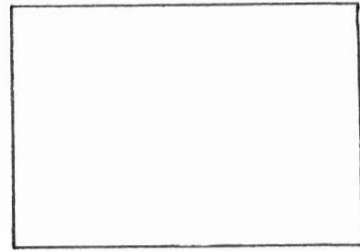


31st March 2009



EXCLUDED FROM
PUBLIC REGISTER

Email to: Australian Competition and Consumer Commission
GPO Box 3131
Canberra ACT 2601

Attention: Tess Macrae

Your Ref: 2655848

Dear Ms Macrae,

Subject: Third line forcing notification N93718 Lodge by PoolWerx Corporation Pty Ltd

As a franchisee of Poolwerx I wish to strongly oppose the third line forcing notification submitted by the Franchisor on the grounds that the Public detriment outweighs the public benefit (if any) of the proposed arrangement and on the grounds that the proposed conduct is not likely to result in such benefit that the conduct should be permitted.

My submission will be in three parts;

Discussions about the notification

Discussions regarding Poolwerx response to ACCC for more information.

Discussions as to previous decisions made by the ACCC with regards to third line forcing within franchising and the areas that the ACCC considers during the decision making process.

Part One: Discussion of Notification N93718

Notification states:

2. Notified arrangement

(a) Description of the goods or services in relation to the supply or acquisition of goods and services to which this notice relates:

The goods and services to which this notice relates can best be summarized by saying that the notification relates to each and every good and service that a franchisee requires both to run their business and to supply to their customers.

(b) Description of the conduct or proposed conduct:

In this section, Poolwerx has incorrectly represented the location and context of the clause referring to Rebates. In the Franchise agreement the clauses relating to rebates are located at 9.8.1, 9.8.2, 9.8.2.1 and 9.8.2.2 and not at 11 to 11.2.2 as Poolwerx notes them to be.

In addition the notification states:

“PoolWerx may pay any rebates or financial incentives received from the manufacturers or suppliers into the Marketing Fund.. ...”

However the use of repeated full stops in the citation give the false impression that the clause continues further, these punctuation marks do not appear in the agreement and what is stated is actually the entire clause¹.

3. Persons, or classes of persons, affected or likely to be affected by the notified conduct

(a) Class or classes of persons to which the conduct relates:

(Refer to direction 5)

PoolWerx franchisees or existing franchisees that are granted a renewal of their franchise agreement. However, ultimately the proposed approved supplier arrangements will affect all PoolWerx franchisees.

Poolwerx regularly asserts the 100% nominated supplier purchases rule on all franchisees. Some franchisees are already signed to the new franchise agreement that states this but many franchisees are still under a contract which requires purchase of 95% of goods and services from nominated suppliers. Despite what their contract says they are still being “strongly advised” that they must purchase 100%². There is some confusion as to how the proposed arrangements would work if not all franchisees can be legally required to purchase 100% of nominated goods and services. This could result in some franchisees being offered more favourable supply arrangements than others³.

¹ Current franchise agreement

² Parliamentary Joint Committee on Corporations and finances, Inquiry into Franchising, Submission Damien Hansen

³ Other existing Poolwerx Franchise Agreements

(b) Number of those persons:

(i) At present time:

140 franchisees. Also see (ii) below.

(ii) Estimated within the next year:

(Refer to direction 6)

Approximately 20 new franchises will be granted to franchisees by PoolWerx and approximately 22 existing franchise agreements will be renewed within the next year.

Statement (ii) fails to take into consideration the number of franchises that could potentially be sold by existing franchisees. These are neither new franchises nor renewals but the purchaser will be affected by the proposed arrangements. It is unknown to franchisees how many franchises are currently up for sale but this figure must surely be taken into consideration in the estimate.

Market Share:

Poolwerx estimates its market share at 5%. This is half the market share that is estimated by competitors and suppliers. For instance an exclusive dealing notification lodged with ACCC by Waterco also in 2009 estimates Poolwerx share of the market as being 10%.⁴

Discussion of Proposed Benefits.

Poolwerx claims that the proposed arrangement will help to:

“ensure franchisees are able to purchase products at lower average prices, which will place franchisees in a better position to compete in the relevant market;”

I refute this claim. Franchisees regularly find that they are not able to acquire goods at lower average prices and frequently encounter situations where substitute goods can be acquired cheaper than from nominated suppliers. Some suppliers have intimated that they could offer better discounts for franchisees if they did not have to recoup the costs of the rebates its must pay to the franchisor. Franchisees, who pay a relatively high amount of royalty fees at 15% of turnover, rely upon significant discounts on goods to remain competitive.

The number of nominated suppliers is very limited. There is in most cases only one supplier for each type of product. Suppliers have a captive market and most do not have to compete with other nominated suppliers for the franchisees’ business. This means there is no incentive to compete on price and no incentive to provide proper levels of product support and customer service to franchisees.

I contend that the reputation and value of the Poolwerx brand and system pivots around the central tenet that Poolwerx franchisees are “the healthy pool people”⁵ and that we are accredited experts. To maintain this reputation, franchisees need to be able to competitively offer goods and services that have been carefully considered to be the most suitable for the customer’s technical requirements, circumstances and desires. Under the proposed arrangement I will not be able to offer the most suitable product, only the most

⁴ Waterco Notification N93741

⁵ Poolwerx Marketing slogan

suitable product from a severely limited range. It is certainly not clear at all that there would be any real benefit to consumers in terms of price. For example if a client has a pump that needs replacing instead of being able to offer a replacement that can be easily fitted to the existing plumbing, franchisees would have to offer replacement models of only one brand of pump that may require alterations of the existing pipe work to install and would need to charge the consumer additional costs to perform the alterations. The proposed arrangements would also have the effect of making spare parts more expensive to obtain. Whilst suppliers offer some spare parts, franchisees frequently need to source parts and goods that are not available from nominated suppliers. In these frequent instances it is hard to obtain a competitive price and also to justify the time needed, the costs involved in sourcing an alternative supplier, to apply for written approval from Poolwerx and often there are more onerous credit terms to adhere to. Under the proposed arrangements, franchisees will find it much harder to compete for repair work and will need to turn down some of this work or pass on the higher cost to the consumer.

Poolwerx asserts the proposed arrangement will help to:

“reduce the time and costs that would otherwise need to be incurred by franchisees in monitoring the quality of the relevant products and the suppliers;”

Franchisees will still need to monitor the quality of the products and could have increases in time and costs where suppliers cut back on technical and sales support to recoup the costs of the rebates paid to the franchisor.

Poolwerx states that the proposed arrangement will:

“promote consistency between PoolWerx franchised stores and businesses,” and “ensure PoolWerx can effectively monitor and control the quality of products used or sold by franchisees so that the reputation and the value of the PoolWerx brand is maintained;”

I would argue that consistency between franchised businesses is of little benefit to the consumer in this type of franchise. Franchisees are not combining or processing goods to achieve a consistent end product that they then sell to customers. Instead franchisees provide excellence in service and expert technical advice and I maintain that it is this that needs to remain consistent to preserve the value of the franchise system, rather than the brand of goods sold. Customers do not engage in business with the franchisee simply because the franchisee offers quality goods, they do so because they want the quality goods that are suitable for their specific needs and appropriate to the unique technical requirements of a healthy functioning swimming pool. The Poolwerx network is renowned for its expert advice and any supplier arrangements should help franchisees maintain that reputation. The quality of the goods is of course important to the consumer but of more importance is the appropriateness of those high quality goods for their needs. This is especially the case in the mobile business environment as opposed to the retail environment.

Discussion of Public Detriment

I submit that there will be detriments to the public resulting or likely to result from the Notification, in particular the possible effects of the notification on the price of goods or services to the consumer and the possible effects on the choices available to consumers in obtaining the most suitable products for their needs.

I am very concerned that there are insufficient procedures and no incentives in place to ensure that suppliers do not increase the price of goods to franchisees and therefore to the consumer to recoup the costs of rebates paid to the franchisor. This effect is particularly acute where only one supplier per type of good or service is nominated. There is no incentive for a sole supplier of a product or service to compete for the franchisees business that would help drive prices down nor is there an incentive to maintain proper levels of service and support. The proposed arrangement may limit the choice in product available to consumers for this reason also.

Franchisees in the course of their business often need to provide customers, especially their real estate and commercial customers, with several different quotes for a product or service. For example if the pump needs replacing the customer may want a quote containing options for different pumps. Under the proposed arrangement, franchisees will only have one choice of supplier and there may only be one or two pump models suitable for the customer's requirements available from that supplier. Franchisees will need to obtain written approval from Poolwerx for any alternative suppliers they may wish to quote for. The prices quoted for products from these alternative suppliers will inevitably not be as competitive and franchisees' will need to reflect this in their quotes to the customer. Franchisees will also need to obtain approval for all products quoted even though the customer ultimately will only choose one of them. This is a lot of unnecessary work and cost for the franchisee. The time involved will mean franchisees will not be able to provide quotes in a timely fashion which will further erode their ability to compete with other businesses.

Franchisees undergo extensive training in the technical and OH&S aspects of their business. The proposed arrangements will make it harder for franchisees to gain sufficient training and expertise in products other than the approved products. This is a detriment to the public as it will reduce the ability of franchisees to properly care for and maintain any alternative products the customer may have and reduces the technical skills of the network leading to reduced quality of service.

Part Two: Discussion of Poolwerx response to ACCC request for more information:

ACCC asks:

- 1. Please provide full details of the rebates received or proposed to be received by Poolwerx from each approved supplier.**
- 2. Does PoolWerx provide information to franchisees about rebates received beyond the acknowledgement in clause 11 of its franchise agreement? Specifically, are franchisees informed of the level of rebates received by PoolWerx in relation to specific products franchisees are required to purchase from approved suppliers**

Poolwerx's response to question 1 contains contradictory statements about disclosure to the statements given about disclosure in the original notification.

Of particular concern is the statement "*the majority of rebates are remitted to the marketing fund*". This is a quantitative statement that franchisees and the ACCC cannot evaluate for correctness until the actual percentage of rebate that goes to the marketing fund and the percentage that is remitted to other non marketing funds is established. I would argue that even though the franchising code does not specifically require disclosure of the amount of rebate, the use of the word *majority* cannot be substantiated as true or false by franchisees. I contend that the full details of the rebate system have not been provided to the ACCC or to franchisees and that this information is vital to examining any proposed public benefit.

Some franchisees may have the words "majority of rebates" written into their franchise agreement contracts, if the franchisor continues to refuse requests for the full details of the rebates, franchisees are not in a position to evaluate if Poolwerx is fulfilling its contractual obligations.

3. PoolWerx has provided details of the range of factors it has regard to in selecting approved suppliers. Please provide further details of the process by which approved suppliers are selected. For example, does PoolWerx identify and approach suppliers it considers may be appropriate, and are opportunities to become an approved supplier made known to a range of potential suppliers such as through a tender process?

The supplier selection process is not shared with franchisees and franchisees are unaware of the criteria and methods used.

4. Please advise how the level of rebates payable by suppliers is determined. For example, are higher levels of rebates paid where a supplier is appointed as the exclusive supplier of a good or service?

I am unable to comment on this as the level of rebates and the determination process is not made known to the franchisees. I am concerned that where there is only one supplier for each type of product that the rebates are highest and that this will inevitably see suppliers attempt to recoup the costs by increased prices to franchisees as there is no alternative supplier of the product to compete for franchisees business.

5. I note that approved suppliers could potentially increase the price of relevant products to PoolWerx franchisees to recover, in part or full, the cost of the rebate. Does PoolWerx have a view on the effect of requiring approved suppliers to pay a rebate to PoolWerx on the cost at which relevant products are supplied to franchisees?

There is great concern within the network that *best buy prices* are not thoroughly and actively pursued. Franchisees can often give examples where they believe they are not getting best buy price. The franchisor's response to queries about pricing is always that the franchisee must obtain written proof that a competitor derives a greater discount or receives a better price than the network. The proof required is an invoice from a supplier to a competitor. Competitors typically need to keep their buy price confidential and so this proof is tremendously hard to obtain. It is unknown how many franchisees have been able to obtain such proof in the past and it is also unknown whether any action was taken

by Poolwerx or the outcomes of any such action. This response clearly puts the onus of *best buy price* back on the franchisees to monitor and maintain.

Poolwerx states that it requires at least one month's notice of any price increases yet no obligation exists for either the supplier or the franchisor to also give franchisees one month notice of price increases. A few months ago, Poolwerx passed on a price increase to franchisees with less than one month's notice. This caused financial losses to be incurred to franchisees that then had to renegotiate contracts with their customers. The price increases covered the entire range of chemical products. Poolwerx franchisees were also misled by the franchisor into believing that prices were fixed for 12 months. This turned out not to be the case and this arrangement saw franchisees picking up the costs unexpectedly for increased prices from suppliers who were heavily affected by the value of the Australian dollar. This occurred in the middle of a franchisees busiest season and was an inconvenience to franchisees and their customers.

It is my view that this process is completely inadequate at maintaining *best buy price* and the lack of alternative suppliers for many core products further compounds the likelihood of skimming by suppliers to recoup rebate costs.

6. PoolWerx states that it reviews all approved supply arrangements on a national basis quarterly and on a state basis monthly. Please advise whether the price at which products are supplied to franchisees, compared, for example, to the prices available for equivalent products from alternative suppliers, is considered as part of these reviews.

Franchisees are not privy to the agenda or meeting minutes of these reviews. Again the onus is upon franchisees to monitor best buy price. The clauses in supplier contracts relating to price maintenance are vague at best.⁶

7. " Please confirm whether the vehicle requirement will apply to existing franchisees that must use a vehicle in connection with their franchise business, when they renew their agreement. If the vehicle requirement does apply to existing franchisees renewing their agreements....."

There would be other franchisees in a better position to comment on how Poolwerx enforces vehicle requirements. However, I am concerned that even though I have a vehicle that is three years old and complies with the extensive requirements for sign writing, that I will not be able to sell my vehicle as a going concern to the purchaser of my franchise should I sell my franchise before the 5 year term expires.

Part Three: Discussion regarding previous ACCC decisions regarding third line forcing:

I note that in the ACCC final notice revoking third line forcing notification from the seal a fridge franchisor⁷ the ACCC makes the following comments with regards to factors taken into consideration:

⁶ Pro forma Supplier Contracts supplied by Poolwerx.

⁷ Seal A Fridge Pty Ltd and Ors, Final Notice revoking third line forcing notifications N50197, N50198, N50199 and N92676 lodged by the Seal-A-Fridge franchisors.

6.10 “One indication of the benefits of exclusive dealing in franchise supply arrangements, particularly the franchise reputation and price benefits outlined above, is the level of franchisee support for the arrangements. If the arrangements genuinely deliver costs savings to franchisees or improve the reputation of the franchise, it could be expected that a large proportion of franchisees would support the arrangements. Conversely, where a large proportion of franchisees object to the notified conduct, it may be that the cost savings or benefits of improved reputation are illusory or insufficient to outweigh the costs associated with exclusive dealing conduct. competitively priced equivalents may be purchased”

For this reason I urge the ACCC to invite comments and submissions from all franchisees in order to satisfy themselves of the answer to the above consideration .

Furthermore, the ACCC states:

6.13 Any reduction in competition from exclusive dealing in a franchise context will be more limited where:

nominated suppliers are chosen through competitive means, for example through a tender process

**the franchise supply arrangements are reviewed regularly
franchisors demonstrate an ongoing interest in maintaining the efficiency of franchisees and therefore an interest in ensuring nominated suppliers deliver value for money**

franchisees may select from multiple suppliers, which allows for ongoing competitive tension between the suppliers and increases the likelihood of individual franchisee preferences being catered for

mechanisms are provided to allow exceptions to the rule, for example competitively priced equivalents may be purchased

the products the subject of the restriction are a small proportion of the franchisees overall costs

franchisees comprise a small proportion of the market or markets in which they compete.

6.14 The manner in which franchisors implement supply restrictions will also be relevant to ACCC assessment of the arrangements. Restrictions should be consistent with franchise agreements and should be implemented with a high degree of transparency. Franchisees should be aware of the nature of the restrictions before entering into the franchise agreements (or treated fairly should the restrictions be later introduced), and restrictions should not be imposed or introduced in an unfair or unconscionable manner.

I contend that the franchisor does not demonstrate an ongoing interest, that in most cases and for most core products, that the franchisee does not have multiple suppliers to select from, the mechanisms provided to allow exceptions to the rule are onerous and impractical where requests for written approval of alternative suppliers in the past has not

been forthcoming and that the products subject to restriction comprise nearly 100% of a franchisees overall costs.

This final notice also states:

6.6 The ACCC notes there are also a variety of ways to maintain consistency and quality. For example, minimum quality standards can be set. Alternatively, where there are multiple suppliers of a suitable product, franchisees may be provided with a selection of suppliers from whom they can acquire goods.

And:

6.8 However, franchisors should explain why similar benefits cannot be delivered through negotiating supply on the basis of voluntary supply agreements with individual franchisees. Franchisors may also be able to negotiate preferred

I contend that there are alternative methods to maintain consistency and quality as there are many other suppliers who could be approved who offer equivalent quality products. I also contend that similar benefits could be obtained on the basis of voluntary agreements with individual franchisees.

I submit that the manner in which the franchisor is attempting to implement the restrictions needs further investigation by ACCC. Franchisees for the most part are completely unaware of Poolwerx notification. There has been no consultation with franchisees, the process is not transparent and there is much confusion over which franchisees it will apply to as well as concerns over whether the rebate system was properly disclosed to franchisees.

Summary

In summary, it seems clear that the ACCC, if it is to be consistent with previous decisions, it must investigate further the claims of the franchisor and the evidence and opinions from franchisees in order to accurately evaluate the public benefit and detriment of the proposed third line forcing conduct.