



The Office of the
Group Chief Executive

28th August 2008

The Secretary
Parliamentary Joint Committee on Corporations and Financial Services
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Secretary

The Motor Trades Association Queensland (MTA Queensland) responds to the Parliamentary Joint Committee on Corporations and Financial Services' (the Committee) invitation for submissions to the *Inquiry into the Franchising Code of Conduct* and related matters. Our submission is attached.

Please contact me if there are issues to discuss associated with our submission. We would be available to attend should the Committee decided to schedule Hearings in relation to this matter.

Yours sincerely

Aivars Blums
GROUP CHIEF EXECUTIVE

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Summary and Recommendations

MTA Queensland is the peak organisation in the State representing the specific interests of 2,500 businesses in the retail, repair and service sector of the Australian automotive industry. Our comments are confined to issues that have direct relevancy to our membership in the automotive trade's value chain.

MTA Queensland is of the view that for the Franchising Code of Conduct (the Code) to be effective across the automotive value chain, the Code should recognise and have the ability to deal effectively with disparate range of arrangements:

- franchises involving large transactions such as motor vehicles; and
- franchises involved in a large number of modest transactions such as fuel retailing.

It is MTA Queensland's view that there are three seminal issues that should be addressed by the Joint Parliamentary Committee on Corporation and Financial Services. They are: exit arrangements; unilateral renegotiation of franchise fees or benefits; and renewal.

The Code is prescriptive in terms of the entry agreement/arrangement but is deficient in prescribing the termination of these instruments. Exit arrangements must now be the focus as there are many instances of unfairness or perceived unfairness in relation to goodwill. It is our view that entry arrangements and exit arrangements are of equal importance.

An issue of concern is the need to delete from agreements subject to the Code the provisions for either the franchisor or franchisee to unilaterally renegotiate the franchise fees or benefits of an agreement. It is MTA Queensland's experience that this is a matter requiring attention.

It is highly desirable that the Code require an enunciation of the basis for any renewal of the franchise. Renewal should be defined in the initial agreement so that both parties are clearly aware of renewal arrangements. Even if there are no provisions for renewal these should be stated rather than the agreement relying on "silence".

Recommendations

1. The Code should be effective and relevant to the automotive value chain and should recognise and have the ability to deal with disparate arrangements:
 - franchises involving large transactions such as motor vehicles; and
 - franchises involved in a large number of modest transactions such as fuel retailing.
2. The three major areas the Joint Parliamentary Committee should consider for improving the competence of the Code include:
 - Exit arrangements;
 - Unilateral renegotiation of franchise fees or benefits during the term of the agreement (gouging); and
 - Renewal.

MTA Queensland Submission
Parliamentary Joint Committee on Corporation and Financial Services' Inquiry into the Franchising Code of Conduct

1. Introduction

- 1.1 The Motor Trades Association of Queensland (MTA Queensland) responds to the Parliamentary Joint Committee on Corporation and Financial Services' *Inquiry into the Franchising Code of Conduct*.
- 1.2 We note the Terms of Reference to which comment is sought. Our responses reflect our membership in the automotive value chain and are stated below.

2. Motor Trades Association Queensland background

- 2.1 MTA Queensland is the peak organisation in the State representing the specific interests of 2,500 businesses in the retail, repair and service sector of the Australian automotive industry. It is an industrial association of employers incorporated pursuant to the Industrial Relations Act of Queensland.
- 2.2 The Association represents and promotes the issues of the automotive industries to all levels of government and within Queensland's economic structure.
- 2.3 MTA Queensland comprises 14 separate divisions, each representative of a specialist area of the State's automotive industry. They are –
- **Australian Automotive Dealers' Association of Queensland;**
 - **Queensland Farm and Industrial Machinery Dealers' Division;**
 - **Auto Electrical Specialists' Division;**
 - **Queensland Motorcycle Industry Division;**
 - **Automotive Engineers' Division;**
 - **Queensland Tyre Dealers' & Retreaders' Division;**
 - **Engine Re-conditioners' Association of Queensland;**
 - **Rental Vehicle Industry Division;**
 - **Independent Tow Truck Operators;**
 - **Service Station & Convenience Store Association of Queensland;**
 - **National Auto Collision Alliance;**
 - **Used Car Division;**
 - **Automotive Under Car Division; and**
 - **Auto Parts Recyclers' Association of Queensland.**
- 2.4 The Association is the leading automotive training organisation in Queensland offering nationally recognised training covering all aspects of the retail motor trades industry. The Association's Motor Industry Training entity is the largest automotive apprentice trainer in Queensland and has trainers positioned in Papua New Guinea and Fiji to

increase knowledge and skills base of the automotive industry and career opportunities in these countries.

- 2.5 In Queensland, the automotive trade's value chain generates in excess of an estimated \$16 billion annually, directly employing more than 60,000 people contributing significantly to both Queensland's and the nation's economy. According to the Australian Bureau of Statistics the automotive trade sector in Queensland employs more than Mining and Agriculture, Forestry and Fishing sectors - respectively 34,300 and 40,700.

3. MTA Queensland's perspective

- 3.1 Our comments are confined to issues that have direct relevancy to our membership in the automotive trade's value chain which have business models based on franchise arrangements which include an estimated:

79	Tyre Franchisees;
26	Mechanical Franchisees;
50	Farm Machinery Franchisees;
74	Motorcycle Franchisees;
12	Brake and Undercar Franchisees;
15	Rental Franchisees;
252	Service Station and Convenience Store Association of Queensland Franchisees; and
274	Australian Automobile Dealers' Association of Queensland Franchisees.

- 3.2 The Franchising Code of Conduct (the Code) has been undergoing an evolution and if some specific aspects of the Code are attended, it could become an important generic regulator that would have the competency and capacity to replace industry specific regulation such as the Oilcode.

- 3.3 We are of the view that for the Code to be effective across the automotive value chain; the Code should recognise and have the ability to deal with disparate arrangements:

- franchises involving large transactions such as motor vehicles; and
- franchises involved in a large number of modest transactions such as fuel retailing.

- 3.4 There are three major areas the Joint Parliamentary Committee (the Committee) could consider to improve the competence of the Code. They are:

- 3.4.1 Exit arrangements;
- 3.4.2 Unilateral renegotiation of franchise fees or benefits; and
- 3.4.3 Renewal.

- 3.4.2 MTA Queensland is of the view that the above issues are priorities to improve franchisee risk management. These important issues should receive attention from the

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Committee to allow franchisees to assess the level of commercial exposure that they should take into consideration when they are evaluating a business model.

- 3.4.3 In considering the Code, it is important that the Committee does not impose any regulations that are likely to fetter or limit the scope of normal commercial negotiation between parties and limit the level of normal competition that should occur in the marketplace.
- 3.4.4 There should be scope in franchise arrangements for proper and competitive commercially negotiated arrangements. If the Code begins to fetter competition then there will be distorted or sub-optimal outcomes for the economy and the consumers.
- 3.4.5 MTA Queensland recognises that franchisees need to make rational decisions, inform themselves and should use their commercial judgment in negotiating franchise agreements. If they need expert advice they should obtain it. The Code cannot substitute for these responsibilities.

4. The Submission

- 4.1 Exit arrangements:
 - 4.1.1 It is MTA Queensland's experience and view that more emphasis must be on franchisee exit arrangements. Termination arrangements for on-selling of a franchise business, its transmittal and the terms it can proceed should include goodwill and a clear statement of beneficiaries and benefits.
 - 4.1.2 The Code is prescriptive in terms of entry requirements and disclosures but is deficient on the basis of termination when a term expires. Exit arrangements must now be the focus and included in the Code as there are many instances of unfairness in relation to goodwill. It is our view that entry arrangements and exit arrangements are of equal importance.
 - 4.1.3 The problem manifests when the other party terminates before or after the agreement. The franchisor secures the goodwill leaving the franchisee with the risk and disposal of stock, pumps, computers etc.
 - 4.1.4 The lack of recognition of goodwill seriously disadvantages the small franchisee in the instance of a large supplier. The franchisee exits with little reward for efficient business operation; his skill set in achieving high benchmarks is of negligible value when the arrangement is terminated. The stance of the franchisor (large supplier) is that the goodwill derives from the branding of the product and not by the franchisee's promotions, reputation and service etc.
 - 4.1.5 It would appear that the Code requires the ability and the authority to reinforce a prescriptive situation for exit or termination even if there is a clear declaration that goodwill is non applicable or non existent or the franchisee's proportion of

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an appropriation is zero. Silence on this issue is most often the cause of disputation.

- 4.1.6 The deficiency of the Code should be remedied and be amended to include termination arrangements. Statutory protection should be available to the franchisee at the conclusion of the franchise to prevent unconscionable conduct and use of market power for an unfair termination by the franchisor/supplier.
- 4.1.7 The rights and obligations of the franchisor and the franchisee concerning exit/termination arrangements should be included in the Code and the *Trade Practices Act*.
- 4.1.8 Anecdotally, many franchisees are changing from franchise arrangements to commission agent arrangements where the Code does not apply. Anecdotally the provisions of the Code are too broad "and no real benefit because at the end of the day the relationship is managed by the supplier"¹.

4.2 Unilateral renegotiation of franchise fees or benefits (gouging)

- 4.2.1 The expunging from agreements subject to the Code the right of either the franchisor or franchisee to unilaterally renegotiate the franchise fees or benefits of an agreement² requires attention.
- 4.2.2 This is an all too common provision which is activated when a franchisee outperforms its business model and an opportunity for "gouging" occurs.

4.3 Renewal.

- 4.3.1 It would be highly desirable that the Code require an enunciation of the basis for renewal of the franchise. It should be defined in the initial agreement so that both parties are aware of renewal arrangements. For example: what are the conditions on which the franchise business will be renewed? Will the franchisor have to pay for goodwill as an entry fee for the next period or not?

¹ For example: A big oil fuel company owned a service station site on the Gold Coast which was leased to a franchisee. Competing big oil outlets were nearby. The franchisee built up the business through upgrades, competitive prices, good service, pleasant outlook, food and other items. It became very popular. Customers queued for service. The franchisee was advised that the big oil company would not renew the franchise arrangement but would operate it. There was no recognition of goodwill which includes taking the business from marginal to highly profitable with high customer satisfaction. Another example may be in the instance of an automotive manufacturer unilaterally terminating franchisee / dealerships

² Unilateral renegotiation is becoming more common. For example a Service Station was achieving high profitability. The franchisor unilaterally midway through the agreement changed fees (gouging) on the basis that fuel sales were high AND the take from the shop was included. The fear for small operators is that if they resist the increased fees it may influence renewal.

- 4.3.2 Renewal is a vexed issue and one that worries many franchisees. Some hold the opinion they have the right to a renewal although it is not included in the agreement. It is obvious if the agreement/document is silent on the right to renewal then it should be clear that renewal will have to be earned by performance. If it is a conditional right of renewal, the conditions to satisfy the right for renewal should be stipulated in clear terms and agreed between the parties.

5 Other Matters

5.1 Fair Contracts

- 5.1.1 Recently, the Ministerial Council on Consumer Affairs agreed that all Australian governments should adopt a new national consumer law which will operate in all Australian jurisdictions based on the current protection provision of the *Trade Practices Act* and where appropriate best practice in state and territory legislation. The MTA Queensland has been and is a strong public supporter of a single, national consumer law.
- 5.1.2 The MTA Queensland is of the view that Fair Contracts should be an important component of the Consumer Protection Framework and be included in new national fair contract law and be enunciated in amendments to the *Trade Practices Act*.
- 5.1.3 Fair Contracts should indicate a need for a clear statement that sets out where the franchise business relationship should be at a designated time, key performance indicators that include realistic and attainable customer satisfaction indicators (CSIs). There should be regular CSI reviews which can be adjusted by mutual consent.

6 Conclusion

- 6.1 MTA Queensland is of the view that the three seminal issues that should be included in the Committee's consideration are – exit arrangements; unilateral renegotiation of franchise fees or benefits; and renewal. These issues should be addressed to provide confidence, predictability and risk management appropriate to franchising across the automotive value chain.
- 6.2 MTA Queensland recognises that the nature of the franchising industry in some areas of the automotive value chain is changing. The strengthening of the Code has meant that in some business areas, franchising arrangements are being replaced by commission arrangements as they provide better commercial outcomes. On the other hand some suppliers are stepping outside the Code to either evade or avoid obligations and are becoming vertically integrated.

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