

OUT16/45387

Manager
New Car Retailing Industry Market Study
Australian Competition and Consumer Commission

By email to newcars@accc.gov.au

Dear Sir or Madam,

New Car Retailing Industry Market Study

Thank you for giving the Office of the NSW Small Business Commissioner (OSBC) the opportunity to provide feedback on the October 2016 New Car Retailing Industry Market Study (issues paper).

The OSBC is committed to supporting and improving the operating environment for small businesses throughout NSW.

The OSBC works closely with small businesses and industry to identify regulatory requirements that place an unnecessary burden or cost on small businesses across a wide range of sectors. This extends to acting as the NSW small business representative on a range of government agency consultations, reviews and reforms.

Our involvement with motor dealers

The OSBC has been involved with motor dealers since 2013. In NSW motor dealers can access remedies for unfair contracts and unjust conduct under Part 6 of the *Motor Dealers and Repairers Act 2013* (MDRA). The MDRA enables motor dealers or an approved motor industry group to apply to the OSBC for assistance in dealing with an unfair term of a supply contract or unjust conduct by a vehicle manufacturer or supplier.

Under the MDRA, parties must attempt mediation and obtain certification from the OSBC before making an application to the NSW Civil and Administrative Tribunal for a declaration that a term of an agreement is unfair.

Fear of retaliatory action has been cited to us by many dealers as a deterrent in proceeding to formalise their complaints and seek remedies for unfair contracts and unjust conduct in relation to manufacturers' supply contracts under the MDRA.

In the course of the OSBC's involvement with the industry we have engaged extensively with industry stakeholders and note several issues present in relationships between car dealers and manufacturers that are relevant to this market study.

Manufacturer warranty

We note that the scope of the issues paper does not extend to demonstrator vehicles – but we highlight that demonstrator vehicles are linked to an issue with manufacturer warranties.

A manufacturer's warranty starts once a vehicle is 'sold'. Dealers' supply-contracts with manufacturers either force or incentivise the 'sale' of cars to achieve sales Key Performance Indicators (KPIs).

New vehicles are often registered as 'sold' to achieve this end, and registered as 'demonstrators'. Once registered as demonstrators the vehicles are reported as 'sold' and the warranty starts (not when the customer takes delivery of the vehicle).

Most consumers would expect the warranty to start once they take delivery of the vehicle. Dealer extended warranties may address the shortfall. Some vehicles may be sold quickly while others may take months to sell.

Dealers are not always able to determine the amount of stock they will receive from manufacturers. They argue that stock allocations are determined by the manufacturer, and dealers are often in a situation where they are bound by contractual obligations and / or KPIs to sell quotas of models, including models that are not top-selling cars.

There are regional differences in buying trends. Dealers complain that sales targets of manufacturers are too high and that dealers are forced to buy unsold vehicles (demonstrators) to comply with the supply agreement. Failure to reach KPIs can mean that they do not achieve sales targets and will not receive margin bonuses.

Manufacturers do not compensate for old stock but give incentives to sell by decreasing the price. Stock is supplied on bailment (a financier buys the vehicles), and the dealer pays interest costs on bailment finances.

Falsely inflated brand sales figures

Manufacturers require or pressure dealers to register new motor vehicles where there is no customer order to falsely inflate brand sales figures against competitor brands.

Margin payments / retail bonuses

If dealers don't achieve their sales KPIs, they may not be entitled to a margin bonus. Margin bonuses are essential to dealers because they are a major source of income along with income from finance and insurance commissions, and service agreements. The availability of margin bonuses is key to the viability of a dealer business as there is little profit in the sale of new cars.

Dealership franchise contracts for the supply of motor vehicles

An inquiry into the market practices of new car sales and the practice of dealers, should arguably extend to the source of the industry practices, which are the supply contracts (dealership agreements) between dealers and manufacturers.

The relationship between dealers and manufactures is characterised by an imbalance in bargaining power in favour of the manufacturer, with dealers offered contracts on a 'take it or leave it' basis.

If a dealer does not agree with the terms of the dealership agreement, there is little scope for them to negotiate variations to the terms, or to have terms inserted into a contract.

Dealers state that their overheads and risk exposure create an imbalance in bargaining power between them and the manufacturer. The imbalance in bargaining power in favour of

the manufacturer is evidenced by a lack of negotiation on terms of the dealership franchise agreement, and in the operation of the agreement.

A manufacturer's policies, standards and guidelines are referenced in dealer agreements (but do not form part of the contract) and unilateral amendments by the manufacturer during the term of the dealership will impact on the terms of the deal, often to the detriment of the dealer. Unilateral changes may be made to sales KPIs, for example, where the sales KPIs are tied to margin payments.

The investment and risk exposure of dealers is high and fear of reprisal deters most dealers from exercising their legal rights in relation to unjust conduct or the imposition of unfair contract terms by manufacturers.

Terminations

Terminations without cause have been cited as a significant source of the imbalance in the relationship, together with end of term arrangements.

Terminations for non-performance are also a source of concern among dealers, particularly when there is no obligation for the manufacturer to highlight performance issues or provide the dealer with an opportunity to address these issues prior to termination.

Exclusivity

Dealership agreements usually do not provide a dealer with any guarantee of exclusivity of a dealership Primary market Area (PMA).

Any requirement for franchisee exclusivity of a dealership PMA would also need to include a prohibition on amendments to the boundaries of the PMA. Altering a dealer's PMA during the term of the dealership agreement can significantly alter the terms of the deal and impact on a dealer's business viability.

The issue of company stores competing with dealers in their PMAs also extends to advertising and a manufacturer's ability to 'capture' the good-will generated by dealers.

Minimum term

The recommendation for a minimum term for automotive franchise agreements was flagged for further consideration in the Review of the Franchising Code of Conduct. Consideration of a minimum term would need to delineate between initial terms and renewals or options.

A requirement for a minimum term could include a method for calculating a sufficient term relative to a dealer's infrastructure expenditure, particularly if the expenditure is required by the manufacturer.

Confidential submissions from dealers to the Review of the Franchising Code argued for a minimum term of the franchise agreement to address a concern that the length of term should be sufficient to recoup capital investment.

Consumer finance

Some manufacturers require that dealers use only the manufacturer's financial services provider for consumer finance, and prohibit the use of other financial service providers.

A dealer's entitlement to bonus payments is tied to the amount of finance that is caused to be written by the dealer.

Application of unfair contracts terms (UCT) law

Dealership agreements often reference other documents in relation to a manufacturer's guidelines and policies that are not annexed to the contract. Dealers are obligated by terms of the dealership agreement to comply with any unilateral variations by the manufacturer to the manufacturer's guidelines and policies, even if it will cause detriment to the dealer business.

Typical variations to the agreement include: variations of stock allocations; variations of sales quotas; variations of performance indicators; and variations to PMAs.

The scope for UCT legislation to impact on Motor Dealer Franchise Agreements is limited, for many dealership agreements the upfront price payable will exceed the threshold of \$300,000 or up to \$1 million for contracts longer than one year.

However, there may be some scope for the legislation to capture renewals of dealership agreements for a term of one year. Smaller regional dealership franchises (which are typically multi-franchise models) may also be eligible to access the legislation.

Should you wish to discuss any of the issues raised in this submission, please contact Nicola Gorton, A/Research and Education Manager, on 02 8222 4882 or by email at nicola.gorton@smallbusiness.nsw.gov.au.

Yours sincerely



Robyn Hobbs OAM
NSW Small Business Commissioner

22 November 2016