AUSTRALIAN AUTOMOTIVE DEALER ASSOCIATION

RESPONSE TO UNFAIR TRADING PRACTICES - SUPPLEMENTARY CONSULTATION PAPER

DECEMBER 2024

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FOREWORD

The Australian Automotive Dealer Association (AADA) welcomes the opportunity to make a submission in response to the unfair trading practices supplementary consultation paper.

The AADA is the peak automotive industry body representing Australia's franchised car and truck Dealers. There are 3,179 new vehicle dealerships in Australia employing more than 61,000 people directly, including around 5,500 apprentices, and generating $73.9 billion in turnover and sales with a total economic contribution of over $18 billion.

There is a structural power imbalance between franchised new car dealers and the multinational car manufacturers to which they are franchised. This has been demonstrated time and time again in various reviews and inquiries.

Despite some changes to the Franchise Code in recent years, we continue to receive record reports from Dealers about unfair conduct stemming from the power imbalance. This is evidenced by the record number of disputes in the industry.

We believe that it is essential that unfair trading practices protections cover franchisees, such as franchised new car dealers. In 2013, the New South Wales Government introduced protections under the Motor Dealers and Repairers Act which provided protections for New Car Dealers in their agreements with car manufacturers. One element of the protections is a prohibition against unjust conduct. The experience of these protections is that they have led to better relations between Dealers and manufacturers. In no way have the protections been found to lead to regulatory overreach or a reduction in competition. The number of car manufacturers selling cars through Dealerships in New South Wales has grown exponentially.

The global automotive industry is facing unprecedented change with forces such as the drive to decarbonise transport and the rise of the Chinese automotive industry. While change cannot be avoided, it is important that fairness is at the heart of an industry transition. Unfortunately, we are already seeing examples of manufacturers navigating this change by resorting to exploitative behaviour towards their Dealers.

Developing these kinds of protections for Dealers at a national level is long overdue and should be implemented as soon as possible.

The AADA strongly advocates that the proposed unfair trading practices protections should be expanded to cover all businesses regardless of size, or at a minimum all franchisees, to protect them against unfair practices at the hands of very large and well-resourced companies in their supply chain relationships.

James Voortman
Chief Executive Officer

KEY POINTS

Unfair trading practices protections should be expanded to ALL businesses.

Expand the definition under the general prohibition to sufficiently cover unfair or unjust behaviour that may not meet the high bar of unconscionable conduct under the ACL.

Expand nationally the unfair trading practices protections provided for motor Dealers in New South Wales.

Carefully consider the regulating of 'ease of cancellation' in such a way that does not jeopardise safety or functionality.

GENERAL COMMENTS

The AADA is encouraged by the decision to further consult on option 4, previously canvassed in the initial consultation, which includes introducing a combination of general and specific prohibitions on unfair trading practices. The AADA considered this to be the option which provides protections for consumers and businesses from the widest range of both current and emerging unfair trading practices.

Overall, the AADA is very supportive of the introduction of a prohibition to prevent unfair trading practices, however, a key concern is that these protections will be limited to consumers. The regulation impact statement (RIS) released in the first consultation found that a growing number of commercial practices fall into the category of unfair business practices or unfair trading practices and cause considerable harm to consumers and businesses and warranted reform in this area. Although the initial thresholds presented in the consultation were narrow, this supplementary consultation seems to be limited to consumers. We have real concerns that franchisees who are exceptionally vulnerable to unfair practices at the hands of their franchisor, due to the significant power imbalance, would not be covered under these protections.

There are a number of examples in the automotive industry of unfair trading practices that cause significant harm to businesses, but which currently fall into existing gaps or grey areas within the ACL. Where these grey areas or unfair practices occur, they often go unaddressed due to the inability to prosecute the case under the ACL or other industry provisions as experienced recently in the case between Mercedes-Benz and its Dealers.

As detailed extensively in our initial submission to the unfair trading practices consultation there are a number of current practices employed by manufacturers that could amount to unfair trading practices. These include early termination of dealer agreements without adequate compensation, setting of unrealistic sales performance and stocking targets, unilateral variations to contracts in business models, with little to no go negotiation with Dealers, and refusing to indemnify Dealers for work done to honour a warranty or Australian Consumer Law obligation. However these are not able to be currently prosecuted.

In a changing market due to external forces, including the New Vehicle Efficiency Standard, new entrants to the market and changing technology types, it is critical that these unfair trading practices are prohibited to protect Australian businesses and ensure they are not susceptible to undue harm.

While the list of specific prohibitions detailed in the consultation paper will generally not apply to dealer/franchisor relationships and the judicial precedent on a general prohibition, may take time to develop the AADA still considers this to be the most comprehensive approach to addressing these practices. A prohibition on these practices will encourage more cooperative attitudes from franchisors towards their franchisees, which will facilitate better discussion in negotiation.

NEED FOR EXPANDED COVERAGE OF UNFAIR TRADING PRACTICES

The AADA is not supportive of a staged approach to the implementation of prohibitions on unfair trading practices. The RIS consultation paper rightly pointed out that many businesses operate in the same climate as consumers and that they are also often subject to unfair trading practices at the hands of larger more well-resourced businesses, and the automotive industry is no exception.

The relationship between automotive franchisors and franchisees is often characterised by a power imbalance between OEMs and Dealers, driven by the superior bargaining power of the former. Dealers make significant non-negotiable investments in their businesses prescribed by the OEMs as part of the franchising agreement, often resulting in a lopsided dependency. Dealers frequently lose bargaining power due to this dependency, leaving them at the mercy of OEMs who can leverage this imbalance to their advantage.

Manufacturers exploit this vulnerability, exposing Dealers to Unfair trading practices and engaging in various practices that cause harm.

These can include, but are not limited to:

- Abrupt termination of Dealer agreements, often executed without the provision of any compensation or forcing Dealers to accept inadequate compensation within very short deadlines.
- Offering short term Dealer Agreements with no possibility of recovering sunk costs.
- Requiring a major investment as a prerequisite for renewing the franchise agreement.
- Pressuring Dealers to take on additional stock and register vehicles as sold to boost the manufacturer's market share.
- Refusing to indemnify Dealers (a legal obligation) for work done to meet an OEM's warranty and Australian Consumer Law requirements.
- Conducting random warranty audits and recovering large amounts of money by projecting results from a small sample over an extended period of time.
- Imposing unrealistic sales and performance targets to justify financial penalties on Dealers for failing to meet them.
- Making significant, one-sided changes to the business model with little to no negotiation with Dealers, resulting in models that poorly reflect Dealer operations and impact profitability.

The recent case between Mercedes Benz and their Dealers is a prime example of Dealers being subjected to unfair trading practices by OEMs, but not having the ability to challenge this behaviour as it does not reach the impossibly high bar of unconscionability. In 2021, Mercedes-Benz Australia (MBAuP) shifted from a traditional franchise model to an agency model without compensating Dealers for their substantial investments or the goodwill generated over the years. As a result, Dealers objected to this change and took legal action, accusing MBAuP of engaging in unconscionable conduct.

Despite presiding judge Justice Beach discovering a list of behaviours prompting concern, including the OEM's decision to convert Dealers into agents without compensating for their established goodwill, he ultimately was unable to find in favour of the Dealers. MBAuP effectively misappropriated Dealer business value by transferring benefits to itself free of cost and cherry-picking favourable aspects of Dealers' businesses for the agency model while leaving the less desirable ones with the Dealers. The Dealers lost the case due to the high legal bar for proving unconscionable conduct, with this case highlighting the regulatory gaps in the law, that need to be urgently addressed.

In his decision, Justice Beach remarked;

"It will be apparent from the reasons that I am publishing that the applicants were successful on many issues of fact but lost on the law, essentially".

"given the facts of this case leading to an adverse result for the applicants, it may be that further consideration needs to be given to the terms of the franchising code and possible modification, but that is a matter for another day and, obviously, in another forum".

The Hon Justice Jonathan Beach, Federal Court of Australia.

Detailed information on the Mercedes-Benz case is available in Appendix A.

Considering the potential exploitative behaviour of OEMs towards Dealers and the resulting harm to Dealer businesses, it is essential that the general prohibition on unfair practices is implemented to ensure a level playing field in the automotive industry.

The AADA strongly advocates that these protections be expanded to ALL businesses regardless of size, or at a minimum all franchisees, as many businesses are subject to unfair practices at the hands of very large and well-resourced companies in their supply chain relationships.

DEVELOPMENT OF A MORE ROBUST GENERAL PROHIBITION FOR BUSINESS

The AADA considers that for this prohibition to make real progress in preventing unfair practices, the general prohibition must be better designed than what is proposed. The proposed prohibition seems to only encompass elements of distortion and manipulation and the casing of material harm.

This is in contrast to the intent of the prohibition set out in the consultation paper that seeks to prohibit unfair practices that either do not meet the high threshold for unconscionable conduct under the ACL or are not prohibited by any other section of the ACL.

The AADA urges extra consideration of the way the general prohibition is developed particularly when considering how this would apply for business-to-business interactions.

The MBAuP case mentioned above, very clearly demonstrates how the proposed general prohibition would not sufficiently cover behaviour which is deemed to be unfair and cause harm.

In the statement made by Justice Beach, he determines that Dealers were successful on many issues of fact but lost on the law. This is highlighted by the fact that he decided, in the franchising context, goodwill only exists if there is an ability to continue operating the business in a substantially same manner. This means that when the franchise agreement ends, then the goodwill also comes to an end. Dealers demonstrated real harm caused by the appropriation of their goodwill, however, because of the differing concept of accounting and legal goodwill, Dealers would not be able to demonstrate material harm.

The AADA considers that this case is a perfect example of behaviour that should be prohibited in the implementation of a UTP prohibition however, this proposed narrow definition would not sufficiently cover this. As such, the AADA urges timely reconsideration and consultation on a robust general prohibition.

NEW SOUTH WALES MOTOR DEALERS AND REPAIRERS PROTECTIONS

Unfair trading practices which occur in business-to-business interactions is already regulated for motor Dealers in New South Wales. There, the power imbalance between franchised new car Dealers and larger, more powerful manufacturers resulted in the development of Part 6 of the Motor Dealers and Repairers Act 2013.

Under Part 6, Dealers are offered protections against Unjust Conduct. Conduct of a manufacturer is unjust conduct for the purposes of Part 6 if it is conduct:

a. that occurs in connection with a supply contract and is conduct that is dishonest or unfair, or

b. that is authorised by an unfair term of a supply contract.

(2) In determining whether to make a declaration that a term of a supply contract is an unfair term or that conduct is unjust, the Tribunal may take into account such matters as it thinks fit and is to have regard to all the circumstances of the case, including the contract as a whole.

(3) Without limiting subsection (2), the Tribunal may consider the following (if relevant) -

a. the extent to which the supply contract is expressed in reasonably plain language and is presented clearly,

b. whether or not there was any material inequality in bargaining power between the parties to the supply contract,

c. whether or not at or before the time the supply contract was made its provisions were the subject of negotiation,

d. whether or not it was reasonably practicable for a motor dealer to negotiate for the alteration of or to reject the term of the supply contract or any matter related to the contract,

e. whether a term of a supply contract imposes conditions which are unreasonably difficult to comply with or not reasonably necessary for the protection of the legitimate interests of any party to the supply contract,

f. whether or not and when independent legal or other expert advice was obtained by the motor dealer,

g. whether any undue influence, unfair pressure or unfair tactics were exerted on or used against the motor dealer -

h. the conduct of the parties in relation to similar contracts or courses of dealing to which any of them has been a party.

i. by any other party to the supply contract, or

ii. by any person acting or appearing or purporting to act for or on behalf of any other party to the supply contract, or

iii. by any person to the knowledge (at the time the supply contract was made) of any other party to the supply contract or of any person acting or appearing or purporting to act for or on behalf of any other party to the supply contract,

h. the conduct of the parties in relation to similar contracts or courses of dealing to which any of them has been a party.

NSW's leading legislation demonstrates that these practices can be effectively regulated against, and the AADA would urge this framework to be adopted in this development of a prohibition. This results in a situation where Dealers across Australia are operating under a patchwork approach to protections against unfair or unjust practices, whereby coverage is determined by the size of your workforce and the location of your business. It seems absurd that a Dealership employing 101 people will not be protected against a Fortune 100 company which generates revenues of hundreds of billions of dollars and employs half a million people. It seems equally absurd that a Dealer operating in Wodonga will not enjoy these protections while a Dealer of the same size in Albury will be protected

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CONCERNS WITH THE PROPOSED SPECIFIC PROHIBITIONS

Notwithstanding the fact that the AADA does not support the implementation of unfair trading practices in a staged approach, we still have significant concerns with elements of the specific prohibitions detailed in the consultation paper.

These concerns are mainly in relation to the provisions to address unfair subscription-related practices, which include prohibiting businesses from offering a subscription contract without meeting certain requirements.

Subscription services offered by vehicle manufacturers and Dealers, differ significantly in their nature and purpose from more traditional subscription models such as Netflix. For vehicle subscription services these often focus on enhancing the functionality and features of the vehicle they own and can include things such as software updates, assistance systems, entertainment or performance enhancements. These services are usually tied directly to the vehicle and are part of an ongoing relationship between the vehicle manufacturer and the consumer.

This is in contrast to generic subscription services (e.g. Netflix) where consumers are paying for access to content which does not directly alter the functionality or experience of an owned product. Additionally, vehicle subscriptions tend to be tied to the particular vehicle model, type or configuration and are more tailored than other subscription services.

As such, when regulating the barriers to cancellation of a subscription services, the AADA urges caution due to the potential impacts on consumer safety and accessibility when cancelling a vehicle-related subscription.

Unlike generic subscriptions, vehicle related subscriptions can often provide access to critical features, and if a consumer cancels a subscription on a whim they could be left without access to essential tools like navigation (which could be particularly vital in areas with low population density or no mobile coverage.

Regulating the ease of cancellation of services in such a way that does not jeopardise safety or functionality needs critical balance and must be carefully considered.

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CONCLUSION

We would be happy to meet with you to discuss our submission and participate in any further consultation. If you require further information or clarification in respect of any matters raised, please do not hesitate to contact me.

James Voortman
Chief Executive Officer
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APPENDIX A: MERCEDES-BENZ DEALER ACTION - CASE STUDY

Mercedes-Benz Australia (MBAuP) changed its business model from the traditional franchise model to an agency model. Almost 80% of MBAuP Dealers objected to the way in which the change to the business model was brought about, launching an action in the Federal Court of Australia. Among their claims was that MBAuP engaged in unconscionable conduct in the way it treated its Dealers.

All claims against MBAuP were dismissed, but in handing down his judgement Justice Jonathan Beach said, "that the applicants were successful on many issues of fact but lost on the law."

He went onto state that "the applicants' strongest case, although unsuccessful, concerned statutory unconscionable conduct".

In the publicly available judgement, Justice Beach listed off a series of behaviours MBAuP, including:

- MBAuP cherry-picked the best bits of the dealers' businesses on which the agency model was imposed and left the dealers with less desirable features.
- The dealers ultimately had a lack of choice concerning the terms of the agency agreements. Ultimately, they were presented on a take it or leave it basis they were given little time to negotiate the final form of the agency agreements and the associated agreements.
- There was no meaningful negotiation that the new model to be imposed would be an agency model.
- And on the main commission aspects, in my view MBAuP and MBAG ratcheted this down as low as they thought that they could get away with.
- I accept that the dealers were ultimately placed in a position of situational disadvantage and possibly constitutional disadvantage in terms of the agency model.
- MBAuP did not consider the individual circumstances of dealers. Moreover, it had little regard for the top 30% of dealers who were likely to suffer under the agency model. It noted that effect but had no sympathy for it.
- There were various themes that from time to time MBAuP put to dealers that were either exaggerated or turned out to be incorrect.
- It was put that the substantial reason justifying the agency model was because of the problem of disruptors, aggregators and future on-line transactions. These so-called concerns were also used in an effort to spook the dealers.

- MBAuP persistently ran the line that a concern was the intra-brand discounting between dealers and that the agency model was designed to avoid this. But the reality was that most of the intra-brand discounting was brought about by MBAuP's and MBAG's conduct in causing over-supply to increase market share and also the incentives to discount that MBAuP itself created flowing from its commission structure with the dealers.

Despite, these assertions, Justice Beach still decided that this behaviour did not amount to statutory unconscionable conduct, reinforcing the very high bar needed to prove such an offence as demonstrated by other cases in the franchising sector such as the Pizza Hut case and ACCC's undertaking with the Retail Food Group.

***Note the above material is taken from Justice Beach's judgement in AHG WA (2015) PTY LTD T/A MERCEDES-BENZ PERTH AND WESTPOINT STAR MERCEDES-BENZ and OTHERS And MERCEDES-BENZ AUSTRALIA/PACIFIC PTY LTD**

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