difference between the new car Dealers and overseas vehicle Manufacturers. The following table outlines the revenue (A$bn) for the top ten vehicle Manufacturers, and the corresponding largest motor vehicle dealership groups:

Entity	Revenue ($Bn) Car Manufacturers 2017 – Car Retailers 2018
TOYOTA	$333.33
VW	$313.93
GM	$231.11
DAIMLER	$225.63
FORD	$195.40
HONDA	$170.76
FIAT-CHRYSLER	$163.43
NISSAN	$134.21
BMW	$124.90
HYUNDAI	$112.42
Automotive Holdings Group	$6.47
AP Eagers	$2.1
Autosports Group	$1.75
Peter Warren Automotive Group	$1.43
Sutton Motors	$1.1
Patterson Chaney	$0.76
Crick Auto Group	$0.75
Alto Group	$0.725
Grand Motors Group of Companies	$0.72
Pickerings Auto Group	$0.55
Motorama Group	$0.53
John Hughes Group	$0.48
NGP Melbourne	$0.47
Heartland Motor Group	$0.43
Rex Gorrell Family Group	$0.40
Stillwell Motor Group	$0.40

It is important to note that the local presence of each of the vehicle Manufacturers are essentially branch offices controlled from head office. It would be foolish to try to argue that just because the local presence of a Manufacturer is small, that it does not wield the enormous power of its parent corporation when dealing with new car Dealers.

The sheer scale and power difference, particularly when we are talking about small family Dealerships rather than large public companies, is why we are of a view that Unfair Contract Terms and other protections against unconscionable conduct found in the Franchising Code should also apply to the relationship between overseas vehicle Manufacturers and domestic new car Dealers.

TWELVE-MONTH NOTICE PERIODS

The AADA supports **Option 2A** and agrees with the RIS's assessment that it will have a positive net benefit. This option would increase the notice periods Manufacturers have to provide to Dealers if their Dealer Agreements will not be renewed from six months to twelve months.

We have consistently made the point that six months' notice is inadequate for businesses which have:

- unique facilities which are difficult and costly to repurpose,
- high value stock and tools,
- a significant number of employees,
- customers with which it has an after-sales relationship.

The additional notice period will allow Dealers enough time for an orderly exit from the network. The view of the AADA is that the issue of a non-renewal notice should be the start of a cooperative process in which the Dealer and OEM work together to manage the closure of the Dealership. This may well result in the Dealership closing earlier than the twelve-month process, if both parties agree.

We believe that as best practice, the twelve-month notice period needs to be accompanied by a concurrent twelve-month plan which spells a series of milestones towards a fair and reasonable exit of the Dealer from the network.

PROVISION OF A REASON FOR NON-RENEWAL

The AADA supports **Option 2B** and agrees with the RIS's assessment that it will have a positive net benefit. There are recent instances in which Dealers have been franchised to a Manufacturer for decades and then been issued with a non-renewal notice for no specified reason.

There are also examples of Dealers meeting each performance indicator set by the Manufacturer to the extent that they are given performance awards by the franchisor in the course of the Agreement. Once again, such Dealers have been issued with non-renewal notices with no reason.

Under the Franchising Code of Conduct, franchisors do not need to provide reasons for non-renewal, and it can be unclear whether franchisors have acted in good faith as required under the Code. The provision of a reason for non-renewal of a Dealer Agreement will make it clear whether the non-renewal has been exercised by a Manufacturer in good faith.

STOCK BUY BACKS

The AADA supports **Option 2C** but disagrees with the RIS's assessment that it will not have a positive net benefit.

AADA believes that the twelve-month notice of non-renewal will assist Dealers in managing down their stock. However, Dealer Agreements and obligations to represent the brand do not end on the day a non-renewal notice is provided and in representing the brand, Dealers must remain stocked at agreed levels. The twelve-month notice period will only assist Dealers in managing down their stock if it is accompanied by a well-developed plan which includes a commitment to buy back stock, tools and parts at the end of the Dealer's term.

Several Manufacturers do have reasonable end of term stock buyback arrangements, but it should be noted that new car Dealers operate in a global industry and that pressure applied on local importers by the parent company abroad means Dealers are aggressively fed with new car stock. The risks for the Dealers at the end of a contract are obvious. We believe that Manufacturers are well placed to distribute "bought back" new cars, parts and tools to the remainder of its network without undue distress.

There are well established formulas which deal with parts and special tools and equipment and the Automotive Code presents an opportunity to develop a framework which formalises these as well as the buyback of brand-new vehicle stock.

We note that the Oil Industry Code of Conduct has requirements for suppliers to buy back stock from retailers, and we see no reason why new car Dealers should not enjoy the same protections.

ENHANCED CAPITAL EXPENDITURE DISCLOSURE

The AADA supports **Option 2D** and agrees with the RIS's assessment that it will have a positive net benefit. Providing a more specific and narrower range of the investment which will be required during the term of the Agreement will allow Dealers to make fully informed business decisions before signing a Dealer Agreement. Our view is that a range of +/- 10 percent from a nominal and agreed figure would meet the requirement. Such an approach would encourage greater transparency from the OEM which should lead to a more cooperative relationship between the two contracting parties.

This does not preclude the OEM from attempting to solicit the Dealers' support in making additional investment during the course of the term. It does, however, restrict the OEM's from hiding behind excessive ranges of potential expenditure to compel the Dealer to make large investments during the course of the term.

Our key point is that the nominated proposed capital expenditure should be directly relatable to the term of the contract being offered to the Dealer to allow that investment to be recouped over the life of the contract.

TENURE

The AADA supports **Option 2E** but disagrees with the RIS's assessment that it will not have a positive net benefit.

The AADA, through its advocacy efforts, including its submission to the Parliamentary Inquiry into the Franchising Code of Conduct, has advocated for a minimum 5-year term with an automatic renewal of one term of 5-years at option of Dealer if not in breach of the terms of the Dealer Agreement.

The RIS assessed this option and found it to not have a positive net benefit. In the absence of the specific 5+5 term option, the AADA strongly advocates that the Automotive Code must include a mechanism which provides a linkage between the investment Dealers make and the contract term they are offered. As noted above, the term of the contract should be long enough to allow the Dealer to recoup their investment.

To understand how important this issue is in the scheme of the Automotive Code, one need only look at a number of the independent reviews which have looked at franchising and the new car retail industry in recent years.

For example, the 2013 Wein review of the Franchising Code of Conduct recommended that:

> *An analysis of the impact of a minimum term and standard contractual terms for motor vehicle agreements should be undertaken prior to a future review of the Code.*

More recently, the ACCC in its review of the New Car Retail Market found that issue should be considered. In its final report its urged consideration of:

- *a required minimum term for dealer agreements with the objective of allowing dealers a sufficient period in which to recoup capital investment required by the manufacturer*
- *limitations on the level of capital investment that a manufacturer can require of a dealer based on the tenure of the dealer agreement offered*
- *enhancing a dealer's rights to be compensated for capital investment required by the manufacturer in the event of non-renewal of the agreement*

Based on these findings, we strongly urge that the proposed Automotive Code includes some form of linkage between investment and term.

SELLING A FRANCHISE

The AADA is of a view that the Automotive Code should make provision to prevent franchisors from using unreasonable delaying tactics when a Dealer wishes to sell their franchise.

There are already provisions under the Franchise Code preventing franchisor from unreasonably withholding approval of a prospective buyer of a franchisee or the transfer of its franchise. The new Automotive Code should indicate what is a reasonable length of time for a Franchisor to approve a purchaser.

The AADA further understands that some Manufacturers are quite directive in buy/sell situations to the point of mandating who the franchise can be sold to, which diminishes the Dealer's freedom of action in trying to achieve the best sale price for their asset. We consider that such behaviour is anti-competitive and against the interests of the Dealer in particular, and the industry as a whole. The AADA recommends that end of contract arrangements should be considered as a specific issue within the Automotive Code.

MULTI-PARTY DISPUTE RESOLUTION

The AADA supports **Option 2F** and agrees there is a vital requirement to include multi-party dispute resolution processes in any new Automotive Code.

The current arrangements under the Franchising Code allow only dispute resolution between the two parties to a Franchising Agreement. The AADA is strongly of the view that a stand-alone Automotive Code of Conduct must make allowance for disputes between multiple franchisees acting in concert and their common franchisor. We note that the ACCC is currently considering relaxing the rules about collective bargaining to allow specified classes of businesses, such as franchisees to bargain collectively with their common franchisor.

The AADA strongly supports the principles behind the ACCC consideration of the matter and argue further that similar principles should be included in the Automotive Code to enable franchisees to collectively bring forward disputes against their common franchisor.

The proposed mediation-focused dispute resolution approach is strongly supported by the AADA, but we note that any appointed mediator must be seen to be unflinchingly independent and resourced appropriately to deal with what could be quite complex matters.

WARRANTY PRACTICES

The AADA is of the view that an Automotive Franchising Code needs to address the issue of warranty practices in franchise relationships between car Manufacturers and new car Dealers.

Dealers are currently subjected to behaviours which leave them financially exposed and are often not empowered to resolve consumer claims, effecting the ability of consumers to enforce their ACL rights. The ACCC has raised concerns that some car Manufacturers have policies and procedures about how Dealers respond to consumer guarantee or warranty claims which may limit a Dealer's ability to provide a refund, replacement or repair to a consumer. This runs contrary to the Dealer's legal right which entitles them to the right of indemnity when they incur expenses to meet a claim.

Due to the imbalance in power, Dealers are reluctant to enforce their ACL right of indemnity and often feel powerless to assist consumers due to explicit instructions from Manufacturers.

For example, the well-known case where Ford Motor Company engaged in unconscionable conduct in the way it dealt with complaints about a faulty transmission is an example of where Dealers were instructed by the Manufacturer to deny consumer's their rights to refunds or replacements.

The Automotive Code provides an opportunity to develop a framework for processes around warranty work, payment and audit. The AADA believes such a framework may well have prevented a situation such as the Ford case.

There is no other industry like the passenger vehicle industry where repairs are as central to the overall business model. Workshops in Dealerships are constantly operating to repair and service customer vehicles, but too often the practices of OEM's mean that they are not fully reimbursed or are subject to unreasonable practices during the warranty audit process.

Manufacturers/Importers issue policy and procedure documents to franchised new car Dealers in relation to warranty payments. Often the policy and procedure documents contain onerous or capricious administrative requirements. While some requirements are necessary in order to ensure that Dealers are not making fraudulent claims, onerous administrative processes are too often used to "claw back" legitimate warranty claims.

Even worse, the policy and procedure documents attached to Dealer Agreements permit the Manufacturer to extrapolate the minor non-conformities based on the sample audited to the entire warranty period. For example, if one photograph is missing for one part in a sample of ten claims and the entire audit period consisted of one hundred claims, the Manufacturer will assume that there are another nine missing photographs, reverse that number of claims and then invoice the Dealer for the monetary value of them.

An additional common problem is that Manufacturers often do not compensate Dealers for the time required to diagnose faults or test repairs. One common complaint is that some Manufacturers direct Dealers to test drive a vehicle at highway speeds after it has been repaired. For a metropolitan Dealer,

it will take considerable time to take the vehicle to a location where it can be driven at such speed. There is no allowance or compensation allocated for that time.

There is no legitimate purpose for either clawing back legitimate warranty claims for minor non-conformities, or extrapolating claw backs based on a sample when the Manufacturer could conduct a full audit.

The AADA is of the view that if the Automotive Code has a framework of fairness for the management of warranty claims, breaches of the ACL will be prevented.

UNFAIR CONTRACT TERMS (UCTS)

Due to the imbalance in power between overseas vehicle Manufacturers and domestic new car Dealers, the AADA believes franchised new car Dealers should be protected by unfair contract term provisions. Of concern is that most Dealer Agreements allow the local importer to unilaterally vary the terms of the Dealer Agreement. Unilateral variation is specifically prohibited by the unfair contract terms legislation, but franchised new car Dealers do not meet the definitional threshold for which businesses should qualify.

For example, one of the thresholds states that only businesses that employ fewer than 20 people are entitled to these protections. In a speech recently, ACCC Chair Rod Sims stated that:

> *"the thresholds sometimes exclude businesses that we think should be protected from unfair contract terms. For example, we think it is likely that the majority of authorised motor dealers fall outside the current thresholds because of the high value of the products sold and perhaps also the number of employees..*

AADA acknowledges that the Treasury is currently investigating reforms to UCTs. It appears that franchised new car Dealers are unique in that they employ a significant amount of people but are also subject to power imbalance in their relations with Manufacturers.

Including these protections under the Automotive Code provides the Australian Government with an avenue to provide these protections to Dealers without aggressively expanding the current thresholds. One suggestion flagged by the ACCC on this issue relates to exempting aspects of the Dealer Agreement from unilateral variation. Aspects such as the Prime Market Area or certain Key Performance Indicators could be quarantined from the unilateral variation.

ANSWERS TO QUESTIONS

1. **What is standard industry practice for non-renewal, is it longer than the minimum six months required under the Franchising Code?**

   In most of the recent cases the AADA has observed, the Manufacturer has provided the minimum required notice period of six months. We are also aware of instances where a Manufacturer has placed a large proportion of its Dealers on twelve-month Agreements, which essentially means that every six-months the Dealer is informed whether they will remain a Dealer.

2. **How long does it take to negotiate new franchise arrangements with a different car manufacturer?**

   Anecdotally, negotiations for a new franchise Agreement from initial conversations to a signed Agreement take approximately nine to twelve months, however such a process can take as long as two years. It should be noted that once a franchise Agreement ends, there is a period in which the Dealership will not operate as it arranges supply of stock, setting up of workshop and organising corporate identity for the new franchisee.

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?**

   The AADA believes that twelve-months should be the minimum statutory notice that the Manufacturer gives the Dealer. This provides the Dealer with more scope to facilitate an orderly transition. Of course, there are unique elements of a franchised new car dealership (size of investment, multiple profit centres, after sales customer relations, etc.) and the greater the notice of non-renewal period the better. While twelve-months is a more appropriate period of notice, it must be accompanied by an exit plan with built in milestones that facilitates and orderly transition for both the Dealer and the OEM.

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?**

   Yes. The Manufacturers will need to engage in better, longer term planning for their network strategies. However, this will be outweighed by the benefits which accrue to the Dealer, their employees and their customers. Twelve months is a more realistic timeframe for a Dealer to engage in such activities, such as managing down stock, providing long-term employees with more notice of potential changes, planning for repurposing of bespoke facilities, seeking out and securing a new franchise.

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?**

   The AADA believes that the matter is not one of Dealers not understanding the process, but that the relevant documentation is made unnecessarily complex and obtuse. A requirement for documents to be written in clear and simple English expression would be of great assistance.

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

   As with many other aspects of automotive franchising, there are good behaviours by some and poor behaviours by others. Some Manufacturers do provide reasons for non-renewal, but many do not. On occasions when reasons are provided, they are laughable. On other occasions no reason is provided whatsoever. The crux of the issue is that the OEMs are not required under the Franchising Code to provide a reason, making claims that the franchisor has not acted in good faith nigh impossible to prove.

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

   Running down stock is not simple in the new car retail industry. Managing directors of local distributors are under immense pressure to play their part in feeding vehicle production plants and the highly competitive Australian market and the fierce battle for market share results in OEMs aggressively pushing their stock onto their Dealer networks. Under many Dealer agreements, Dealers must maintain an 'automatic release floor plan facility' with their financier. The automatic release system means that Dealerships are constantly being fed with new stock. Dealers who revert to a manual release facility can be penalised by the OEM. There have been occasions whereby at the end of a term which is not being renewed, an OEM has refused to buy back stock and has suggested the Dealer report as sold stock in the Dealership and stock in transit.

8. **How much stock would a dealer typically have remaining when an agreement is not renewed?**

   This may well depend on how astute the Dealer is and how helpful the OEM is. One comment to make in this regard is that residual stock has often been unsold for a reason, most likely because it is a less-desirable product. Another comment is that the level of stock may well turn on market conditions in the month or two leading up to the end of the term.

9. In what circumstances do buy-back arrangements generally apply in current agreements (for example, at non-renewal, termination by agreement)?

Once again there are good behaviours and there are poor behaviours. Some agreements provide for buy back of stock at termination and end of term. Other agreements are completely silent on stock buy backs.

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?

This may happen on occasion, but it is certainly not the norm. Such behaviour would require prior consent by the Manufacturer, a capacity of the purchasing Dealer to be able to take on additional stock, and the unwinding of the floorplan finance. Due to the auto-release arrangements described earlier, at any given time Dealers are generally fully stocked and have no capacity for additional units. Further, any such action would be totally voluntary, which would leave behind unwanted or undesirable stock.

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

Generally speaking, Manufacturers like to protect brand equity. Having a great deal of stock at auction is an outcome most responsible OEMs would like to avoid. Having said that, we have seen cases in recent times in which major OEMs have simply refused to entertain any buy-back of stock whatsoever.

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

Some OEMs currently incorporate buy-back options into their Agreements. AADA would be surprised if mandating stock buyback results in a reduction in Agreements. In our experience, this is not a consideration in deciding on the appointment of a Dealer.

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?

Under the Franchising Code there are safeguards for franchisees from having to incur significant capital expenditure. However, these are easily circumvented as OEMs use the threat of non-renewal to force Dealers to incur additional capital expenditure within the term of their current Dealer Agreement in order to be ready for their ‘new’ Agreement. This expenditure is not treated as requiring prior disclosure to Dealers when entering into their initial Dealer Agreement because Manufacturers take the position that the expenditure is for an entirely new Agreement.

Manufacturers can also compel Dealers to incur undisclosed capital expenditure during the term of the Dealer Agreement by amending their 'Franchise Standards' or 'Dealership Fit out' policies effectively requiring Dealers to refurbish or relocate; and providing a written statement setting out the rationale for the expenditure, the benefits and risks of making the investment in accordance with clause 30(2)(e) of the Code. In practical terms, providing this 'written justification' is easy for Manufacturers and there is no mechanism for Dealers to challenge it.

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?

Practice varies. But some OEMs give wide ranges in a presumed attempt to maintain maximum flexibility. It is not uncommon for ranges of capital expenditure to be 100% to 200% above the base figure.

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

Some OEMs engage in discussions on the capital expenditure required in an open and honest way. Others are less forthcoming and there are many examples where the capital expenditure for a project turns out to be substantially greater than the amount discussed prior to the project.

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?

The AADA is unable to address this specifically because of confidentiality concerns, but we are able to mention a European brand that came to Australia, appointed twenty Dealerships, and then left the market after only twelve months. Another European brand put its Dealers on twelve-month contracts, and then terminated a large proportion of them. In both cases, Dealers were required to make substantial investments which were then never recovered.

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?

Franchised new car Dealerships undertake capital investments to build facilities under strict guidance from their franchisor who receive their Corporate Identity (CI) directives from head office overseas. There is very limited scope for a Dealer to undertake these investments with an eye to a potential future

agreement with another distributor. Even, if a Dealer is fortunate enough to accommodate their new franchise in a stranded facility, it is almost certain that the new franchisor will require significant investment to bring the facility up to the required standard of the new brand. Manufacturers are typically very prescriptive in their CI requirements, often specifying lighting, tiling and even furniture. They will also stipulate the suppliers of the fit-out materials meaning that ultimately Dealers build facilities that are very bespoke and unlikely to be compatible with any other brands.

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?

Establishing unconscionable conduct has proved to be notoriously difficult because of the high threshold imposed. Furthermore, Dealers are very wary to engage in court action against very well resourced multi-national companies.

19. 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?

See response to Q13.

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

Many OEMs already provide 5-year minimum terms and would not have to change. Introducing minimum terms would potentially encourage OEMs to set up their Dealer networks in a responsible manner.

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

OEMs report that product development, testing and verification programs required for vehicle models is more than 7 years prior to introduction into the market. Based on this assessment minimum five-year agreements can be aligned with their product cycles.

22. 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?

Consumers requiring repair and service work on their vehicles, especially in rural and regional areas, often depend on their local Dealer. Not having a local Dealer, especially for warranty repairs, can become a major inconvenience.

OEMs may allege that the 5+5 system we are proposing restricts flexibility. Dealers take on much of the risk when it comes to signing a Franchise Agreement and given the financial commitment, they make deserve a tenure commensurate with this investment. In the absence of the prescriptive 5+5 option, the Automotive Code should have a mechanism which links investment demanded by the OEM to the term given to the Dealer.

23. 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?

Naturally the longer the term, the greater degree of certainty Dealers will have. Again, the AADA would like to reiterate that more important than a minimum term is strong linkage between investment and tenure, which allows Dealers to recoup their investment.

24. 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?

AADA acknowledges that changing business models are a consideration for OEMs and that there are concerns about being locked into Agreements which restrict flexibility to respond to changing market conditions. However, the same principle should apply when OEMs mandate investment from Dealers – don't ask for major investments, which can only be recouped over a term of seven years for example, if there is concern around changing market conditions.

25. Would an ability to enter into multi franchise mediation make car dealers more likely to utilise mediation as a means to resolve disputes?

Definitely. Dealers are always concerned about the possibility of retribution and discrimination for a single Dealer making a case against an OEM. Based on information received from professional mediators familiar with the industry there have been less that 10 new car franchise mediations under the Franchising Code since its inception. The mediation process as it stands is ineffective at addressing Dealer concerns.

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

There is a low level of general awareness of the existing dispute resolution procedures in the Franchising Code and there is little willingness for car Dealers to engage in this process. The reasons mentioned above regarding the fear of retribution are a driving factor.

Section 14

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

The AADA is opposed to a voluntary approach as we believe the Australian arms of the vehicle Manufacturers are merely extensions of their offshore multinational parent companies. These parent companies issue directives on how the local arm is to operate. In short, directives are issued from abroad and it is highly unlikely that these directives pay any attention to a voluntary code of behaviour.

A voluntary system is also concerning because it does not compel all Manufacturers to participate and even for those who do participate, it is easy to withdraw. This is particularly concerning when you consider that there is high level of turnover of senior management at the Australia arms of Manufacturers. Often, new senior managers are dispatched to Australia from abroad. They bring with them a new approach and may use the benefit of volunteerism to withdraw from any process which they perceive to interfere with their commercial aspirations.

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

We are comfortable with the regulatory costs underpinning this RIS. These costs are manifestly insignificant when considering the scale of the OEMs.

29. What additional regulatory costs should be included?

We would like regulatory costs to be included for developing a warranty/ACL framework and extending certain unfair contract terms to Dealers. We expect these costs will be insignificant for the OEMs.

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

The AADA can only speak to the problems in the new car retail market.

31. 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?

See above.

CONCLUSION

Our experience shows that leading car Manufacturers base their success, at least partly, on cooperative and mutually-beneficial relationships with their Dealer networks. But even those relationships can be made better through a comprehensive and mandatory Automotive Code of Conduct. As we argue above, such a Code should protect the weak from the strong, include meaningful dispute resolution procedures, and prevent exploitation when the relationship comes to an end.

We would be happy to meet with you to discuss our submission. If you require further information or clarification in respect of any matters raised, please do not hesitate to contact a member of the AADA team.

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