AUSTRALIAN MOTOR INDUSTRY FEDERATION

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Unfair Contract Terms Consultation Paper
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Thank you for the opportunity to provide a submission in relation to proposals to extend unfair contract term protections to small business. Given the ubiquity of various contractual arrangements within the many cleavages of the retail motor trades in Australia, the Australian Motor Industry Federation (AMIF) holds a particular interest in developments in this policy area.

AMIF is the pre-eminent body representing the interests of over 100,000 retail motor trades businesses, which businesses employ over 310,000 people and which have an aggregated annual turnover in excess of $208 billion. Those figures, combined with the industry's scope and size, make the retail motor trades the largest stand-alone small business sector in Australia. The Federation's membership consists of automobile chambers of commerce and the majority of state and territory motor trades associations.

AMIF's Position:

- Unfair contractual arrangements, while not exactly prolific, are reasonably easy to find operating within the retail motor trades. When found, that often exist as 'take it or leave it' propositions, upon which the ongoing viability of a retail motor trade operation may depend. For some traders, there is little alternative for them other than to cop the considerable bad that can come with a bare subsistence good.

- AMIF supports, in principle, proposals outlined in Option 3 of Treasury's Discussion Paper on this matter, which would see legislative amendment to extend the unfair contract term provisions to small business contracts.

- AMIF once again suggests to Treasury that there remains a need for careful consideration to be given to any attempts at defining the term, 'small business', as even larger retail motor trade businesses can, in relative power relationship terms, be substantially smaller than the entities with which they form contractual arrangements.

- AMIF suggests it far better for any 'definition' of 'small business' to be conceptually based, or expressed in terms of relative power relationship.

DISCUSSION:

It can be easy to regard the retail motor trades as one distinct bloc within the Australian economy. While to do so is acceptable on some levels, it is misleading to do so on others. Within the retail motor trades are some 36 discreet trade qualifications. While a good many issues affecting retail motor traders might be seen to apply uniformly, there can nevertheless exist patinas to issues that are specific to a particular trade. In some rarer instances, there can be policy issues specific to a trade within the broader retail motor trades. This 'pocket specificity' can make for challenges in the development of national policy.

What can be said with some certainty about retail motor traders are that, typically, they are small, 'mum and dad' type operations. Franchise systems are particularly prevalent. Also prevalent, though, are other forms of contractual arrangement, which seek (and, sometimes, merely allege) to proscribe specific performance requirements to both parties to mutual benefit.

Franchise systems are ubiquitous within the realm of new vehicle retailing. While AMIF understands that matters relating to franchising are not within the scope of Treasury's consultations in this instance, there nevertheless remains an aspect characteristic of franchising in the new vehicle retail space that comes close to meeting the criteria for further consideration in the context of unfair contracts.

It would be somewhat irregular these days to find a motor vehicle franchise agreement that failed to comply with the requirements of the Franchising Code of Conduct (the Code). What might be noticeable within an agreement, however, might be repeated reference to the franchisor's Policy and Procedures Manual, or like document. It may even be explicitly mentioned in the agreement made under the Code that a breach of specific articles within the Policy and Procedures Manual constitutes a breach of the broader agreement.

What can sometimes be found, though, is that said Policy and Procedures Manual – itself subject to little, if any, form of regulation – can be a document particularly arbitrary and pernicious in nature. Certainly, there have been examples of franchisor policies and procedures bought to the attention of AMIF in the past that would easily meet the three pronged test of being unfair by being;

- representative of a significant imbalance in rights, obligations and power relationship of the parties;
- not reasonably necessary for the protection of the franchisor's legitimate interests; and,
- demonstrated to cause detriment to the franchisee when given effect.

Nevertheless, documents of that sort -- which, in effect, compel specific performance requirements to be met by both franchisor and franchisee – seem beyond the scope of almost any regulatory framework. The manifested effect of those documents on the behaviour of the smaller party is also suggestive of the caution AMIF heeds around attempts to numerically, or otherwise rigidly, or specifically, define 'small business'.

AMIF suggests it far better for any such 'definition' to be conceptually based, or expressed in terms of relative power relationship. For while a typical, mid-sized, metropolitan new motor vehicle dealership may appear, by some criteria, to be anything but a 'small' business in terms of number of employees, or turnover (or a combination thereof of those metrics), it will assuredly be a 'small' business when compared with the scale and scope of its supplier.

Franchising and its artefacts aside, there are a number of other contractual arrangements that exist in an almost sector-specific manner. Those sectors and their contractual arrangements include;

- motor body repair and insurers' preferred repairer agreements;
- engine reconditioning and certain parts suppliers in that sector, and;
- parts recyclers and the contractual arrangements particular to certain mechanisms of parts-vehicle acquisition.

While the following discussion pertains specifically to those three areas of the retail motor trades, it is worth noting that unfair contracts can be evidenced in almost all of the trade's cleavages. For example, since the 2006 repeal of both the *Petroleum Retail Marketing Franchise Act (Cth) 1980* and the *Petroleum Retail Marketing Sites Act (Cth) 1980*, some contractual arrangements employed by some fuel suppliers can rightfully be described as unscrupulous. This can particularly be the case when the supplier has carefully constructed its operations so as to avoid evoking either of the Franchising Code of Conduct, or Oilcode. Tending towards being most accurately described as commission agencies, retail operators party to those arrangements can find contractual terms – especially those terms around tenure arrangements – as simply pernicious. Misuse of market power in these arrangements is rife.

The operational arrangements for these retailers can also be characterised by being established through the operation of a suite of contracts. Some are contracts that grant tenure and specify the minimum conditions for that tenure. Others prescribe the terms and conditions governing the supply of goods and/or services; the main one being the supply of petroleum products, particularly where the use of brand is involved. In almost all like circumstances, the key elements that determine a fuel retailer's profitability are governed by a contract.

Furthermore, the significant contracts are characteristically between the business operators and large businesses such as an oil company, or large wholesale supplier/landlord, where there is a significant imbalance in market power and financial resources. Yet, metrics such as turnover (as against and distinct from profitability) might preclude that business operation from being considered as a 'small business'.

Motor Body Repair

Arguably the most contentious area of contractual arrangement within the retail motor trades lies within the motor body repair sector. The majority of contracts in that sector take the form of preferred (or accredited, or nominated, or some other like term) smash repairer (PSR) agreements, which are made between insurance companies and motor body repairers.

Relationships between collision repairers have historically been strained, with the operation of the terms of PSR agreements invariably the focus point of tensions. Despite Roundtables convened by the Australian Competition and Consumer Commission in 2002; a 2005 Productivity Commission Inquiry into the collision repair and insurance industry; and, the development and launch in 2006 of the (voluntary in all jurisdictions except New South Wales where it is mandated) Motor Vehicle Insurance and Repair Industry Code of Conduct, motor body repairers continue to be positioned in invidious situations as a result of the operation of PSR agreements to which they are party.

While perhaps seeming benign, or fair, at superficial examination, closer examination will reveal there to be generally sufficient freedom and scope within PSR agreements as to facilitate a seamless shift of full advantage to the dominant party (the insurer) through the agreement's operation. A closer evaluation of typical PSR agreements can show, for example, evidence of the entitlement of one party (invariably the insurer), but not the other to:

- avoid or limit the performance of the contract or parts thereto;
- terminate the contract at will;
- apply sanction (such as non-award of work) for contract 'breaches';
- unilaterally vary contract terms;
- prevent the seeking of professional advice in relation to the contract;
- renew or not renew the contract;
- act as arbiter of unquestionable authority over quotes and work methods;
- unilaterally vary elements of agreed-to work methods or components to be used; and,
- accept no responsibility for the performance of any guarantees over work standards.

Ostensibly, PSR agreements seek to outline a mutually beneficial arrangement between two parties. While that can sometimes be the outcome, it can also equally be the reality that the insurer – through the operation of the agreement – exerts significant coercion and control over the repairer. AMIF would argue that virtually all PSR agreements have the potential to meet the three pronged criteria of being unfair; if not in the context of their enunciated terms, then most potentially through their operation and effect upon repairers in the market.

What is particularly salient with respect to these PSR arrangements is that they can form not just the foundation, but the structure, walls and roof of a collision repair business. Having an agreement of that sort in place can mean the difference between a repairer being in business and not. This is a circumstance rarely lost on insurers and a reality that repairers all too keenly feel. Given some of the mechanisms employed by some insurers in the administration of their agreements it is completely understandable that the tensions between insurers and repairers exist.

Attention is drawn to the confidential attachments to this submission, in which copies of typical PSR agreements have been included.

Engine Reconditioning

With the ever increasing complexity and applied engineering of contemporary motor vehicles in recent years, the field of engine reconditioning has become one of hugely increased precision, skill and specialisation. In that field, however, it can also be argued that there has been something of a transition in terms of parts supply. Many domestic Australian suppliers of components (such as gaskets sets, bearings, pistons and the like) have variously withered, ceased to exist, or established operations offshore. This often means that component choice in the market can be limited. Something that has also become evident in this field is that, in some instances, component quality has also suffered.

Terms of supply agreements in this field can also be characterised as being singularly lopsided and significantly favouring suppliers over engine reconditioners. While AMIF accepts that questions of component quality and warranty standards subsequent to component failure are more questions for the Australian Consumer Law (ACL) to address, it nevertheless considers that the agreements underpinning supply of those components typically represent a massive abrogation of responsibility; firmly place the reconditioner in an invidious situation of disadvantage and, thus, can be demonstrated to be unfair.

It is AMIF's understanding that, in the event of (say) a component failure lending to a catastrophic failure of a reconditioned engine (in several known instances, crankshaft failure in medium to heavy diesel engines), the reconditioner compelled to warrant *their* work will find themselves subject to terms of supply whereby they will be responsible for *all* costs associated with the demonstration and proving of component failure as the cause for catastrophic failure. This can involve the reconditioner engaging in the costly exercise of obtaining independent engineering and / or metallurgical evaluation and analysis.

Further, the conditions of supply clearly indicate that the supplier (of the failed component) bears no responsibility for any and all costs associated with rectification work (which can run into the many thousands of dollars). All the while, the best outcome that can be anticipated by the reconditioner, from the supplier, will be a replacement component for the one that caused the subsequent damage.

Again, while accepting that questions of goods and / or services failure are matters for the ACL to canvass, the *agreed conditions* of supply in these instances adopt an 'all care and no responsibility' stance and, as such, in operation, arguably meet an unfortunate gold standard for the three pronged test leading to business (and consumer) detriment.

It is worth noting that similar supply arrangements can be evidenced across many other sectors within the retail motor trades.

Automotive Parts Recycling

If component suppliers in the field of engine reconditioning can adopt an 'all care; no responsibility' positon in their supply agreements, then some suppliers in the automotive parts recycling sector elevate that position to an art form. This can be particularly evidenced in the terms and conditions for bidding and purchasing items at auctions dedicated to that purpose.

It is common practice for automotive parts recyclers to obtain stock by acquiring – typically at specific auction and sometimes 'online' – written-off vehicles. There can be numerous ways in which a vehicle can be categorised as written off; such as it being uneconomic to repair, or statutory (type, incidence and severity of damage), or arising from water immersion.

What can happen, however, is that the reason for that status being accorded can, to some extent, follow and attach to components sourced from that vehicle. Major components such as engines, transmissions, drive trains and electronic control units have mere scrap value if, for example, the vehicle from which they are sourced has been written off due to water immersion.

AMIF is aware of a number of instances in which parts recyclers have acquired vehicles at auction only to subsequently discover that the vehicle in question was not of the specification as advertised online, or clearly had suffered water immersion. AMIF has been informed of one particularly memorable instance, when over 12 litres of water was drained from the transmission and engine of a vehicle purchased at auction, with no indication given, at the time of offer for sale, of that vehicle having been written off for that reason.

In those circumstances, however, the terms of trade offered by the auction house – which, it must be noted, might be the 'only game in town' due to its contractual arrangements with insurers – deny virtually any and all avenues of recourse for compensation to the acquirer. This can mean that the acquirer, in the instances of AMIFs Members, parts recyclers, being significantly disadvantaged financially. Further, the position of dominance by the auction house, as asserted by its terms and conditions, offers the recycler zero remedy.

Attention is once again drawn to the confidential attachments to this submission, in which a copy of a typical terms and conditions agreement is provided.

Summary

Unfair contractual arrangements, while not exactly prolific, are reasonably easy to find operating within the retail motor trades. When found, that often exist as 'take it or leave it' propositions, upon which the ongoing viability of a retail motor trade operation may depend. For some traders, there is little alternative for them other than to cop the considerable bad that can come with a bare subsistence good.

As Treasury would be aware, AMIF (and its predecessor bodies) has been, and remains, a vociferous advocate of a fair business-to-business contracts regime. AMIF sees the adoption of the Discussion Paper's Option Three as an excellent first step towards the attainment of that goal.

AMIF hopes, however, that the process involved in the consideration of those options, and others, is not unnecessarily distracted, or becomes mired, in discourse around what comprises a small business for the purposes of this reform. Rather, AMIF hopes that the sensible approach is adopted, which approach has a basis founded on the concept of relative size of parties and their respective market and financial power.

AMIF trusts that the contents of the confidential attachment to this submission proves informative and instructive to Treasury. AMIF stands ready to provide the Treasury with any further clarification it requires regarding those documents, or any other assistance it requires generally on this matter. AMIF again thanks the Treasury for the opportunity to provide comments on the proposals outlined in the Discussion Paper.

AMIF NATIONAL SECRETARIAT

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‘Package’ of confidential attachments follows.