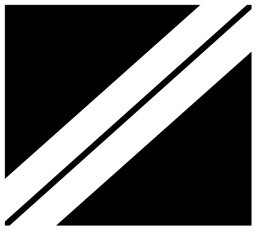

Motor Trades Association of Australia

Submission to the

Department of Resources, Energy and Tourism

Review of the Oilcode

April 2008

OILCODE REVIEW SUBMISSION

1. INTRODUCTION

This submission to the Commonwealth Department of Resources, Energy and Tourism for its review of the *Trades Practices (Industry Codes – Oilcode) Regulations* 2006 has been prepared by the Motor Trades Association of Australia (MTAA). MTAA is the peak national representative organisation for the retail, service and repair sector of the Australian automotive industry. The Association is a federation of the various state and territory motor trades associations and automobile chambers of commerce, as well as the New South Wales based Service Station Association Ltd (SSA) and the Australian Automobile Dealers Association.
Members of the MTAA Federation include:

- the Australian Automobile Dealers Association (AADA)
- the Motor Trades Association of the ACT (MTA ACT)
- the Motor Traders Association of NSW (MTA NSW)
- the Motor Trades Association of the Northern Territory (MTA NT)
- the Motor Trade Association of South Australia (MTA SA)
- the Motor Trade Association of Western Australia (MTA WA)
- the Service Station Association Limited (SSA Ltd)

MTAA also has a number of Affiliated Trade Associations (ATAs), which represent particular subsectors of the retail motor trades, ranging from motor vehicle body repair to automotive parts recycling and relevantly, for this review, the Australian Service Station and Convenience Store Association (ASSCSA). MTAA represents the interests, at the national level, of over 100,000 retail motor trade businesses with a combined turnover of over $120 billion and which employ over 316,000 people. The vast majority of businesses represented by MTAA employ five or less people.

The Motor Trades Association of Australia (MTAA) has centrally then, been a major stakeholder in the development of downstream petroleum sector policy. However, while MTAA did support reform of the regulatory arrangements for the petroleum sector, it did not believe that the Oilcode, as it is currently written, could effectively address the public and competitive interest secured by the two petroleum Acts (the *Petroleum Retail Marketing Franchise Act* (Cth) *1980* and *Petroleum Retail Marketing Sites Act* (Cth) *1980*) which it was claimed it could properly, necessarily and sufficiently secure. The Association, therefore, has had an ongoing interest in Oilcode's operation following its commencement and has a particular interest in this Review.

This Submission is informed by the Association's extensive insight and understanding of how Oilcode has operated in the market and by the experiences and reports of our many service station operators themselves. As such, this Submission must be considered to represent an accurate assessment and illustration of the practical, 'on the forecourt' operation of Oilcode.

It is necessary for MTAA to advise that is has numerous concerns over the Oilcode, many of which it may have even foreshadowed at the time of Oilcode's negotiation and drafting in its development. These concerns are over a number of matters, which can be summarised as

being the issues of: tenure, disclosure, dispute resolution, Terminal Gate Pricing (TGP) and contractual terms.

This Submission discusses these issues of concern to MTAA in a relatively broad manner. There are a number of reasons for that and they are mostly attributable to the sensitivities that exist around matters of confidence, proximity to events themselves and – significantly – the nature of the market power relationship existing between fuel retailers and their refiner-marketer suppliers.

2. TENURE

MTAA strongly believes that the Oilcode must provide for a minimum tenure period for service station operators. That tenure period needs to be consistent across all types of retail operation irrespective of a fuel retailer's relationship with its supplier (for example, as being either a franchisee or a commission agent), or the financial consideration involved. MTAA believes that the character of that relationship determines some fundamental 'rights' of the retailer in question. Principal among those is, arguably, a right to occupy the site.

Any small business – particularly in today's competitive economic environment – represents a substantial investment by its proprietor. The business operator will also have a number of imperatives to consider, such as maintaining commitments (on a number of levels) to staff, to suppliers and to any financiers. As such, small business' need a reasonable opportunity to both meet those commitments and to recoup its often not inconsiderable investment.

In the retail petroleum sector, franchisees, commission agents, lessees and independents (where leasing from third parties), cannot be classified as anything other than small businesses and, therefore, are entitled to the same opportunities as business operators in other sectors. Section 13 of the (repealed) *Petroleum Retail Marketing Franchise Act* (Cth) *1980* (PRMF Act) offered some security of tenure for fuel retailers through prescribing fuel reseller agreement terms. Oilcode, while also offering some specifics in that regard, nevertheless contains qualifiers and other conditions, which a supplier may use to its advantage. As such, under Oilcode, no real certainty in terms of security of tenure exists for site operators (excluding, unavoidably, any reasons applicable under Division 4 of Oilcode). In MTAA's view clause 32 (11) (c) of Oilcode provides a 'loophole' that is currently being manipulated or exploited by supplier / franchisors on some occasions and which is effectively eroding the minimum tenure period that was promised to service station operators during the development of, and by, the Code.

Under that clause, some oil companies/suppliers are avoiding offering tenure by charging an upfront fee of less than $20,000.00 and thus avoiding having to offer a minimum tenure period to their resellers. This creates a scenario whereby a reseller – whose existing agreement may have recently ended, but who may have reasonably anticipated a renewal of that agreement in similar terms – may find themselves effectively operating on a month-by-month tenure basis. In that scenario, there is also no requirement placed upon the supplier / franchisor under Oilcode to provide any guarantee of its intention to enter into any other form of arrangement. This could effectively place a reseller on '30 day's notice', and is effectively a tenure of 'termination at will' by the lessor/franchisor.

Additionally, this situation creates an artificial distinction between various resellers of the supplier: those with some security of tenure and those with little or no security of tenure. Given the characteristics of the cash flow required to operate a reseller site, the exemption threshold of $20,000.00 set by Oilcode is meaningless. Invariably the reseller will retain a number of avenues through which to construct arrangements between it and the lessee so as to achieve its financial objectives through the operation of the reseller site. Fundamentally, then, MTAA believes that in any circumstance where a supplier offers the right to occupy a site to an incoming reseller and where that right is conditional upon the buying and selling of the supplier's products (such as branding, lubricants as well as in some cases, petrol), then a minimum term of tenure needs to also be a condition of that occupation.

The Association **recommends**, therefore, that the clause in Oilcode relating to the $20,000.00 exemption threshold be removed and that this removal be done in the context of ensuring reasonable minimum terms of tenure for all resellers.

As another example, other companies, at the end of a lease period, are using 'hold over' provisions for one year and not offering a set-lease period; though the Code itself does not permit 'hold-overs'. In other circumstances, oil companies are requiring 'franchise fees' of up to $350,000.00 for a five year lease, even though such is commercially unsustainable.

In light of this sort of supplier behaviour, which has become increasingly prevalent in the market since Oilcode's commencement, the Association believes that Oilcode needs to be amended so as to ensure appropriate, reasonable and secure minimum tenure periods for resellers, irrespective of the nature of their relationship with their supplier.

The Association, again and still, **recommends**, therefore, that clause 32 (11) (c) of Oilcode, should be removed and that all suppliers should have to offer a minimum tenure period of five years, with a five year renewal option. For those that might object to that, there are already in the Code clauses which provide for a lesser period of tenure to be negotiated in certain circumstances. MTAA believes that those arrangements provide sufficient flexibility so as to not unfairly 'lock-in' either party to a specified tenure period where such an arrangement cannot be sustained.

3. DISCLOSURE

MTAA has a number of issues in connection with the disclosure provisions of Oilcode. In particular, the Association believes that the disclosure required to be given in the area of 'Materially Relevant Facts' (section 29 of Oilcode) falls short in terms of the level and nature of disclosure required by an intending, or continuing, fuel reseller, in order for it or they to make a sound and balanced business decision.

The Association believes that there should be, for a part at least, a requirement to disclose a supplier's history of disputation (as might have or has occurred under the dispute resolution framework of Oilcode). Presently, section 20 of Oilcode only compels suppliers to disclose materially relevant facts that are – in essence – more indicative of breaches of the *Corporations Act* (Cth) *2001* or Industrial Relations law rather than matters that are at the essence of the relationship.

While reference is also made within this section of Oilcode to contraventions of 'trade practices law' and 'unconscionable conduct' – concepts which have proven, in recent years, to be difficult, if not impossible, to establish at law before the courts – there nevertheless remains a 'disconnect' between a supplier's requirement to provide disclosure around matters of this nature and the outcomes and processes of Oilcode's dispute resolution mechanism. It appears, therefore, that suppliers technically have a need to only disclose matters of enormous significance; the impact of which being arguably greater upon aspects of their operations than it might be upon an existing or intending reseller and this is of little practical informative or judgemental value relative to the franchise.

Simultaneously, the contextualisation of 'materially relevant facts' in this manner and at that practical level within Oilcode helps to facilitate a regulatory 'blind spot' over the behaviour of some suppliers in the market place. It is these circumstances that also assist some suppliers in demonstrating to subjection, in some instances, the reach and effect of their market power when compared to the level of market power held by resellers when new, or continuing, reseller agreements are under negotiation. The level of disputation between a supplier and a reseller is often a better and more appropriate indicator of the business relationship than that provided by court proceedings.

The Association **recommends,** therefore, that the disclosure provisions of Oilcode be amended so as to make 'materially relevant facts' inclusive of a supplier's history of all relevant disputation (under the dispute mechanisms of Oilcode), and for disclosure of that nature needing to be ongoing. That is to say that any dispute under the dispute mechanisms of Oilcode needs to be a trigger for the updating of a supplier's disclosure documentation, which – as a 'materially relevant fact' – would then require the dissemination of those details among the supplier's reseller network. The Association believes that a requirement for disclosure of this level and extent would also encourage dispute resolution.

MTAA and its Members also **recommend** that the 'on-going' disclosure requirements on suppliers should include an obligation to disclose immediately any change in the supplier's business operating arrangements that could impact upon a reseller's opportunity to realise a return on its investment.

4. DISPUTES

Anecdotal, but reliable, reports from Association Members, taken in combination with its own observations, lead the Association to have some concerns regarding the model employed for the resolution of disputes between parties to a fuel reselling agreement under Oilcode. Under section 29 (6) of the Franchising Code of Conduct, parties to a dispute *must* attend mediation (if dispute mediation has been requested) and make efforts to resolve the dispute.

By contrast and contradiction, under Oilcode, no such compulsion is placed upon parties to a dispute to undergo mediation. It is, therefore, not binding on a supplier to participate in dispute resolution under Oilcode. It should be.

MTAA **recommends** that the Oilcode dispute resolution clauses be amended to require parties to attend mediation.

The Association is aware of one dispute where the mediation was attended by a supplier representative who clearly had no authority to make decisions on behalf of the supplier. This was tactically and deliberately done. This situation introduced unnecessary delay (and, therefore, cost) into the mediation process. MTAA believes, therefore, that mediation of disputes must require attendance by representatives of the parties involved who have the clear and declared authority to make decisions and commitments in and on the matter.

MTAA **recommends** that that result could be achieved if Oilcode were to be amended to include a clause similar to section 29 (7) of the Franchising Code of Conduct, which states:

> *For subclause (6), a party is taken to attend mediation if the party is represented at the mediation by a person who has the authority to enter an agreement to settle the dispute on behalf of the party.*

Presently, where a dispute has been mediated and a ruling of the Dispute Resolution Adviser on the dispute (on the advice of the Mediator) has been made, that ruling is not binding on the parties. Instead, the ruling is declared, by Oilcode, to be a 'non-binding determination'(section 45 (6)). It is MTAA's belief that a determination with this status places no enforceable requirement upon a party to a dispute, found to be 'at fault', to make any remedy.

When that is taken in connection with section 46 of Oilcode (or, at the very least, that section's import), it is MTAA's understanding that no element of an Oilcode dispute mediation – including a non-binding determination - may be admissible as evidence or, indeed, so much as submitted as persuasive, in the event of a dispute progressing beyond mediation and being placed before any assembly, tribunal or the courts. The Association believes, then, that the dispute resolution arrangements of Oilcode need to be reviewed with the objective of Oilcode incorporating procedures and rules that can impose binding, enforceable decisions on parties that are also judiciable before the courts.

MTAA **recommends**, therefore, that the dispute resolution arrangements of Oilcode be reviewed and for that review to be conducted in the comparative context of similar arrangements as might be found in other Codes, regulatory regimes or tribunals.

MTAA further **recommends** that the objective of this review needs to be the amendment of Oilcode's dispute resolution arrangements so as to create outcomes for dispute resolution under Oilcode that are binding, enforceable and admissible as evidence (and, thus, judicable) before the courts.

5. TERMINAL GATE PRICING (TGP)

It is worth noting the characteristics of the wholesale fuel supply sector in order to put TGP arrangements in some perspective. The sector is dominated by four main suppliers that are highly vertically integrated (in that they encompass operations from exploration through to retailing). The four major supplier/refiners also have a near exclusive possession among them

of any fuel storage and / or distribution facilities. They are described by the Chairman of the ACCC as having "established a comfortable oligopoly"[1].

MTAA believes that optimal benefits to society are derived from outcomes that encourage diversity in market competition and choice. A starting point to achieve those benefits is outcomes that support a freedom to compete in the market. This freedom would then support a diversity and choice for consumers (including resellers as consumers), which situation facilitates competition in the market. It is then the open, competitive market that delivers optimal benefits to society.

The Association believes that a transparent and competitive wholesale fuel market delivers the best outcomes for all participants involved in fuel reselling and, indeed, for consumers. Having a pretended regulatory structure on and for a Terminal Gate Pricing (TGP) is all well and good, but what if the vast majority of reseller purchases are not made at TGP? Nor does posting a TGP ensure, or indeed require, that any sales actually occur at TGP. Additionally, how does the regulatory structure around TGP pricing countenance the 'offset' of any rebates, that might subsequently be paid to a reseller, in the event that the reseller does purchase at TGP? What then does TGP mean or do? That is to say, TGPs are rarely an accurate reflection or representation of wholesale buying price.

While not wishing suppliers to betray any commercially confidential information, true transparency around wholesale pricing arrangements will only be realised when there is a degree of transparency around the discount structure suppliers apply. Oilcode places a requirement upon suppliers to declare and advertise their TGPs, but at the same time imposes no requirement upon suppliers to declare and advertise any aspects of their actual wholesale pricing structure or to sell at it.

Nor does Oilcode contain any provisions to ensure a prohibition on predatory below-cost selling. This aspect, when considered in connection with the relatively untested section 46 (1AA) of the TPA, suggests the possibility for, any or a major, supplier to structure its own retailing in such a manner as to place it or they at a considerable advantage within the retail fuel sales sector of the market.

The Association believes, therefore, that a terminal gate price should be mandated as a feature and requirement of a transparent wholesale price regime for all sales from refineries or terminals. Any other add-on costs such as freight and/or double handling should be a separate commercial arrangement, but transparent, known and available to all. The Association also believes there is no place in the market for rebates or hidden discounts after the event; selectively offered and enjoyed secretly. Any volume discounts available need to be based on actual (published) volumes being attained and need also to be open, or accessible, to audit. The objective of this proposition is to achieve competition at the wholesale level, and for any discounts to be transparent and available to all in the market. The Association also believes that Oilcode needs to be amended so as to prohibit the practice of sustained below-cost selling in the wholesale supplier sector of the market as per the new provision of the Trade Practices Act.

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[1] Petrol Prices and Australian Consumers: Report of the ACCC Inquiry into the price of unleaded petrol. December 2007; page v

The issue of temperature correction pricing (the so-called 'L15 price') also needs to be considered by the Review in this context. Regulations in each jurisdiction require that wholesale sales of fuel to resellers by delivery direct from a 'primary storage facility' must indicate on the invoice to the reseller, an ambient volume and a L15 (temperature corrected) volume and price. The reseller is entitled to take receipt of the product at the L15 price. Certain oil companies, through their own internal information technology (IT) systems, block this practice and the reseller is then forced to enter into the site system only the ambient volume. This is totally against the spirit of the Oilcode and L15 pricing and statute and practice.

MTAA proposes that L15 must need then to be mandated as the receipted volume, not the ambient volume that oil company IT systems allow.

The Association **recommends** that arrangements need to be put into Oilcode to ensure that transparency and competition occur at the wholesale level of the market. The current terminal gate pricing arrangements do not deliver a transparent and competitive wholesale market.

The Association also **recommends** that any rebates or discounts available after the event of a wholesale purchase be made known to all. MTAA also **recommends** that any volume discounts available need to be based on actual (published) volumes being attained and need also to be open, or accessible, to audit.

The Association also **recommends** that L15 needs to be mandated as the receipted volume across the supplier / reseller system.

6. CONTRACTUAL TERMS

It is worth the review of everything associated with Oilcode's history to recall that the adoption of the Oilcode was also intended to be accompanied thus by necessary amendment to the *Trade Practices Act* (Cth) *1974* (TPA). The purpose of this fact was to ensure that those 'protective-of-resellers' provisions contained within the Acts to be repealed would find some substantive form and effect within the TPA. While there have been a number of amendments made to the TPA since the commencement of Oilcode, there have been none made that parallel and substitute for the protective mechanisms that were specifically afforded to resellers under the now repealed Acts. It is an anodyne comment to make that Oilcode pretends to make an effort to outline elements of procedural fairness when a supplier / reseller agreement is being negotiated. More though true is a comment that Oilcode does little to deal with the elements of substantive fairness in the nature of the relationship for the duration of a supplier / reseller agreement.

By way of demonstration there can not be found any comparison in Oilcode to either section 20 or section 17 of the former PRMF Act. Under the provisions of that Act, suppliers could not engage in, or demonstrate, any discrimination between franchisees with respect to discounts, allowances, pricing, rebates, credits, royalties and so on. Nor could a supplier arbitrarily – and in an opportunistic manner – use the event of an agreement renewal to significantly vary the terms of that agreement to the supplier's distinct favour. That necessary and valuable power and authority is lost.

For instance, section 17 (3) of the PRMF Act prescribed the procedure relating to renewal (or non-renewal) with regard to a proposal as *not* having been made in accordance with the relevant section of the Act if:

> (a) An amount payable by the franchisee under the franchise agreement as proposed to be renewed (other than an amount payable in respect of motor fuel or other stock and trade) would be, or would be calculated or determined in such a manner as to be, unreasonable, having regard to the market value of any interest, goods or services to which the amount relates

Similarly, section 20 (1) of the PRMF Act required that:

> A corporation that is a franchisor in relation to two or more franchise agreements shall not, in relation to motor fuel supplied or to be supplied under those agreements (whether by it or another person), cause or permit any discrimination between the persons who are franchisees in respect of:
>
> (a) the amounts payable by the franchisees in respect of the fuel, or
> (b) any discounts, allowances, rebates or credits given or allowed to the franchisee in respect of the fuel.

In the absence of specific amendments to 51AC of the TPA to deliver stronger protections from 'unconscionable conduct', or the adoption of an 'unfair business-to-business contract regime', MTAA remains concerned that the absence in Oilcode of clauses such as those sections of the repealed Acts will further reinforce the imbalanced nature of the power relationship existing between suppliers and resellers in favour of suppliers. For example, the Association has received anecdotal, but reliable, reports of suppliers exerting 'influence' through the employment of a number of strategies – all available to them under existing Oilcode provisions – to effectively change the nature and structure of reselling agreements while those agreements remain effective and on foot.

MTAA is aware, for instance, of an agreement renewal negotiation currently underway where the reseller is being asked to pay a substantial up-front franchise fee, and a fuel surety (which is greater than the value of a tanker load of fuel), yet the reseller is consistently owed each month substantial funds by the supplier in the form of supplier rebates.

The 'starting point' for these negotiations represents a significant departure from the reseller's current arrangements with its supplier and raise concerns for the reseller that its operations may be substantially impacted by any new agreement in favour of the supplier. Any detrimental destabilisation of his fuel reseller arrangements is understandably of great concern both to him and to MTAA.

MTAA **recommends**, therefore, the amendment of Oilcode in a manner to provide it with similar effect to the sections 17 and 20 operative then, of the repealed PRMF Act.

7. SUMMARY

Under the two now-repealed Acts it is fair to suggest that, while there existed tensions between suppliers and resellers, the power relationship between those parties remained in more appropriate economic and social balance than it is currently operative. Under those

Acts, suppliers needed to give some consideration of the broader interests of their franchisees and resellers. The establishment of Oilcode seems to the Association to have disturbed this balance and changed negatively the nature of the power relationship between suppliers and resellers in favour of the supplier.

MTAA finds it disturbing that since the promulgation of the Oilcode, the anecdotal, but reliable, reports it has received from its Members suggests to it that market conditions, and market price and power, have swung to a considerable extent in favour of the major Australian fuel suppliers. Certainly, some of these suppliers have been more 'advantaged' than others – or have positioned themselves to be so – and, as such, reports received by the Association of some behaviour in the market have been most disquieting. Equally, those reports are of circumstances most devastating to those resellers affected.

In conclusion therefore MTAA makes the following recommendations:

1. that the clause in Oilcode relating to the $20,000.00 exemption threshold be removed and that this removal be done in the context of ensuring reasonable minimum terms of tenure for all lessees;

2. that clause 32 (11) (c) of Oilcode, should be removed and that all suppliers should have to offer a minimum tenure period of five years, with a five year renewal option;

3. that the disclosure provisions of Oilcode be amended so as to make 'materially relevant facts' inclusive of a supplier's history of all relevant disputation (under the dispute mechanisms of Oilcode), and for disclosure of that nature needing to be ongoing;

4. that the 'on-going' disclosure requirements on suppliers should include an obligation to disclose immediately any change in the supplier's business operating arrangements that could impact upon a reseller's opportunity to realise a return on its investment;

5. that the Oilcode dispute resolution clauses be amended to require parties to attend mediation;

6. that Oilcode be amended to include a clause similar to section 29 (7) of the Franchising Code of Conduct, which states: *For subclause (6), a party is taken to attend mediation if the party is represented at the mediation by a person who has the authority to enter an agreement to settle the dispute on behalf of the party*;

7. that the dispute resolution arrangements of Oilcode be reviewed and for that review to be conducted in the comparative context of similar arrangements as might be found in other Codes, regulatory regimes or tribunals. MTAA further recommends that the objective of this review needs to be the amendment of Oilcode's dispute resolution arrangements so as to create outcomes for dispute resolution under Oilcode that are binding, enforceable and admissible as evidence (and, thus, judicible) before the courts;

8. that Oilcode needs to be amended so as to prohibit the practice of sustained below-cost selling in the wholesale supplier sector of the market as per the new provision of the Trade Practices Act;

9. that arrangements need to be put into Oilcode to ensure that transparency and competition occur at the wholesale level of the market. The current terminal gate pricing arrangements do not deliver a transparent and competitive wholesale market;

10. that any rebates or discounts available after the event of a reseller purchase be made known to all;

11. that any volume discounts available need to be based on actual (published) volumes being attained and need also to be open, or accessible, to audit;

12. that L15 needs to be mandated as the receipted volume across the supplier / reseller system, and;

13. the amendment of Oilcode in a manner to provide it with similar effect to the sections 17 and 20 operative then, of the repealed PRMF Act.

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4 April 2008