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14 May 2007

General Manager  
Cc Paula Preston  
Adjudication Branch  
ACCC  
PO Box 1199  
Dickson ACT 2602

Dear Sir/Madam,

Following my telephone discussion with Marina, I am writing to seek guidance and a review of the Exclusive dealing notification N91131 lodged by Sleepy's Pty Ltd on 10 June 2003.

I entered into a franchise agreement for the Penrith Sleepy's store in August 2005. My husband manages the store.

In March 2005, when we first met the franchisors, the approved suppliers included 2 mattress suppliers (Sealy and Sleepmaker) and a number of accessory suppliers. We were told by the franchisors and franchisees we met at the time, that the 2 mattress suppliers:

- held the majority market share in Australia
- were considered to be the premium quality suppliers in Australia
- maintained a healthy competitive relationship within the group which facilitated sales; "kept them honest".

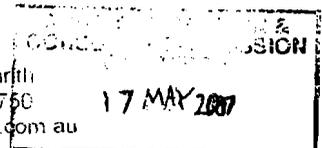
While Sleepy's negotiated the general range and costs, discounts were available from the local supplier representatives, in particular to support promotional activities by each franchisee.

Our franchise agreement states we "will purchase Approved Stock only from Approved Suppliers", Sleepy's may "in its absolute discretion, change Approved Stock, Approved Services or Approved Suppliers" and that "words importing the singular include the plural and vice versa".

About 2 weeks after we opened a store at Penrith, one of the Sleepy's directors advised that Sealy were being removed from our approved supplier list. This was presented as an opportunity that would offer significant advantage to our business.

In the opening weeks when we had the 2 suppliers, we traded extremely well with promotional discounts and support offered by Sleepmaker. One particular promotion saw us set a weekly sales record for the Sleepy's network. With the move to the single mattress supplier, Sleepy's advised that the previously available, locally negotiable, discounts and supplier support were no longer available.

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We now struggle to offer our customers competitive pricing and quality product while running a sustainable business.

We have had 3 price increases over the last 14 months, amounting to over 10%, in addition to changes to some bed specifications that we believe we not appropriately cost adjusted. Whilst researching the market for alternate suppliers, we have seen wholesale pricelists that suggest other manufacturers have not delivered similar price increases over the same period, despite the use of some common components e.g Dunlop foams. Some of this has been passed onto our customers; some has been absorbed. Sleepy's however benefit through every price increase as the rebate they claim directly from the supplier is % based.

Further, we have experienced significant quality and supply issues over an extended period. This has resulted in impacts to our customers by way of delayed deliveries and changes to the purchased product, in particular the tick (material cover of a mattress), without prior notice.

Sleepy's even advertise a "Specification Guarantee" that states that "We guarantee that the specification and construction of the mattress we deliver will be exactly the same as the one selected by you in store". This is regularly not the case.

In looking to relieve the issues the single supplier arrangements has created for our business and our customers, I came across the Exclusive dealing notification above. I noted the following points which appear to be different to our current experience:

- a. "nominated suppliers to consist of at least approximately ten suppliers". We currently have 1 supplier, Sleepmaker, for what amounts to over 99% of our business. We have 1 foam mattress supplier and 2 accessories suppliers. The foam mattress supplier (Dunlop Foams) and 1 of the accessories suppliers (Tontine) are owned by the same company (PAC Brands) as our mattress supplier. In fact, it was suggested at the presentation of the move to the "single supplier" that we would eventually purchase all of these products from Sleepmaker to make our ordering simpler – this has not occurred.
- b. "the purpose of the restriction is to ensure quality standards are met". We have continued to experience quality issues over an extended period of time. In addition, Sealy, the supplier who was removed from our approved suppliers, were and still are, considered to hold the major market share in Australia and have the highest quality within the industry. It is clear that this supplier was removed from our approved list for very different reasons.

Sealy and Sleepmaker offered stores a 15% discount for the purchase of floorstock. Sleepy's failed to advise us prior to signing our agreement that Sleepy's claimed the initial floorstock discount for new stores. Further, as we were new to the business, Sleepy's planned and ordered our floorstock, filling our store despite our belief that the impending changes had been planned for months. The change to the supplier arrangement meant that approximately 75% of our stock had to be changed just weeks after our opening. Further, we would no longer receive floorstock discounts under the new supply arrangements. In addition, Sleepy's received a rebate (of an undisclosed amount) for both the initial floorstock and the new range. In light of the timeframes involved, we requested Sleepy's provide us with the initial floorstock discounts; they have refused.

As part of our franchise agreement, we contribute to an advertising levy. This levy was stated to be 5%. Sleepy's invoice us for a 4.4% advertising levy and 1.1% training levy, referring to a clause in our agreement about GST being added to supply. I have questioned the levy as being regarded as supply and given that both the initial franchise fee and the administrative fees we pay monthly were

GST inclusive, believe Sleepy's to be overcharging this levy but have failed to come to any agreement with them.

Further, prior to our joining the franchise, Sleepy's presented that they believed only low cost marketing was needed to achieve the required results i.e. there was no national branding or advertising using higher costs mediums such as television and radio. Simply, a flyer was produced for letterbox distribution every month. Any collected levy in excess of the flyer distribution was claimable by franchisees for local promotions. This was changed in May 2006 after Sleepy's hired a marketing and branding consultant. In mid to late May 2006, we were advised that any excess would not accrue past 1 May 2006. This was now to be used for a National radio campaign that would commence in July 2006 – this never eventuated in Sydney as Sleepy's felt Sydney radio was too expensive and not justified given the number of stores open in Sydney.

Additionally, it took months for Sleepy's to provide any detail in regards to the advertising levy despite repeated requests. Firstly, I requested the detail regarding the expenditure attributable to our flyer distribution so I could claim against the excess that had accrued up to May 2005. Sleepy's initially advised that there was no longer an excess as they had used it all. After further discussion, they agreed to refund some of the levy. They are still to explain a number of costs attributed to our store. Secondly, I requested a report of the overall fund usage given the changes that had occurred. They have provided a 1 page auditor's report with a 1 page document outlining at a very high level the fund usage. One line, general advertising expenses, accounts for almost \$300000 in 2006, despite the fact that the only advertising undertaken was the printed flyer and the newspaper advertising and these are separately itemised.

Sleepy's also receive a contribution from Sleepmaker. With the move to the "sole supplier" arrangements, we were advised that Sleepmaker would fund local newspaper advertising on a fortnightly basis for each store. This was stopped by Sleepy's in September 2006 due to some franchisees not paying their levy in a timely manner and issues with others not adopting the new branding requirements.

Since 2006, Sleepy's have changed from a full franchisee model to incorporating company stores, joint venture stores and full franchisee stores.

We have now been put on stop supply by Sleepmaker due to a disagreement over one of our initial order invoices. Sleepy's placed the order, failed to follow correct procedure in placing the order and then failed to address issues we raised when they changed our supply arrangements from being via BSL Finance to direct to the suppliers. They have ignored requests from both myself and solicitor to have the issue resolved, leaving us in the current position of having no supply.

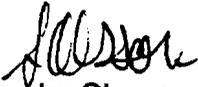
I am seeking your direction in regards the following:

- a. Should Sleepy's have disclosed to us prior to our signing the franchise agreement the impending change to the supplier arrangements as being "material to the running of the franchised business"?
- b. Is our supply arrangement third line forcing? If so, does the abovementioned notice provide Sleepy's the immunity to allow this to continue? Does our franchise agreement allow them immunity to third line forcing?
- c. What constitutes an audited report of the promotional fund expenditure? Am I entitled to see a more detailed explanation of promotional funds usage?

- d. Are there any mechanisms available to ensure that the company and joint venture stores do not attract advantageous, anti-competitive benefits as a result of the "company" relationship?
- e. Could the activities above constitute unconscionable conduct?
- f. What steps can be taken in relation to these issues?

I appreciate any assistance you may provide in better understanding this situation. Should you require further information, do not hesitate to call.

Yours Faithfully,



Sandra Olsson