



TOYOTA MOTOR CORPORATION AUSTRALIA LIMITED

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Committee Secretary
Senate Education and Employment Committee
PO Box 6100
Parliament House
Canberra ACT 260

Re: Inquiry into General Motors Holden Operations in Australia

Toyota Motor Corporation Australia Limited (**Toyota**) appreciates the opportunity to provide a submission to the expanded 'General Motors Holden Operations in Australia' Senate Inquiry that now extends to investigating the regulation of the relationship between all car manufacturers and car dealerships in Australia. We note that Toyota has supported the numerous reviews into the automotive franchising sector that have been undertaken particularly over the past three years.

Toyota's submission is divided into two sections. The first section provides the Inquiry with an understanding of Toyota, our dealers, and the automotive industry more broadly. The second and more substantial section of the submission seeks to address all the topics listed in the Terms of Reference of the Inquiry.

Toyota's operations in Australia

Toyota is a sales and distribution operation, having previously also manufactured vehicles in Australia for 54 years until 3 October 2017. Toyota has retained a significant local presence in Australia beyond the closure of local vehicle manufacturing operations in Altona (Victoria). This local presence includes import and distribution activities, maintenance of a significant research and development division, as well as the establishment of a Centre of Excellence at our Altona site.

Toyota imports, markets, sells and services motor vehicles and related components, parts, and accessories in Australia. Toyota distributes all vehicles via its network of independent franchisees.

In 2019, Toyota was the top selling automotive company in Australia for the 17th consecutive year. In 2020, despite the challenges of a global pandemic, Toyota currently has a year to date market share of 21.5% and we continue to build upon our reputation of delivering reliable vehicles to our valued Australian customers.

Toyota's dealer network

Toyota has an expansive dealer network that is comprised of 198 dealers and 279 dealership sites across Australia. We note that dealerships are often referred to as small family-run businesses, however the purchase price of a Toyota dealership can range between \$2.5 million and \$30 million, with many Toyota dealers being large and well-resourced businesses, often part of group entities including publicly listed companies with operating profits up to \$100 million in 2019.



Moreover, unlike other franchised sectors, the automotive franchising sector is built on integrated relationships and complex business arrangements. Toyota is intrinsically linked to its dealers as evidenced also by Toyota Finance Australia's provision of approximately \$2.0 billion in equity funding to Toyota dealers and associated dealer group entities¹. It is therefore in our collective interest that dealers succeed commercially and that dealers carefully consider and manage their funding requirements and long-term profitability.

Toyota is dedicated to ensuring best practice is exercised across our dealership network to deliver the best experience for our dealers and our customers. The National Toyota Dealer Association (**NTDA**) was established to ensure a collaborative relationship between the dealership network and Toyota while respecting the requirements of the *Competition and Consumer Act 2010* (Cth).

The NTDA has many functions, including exploring new opportunities, sharing industry learnings, as well as providing a forum to raise concerns or complaints so they can be addressed in an informal forum without the need to progress to expensive and lengthy formal dispute resolution. Toyota also invites its dealers to participate in a broad range of other forums, including business improvement forums which facilitate enhanced benchmarking. The core objective is to continuously improve the performance of our dealers and therefore the success of the Toyota brand to the benefit both of Toyota and the dealer network.

The evolving automotive landscape in Australia

The new vehicle market in Australia has changed significantly in the last 35 years due to government's introduction of administrative arrangements for the automotive industry that began with the implementation of the passenger motor vehicle manufacturing plan (the 'Button Car Plan') introduced in 1984. In addition, the proliferation of bilateral and multilateral free trade agreements has resulted in hyper competition on the Australian domestic automotive market as a result of lower tariffs and duty charges.

As an outcome of the above, Australia is one of the most open and competitive new vehicle markets in the world with 69 different brands competing for an average of 1 million sales a year, while in the USA a similar number of brands compete for an average of 17 million sales a year. While more competition benefits consumers, it also spreads the share of sales across more brands, therefore impacting individual manufacturers sales volumes, which in turn has implications on dealership networks.

Disruption happens in all industries and the automotive industry is no exception. Manufacturers and dealers must have the flexibility to react to changes as they occur. The automotive industry is continuing to undergo significant transformation, as evidenced through events such as the closure of manufacturing facilities and the shift from vehicle ownership to vehicle usership with the arrival of car share/ride share companies. Other intermediary groups and new entrants such as technology companies focused on autonomous vehicles, will continue to disrupt the entire industry along with a range of Government policy measures, for example the Specialist and Enthusiast Vehicle Scheme allowing uncapped import volumes that compete with established dealers without the support framework offered for vehicles imported by branded distributors. The industry must be prepared for changes and ensure a pragmatic approach is taken so dealers, manufacturers and other key players stay relevant and continue to thrive commercially.

¹ Toyota Finance Australia Limited is a related body corporate of Toyota Motor Corporation Australia Limited as defined under section 50 of the *Corporations Act 2001* Cth

Below are comments on the specific matters outlined in the terms of reference of the Inquiry.

1. Practices employed by manufacturers in their commercial relations with dealers

(a) Investment required and tenure provided

Toyota includes significant capital expenditure requirements in the special conditions in a dealer agreement. There is a consultative process between Toyota and the relevant dealer prior to execution of the dealer agreement and the special conditions.

In the case that capital expenditure is required (noting that this is not always the case) during the term of the agreement, Toyota will work with the dealer to ensure it is a manageable outlay. Toyota puts significant emphasis on disclosing information that is meaningful and as precise as possible. In 2018 Toyota developed a 'Facilities Calculator' to assist dealers in calculating the pay-back term for the required capital investment in line with the term of the dealer agreement. Dealers are also provided with a facilities manual that outlines the minimum standards for a Toyota dealership, including details around layout and merchandising, down to the specific materials that will be required.

Toyota Australia has and will continue to accommodate changes to the context in which a dealer operates after finalisation of the dealer agreement (for example in the event of a natural disaster such as bushfire and drought which affects the dealer's surrounding community and economy). In such cases, Toyota and the dealer adjust previously agreed capital expenditure requirements to a more appropriate level given the change in circumstances.

As at 1 June 2020, new 'significant capital expenditure' disclosure requirements were introduced under changes to the Franchising Code of Conduct (**Franchising Code**)², including requiring disclosure of anticipated outcomes and benefits of the expenditure, and a discussion between the parties about the circumstances under which the expenditure is likely to be recouped, before the dealer agreement is signed. It is comforting to know that Toyota's existing practices already comply with this new legal requirement.

In terms of dealer tenure, five-year minimum term dealer agreements have been standard practice for Toyota, therefore providing a level of certainty for dealers to recover their investments. Toyota recently made amendments to our standard dealer agreement which commenced on 1 May 2020. This was a consultative 8-month process with the NTDA and their independent legal advisor to further strengthen our industry leading agreement. The standard term of the new dealer agreement is also 5 years. Dealers will receive a one off 2-year further extension if:

- a) they have completed any facility redevelopment agreed between Toyota and the dealer under the consultative process described above; and
- b) they were compliant with all other policies.

Subject to certain conditions being met, it is Toyota's intention to extend the new dealer agreement at the end of the term for a further standard term of 5 years. Again, this provides dealers with a level of certainty to be able to recover their investments over the term of their dealer agreements.

² Competition and Consumer (Industry Codes – Franchising) Regulation 2014 made under the *Competition and Consumer Act 2010* (Cth).

(b) Termination and compensation practices

Toyota rarely terminates dealers. If dealers are no longer keen to be a part of the journey with Toyota, we exercise the non-renewal clause in our dealer agreement as a last resort. This decision is only undertaken after Toyota has considered all other avenues and after having worked collaboratively with the dealer.

If a dealer decides to sell the business as part of the non-renewal process (the most common scenario), the dealer is required to make an 'Application to Transfer' to Toyota and obtain Toyota's consent in respect of the incoming franchisee. In line with the Franchising Code, Toyota will not unreasonably withhold consent. Further, as part of ensuring a respectful exit for the outgoing dealer, Toyota will provide the dealer with assistance where required.

As at 1 June 2020, if a dealer is not renewed, the parties need to agree on a plan to have agreed milestones for managing the reduction in the stock of vehicles, spare parts, repair, and servicing equipment and for the parties to work together to achieve that plan. Also in this case, Toyota's already established practice of providing dealers with a 'wind down' plan covers many of the facets of this recent change in law.

Given the Toyota practices outlined above in relation to investment, tenure and termination, Toyota does not compensate dealers in the event of termination / non-renewal. Toyota is of the view that the issue of compensation should only arise if termination has been conducted wrongfully, in which case, a dealer would have a right under the existing legal regime to recover damages.

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(c) *Performance requirements*

A strong and high performing Toyota dealer network is vital to Toyota's long-term success. Toyota works closely with dealers in respect of their performance and their overall compliance with the dealer agreement.

Toyota has a robust performance improvement system, which was recently reviewed and revised. Toyota acknowledged that its previous performance management regime was skewed towards sales performance and not in harmony with our 'Toyota for Life' qualitative standards incentive program introduced in 1 January 2015 which rewards dealers for providing customers with the best experience in all areas of dealership operations. The new performance management regime developed now closely monitors dealers' performance on several facets, making it an even more balanced and sustainable model.

Toyota also sets KPIs that are measurable and unique to each dealer and recognises improvements made by dealers. If there is a situation where a Dealer is not meeting performance requirements, Toyota will work with the dealer to address any issues. Toyota, through its regional offices, conducts regular reviews of how dealers are tracking in respect of their performance. Toyota also provides dealers with the relevant assistance required in the event a dealer is not performing at the requisite standard. If required, we also implement a performance improvement plan for dealers.

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(d) *Behaviour around warranty claims/Australian Consumer Law*

Toyota and its dealers are committed to resolving customer concerns quickly and effectively, and in accordance with customers' rights under the consumer guarantees in the Australian Consumer Law (**ACL**).

As part of its core value of *kaizen*, or continuous improvement, Toyota has implemented a number of measures which include:

- the publication of the Toyota Guest Charter, a customer facing document on the Toyota website at <https://www.toyota.com.au/toyota-guest-charter>;
- the introduction of an overarching policy document in relation to the statutory consumer guarantees, called the Guest Rights Guide. This Guide is designed to help dealers understand customer's legal rights under the ACL;
- the introduction of a new warranty the Toyota Warranty Advantage, a 5-year unlimited kilometre warranty which commenced on 1 January 2019; and
- rollout of training to the dealer network, focussing specifically on the statutory consumer guarantees.

Toyota has also been reviewing its processes for considering and assessing consumer requests in accordance with the ACL.

Dealers also have the benefit of a statutory indemnity from Toyota for cost incurred by them as a result of manufacturing defect claims under the ACL. A similar indemnity is also provided for contractually in the Toyota dealer agreement.

Toyota assists dealers with manufacturer's warranty repairs. Toyota works together with our dealers in respect of warranty claims. Dealers can contact the Toyota warranty and technical help desks if they have any warranty or technical concerns.

Dealers are required to diagnose vehicles and lodge warranty claims. Most claims (more than 90%) are approved automatically. Toyota only reviews warranty claims for significant amounts or when specific requirements are not met. Toyota also allows dealers to claim any reasonable time incurred in respect of inspecting / diagnosing vehicles as part of a warranty claim. Toyota does not deny warranty claims that are legitimate.

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(e) *Unfair terms in contracts*

On 12 November 2016, the unfair contract term provisions in the ACL were extended to cover terms of standard form contracts to which small businesses are parties. The Government announced in March 2019 that it would further strengthen the protections for small businesses from unfair contract terms that it introduced in 2016. On 13 December 2019, the Department of the Treasury released a Consultation Regulation Impact Statement on enhancements to unfair contract term protections. The paper sought feedback on the application of any enhanced unfair contract term protections to franchise agreements and closed on 27 March 2020.

One of the drivers for the above change is the argument that some dealers not being protected by unfair contract terms regime as they are not small businesses. This is not true of Toyota as Toyota adopts a standard agreement with all dealers, including dealers that fall within the definition of a 'small business' under the unfair contract terms regime. This means that the entire dealer network (no matter what the size of the dealer) receives the protection from unfair terms in contracts. Another way in which Toyota prevents unfair terms in contracts is via a consultative process with the NTDA. For example, any changes to the dealer agreement are made with close consultation with the NTDA to ensure transparency and to promote fairness.

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(f) *Goodwill and data ownership*

To aid the Inquiry's understanding, there are two different forms of 'goodwill' which are relevant to this discussion. Toyota, like other manufactures, is the owner of a suite of valuable trademarks which have been strengthened over decades with significant investment into the brand. Dealers do not pay a 'franchise fee' or a trademark licence fee. Toyota grants dealers a non-exclusive free of charge licence to use the Toyota name and the licensed trademarks during the term of the dealer agreements. Accordingly, goodwill in those brands and trademarks should rightly vest with Toyota.

Secondly, there is also goodwill that attaches to the dealer's business. That goodwill arises for accounting purposes when a sale of a business takes place at a price which exceeds the value of its net assets. That excess is called 'goodwill' and it is commonly understood and recognised as belonging to the dealer.

On the question of data ownership, as we move towards connected mobility, Toyota is handling expanding volumes of data, including personal data. Our approach to protecting our customer's data is underpinned by our core value of respect for people, and our guiding principles. Toyota's Privacy Policy provides clear notification about why, how, when and to what purpose we collect personal information from our stakeholders.

Dealers must also comply with the Australian Privacy Principles regarding notification and consent for collection and handling of personal information and provide clear instructions on how customers can change permissions, correct, or remove their data from services and channels. If a dealer becomes aware of a data breach involving Toyota customer data, it must immediately notify Toyota.

As part of the Data Sharing Policy agreed between Toyota and the NTDA, Toyota may obtain customer data from its dealers for a number of purposes, such as sharing vehicle service history, customer support / experience and product development.

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2. Existing legislative, regulatory, and self-regulatory arrangements

The relationship between dealers and manufacturers has most recently been under review for several years since the Market Study into New Car Retailing Industry was released in 2017 by the Australian Competition and Consumer Commission (**ACCC**). This was followed by a Regulation Impact Statement into Franchise Relationships Between Car Manufacturers and New Car Dealers in 2019 by the Department of Industry, Innovation and Science.

In February 2020, the Automotive Franchising Draft Regulations were released by the Department of Industry, Science, Energy and Resources which resulted in the most recent Franchising Code reforms that were implemented from 1 June 2020. Further, on 20 August 2020, the Government released its response to the 2019 Parliamentary Joint Committee's 'Fairness in Franchising' report which investigated the operation and effectiveness of the Franchising Code.

The Government's response does not specifically address the 71 recommendations proposed in the report - 27 of which were referred to a Franchising Taskforce comprised of government agencies to assess in more detail - but does address themes from the report covering pre-entry, operational, and exit issues in franchise relationships. These themes overlap with the Terms of Reference of this Inquiry.

Some of the key changes proposed by the Government in its response are as follows:

- increased penalties: increasing the maximum civil pecuniary penalty under the Code to \$133,200, doubling the penalties that apply for its breach. The Government will also impose pecuniary penalties for breaches of clauses in the Code regarding the use of marketing funds;
- increased disclosure requirements: targeted improvements to the information that must be disclosed to prospective franchisees; and
- significant capital expenditure: strengthening franchisees' rights when a demand for significant capital expenditure is made, including by prohibiting franchisors from requiring franchisees to undertake significant capital expenditure unless it is disclosed prior to entering into a franchise agreement, it is legally required or the franchisee agrees.

In addition, the Government has indicated that consultation with the franchising sector will inform its development of:

- a public register of franchisors, to help prospective franchisees make an informed decision before entering a franchise agreement; and
- amendments to the Franchising Code to facilitate negotiated early exit of franchise agreements.

The Government has not provided any indication of the timing for implementation of the changes to the Franchising Code.



Most recently, on 22 October 2020, the ACCC announced a blanket class exemption for franchisees and small businesses. This is due to commence in early 2021 and will allow dealers to collectively negotiate with manufactures regardless of their aggregated turnover and without having to seek ACCC approval. This means that dealers can now work together, also through an industry or a group representative, to collectively negotiate supply terms and prices without needing to worry about a possible competition law breach, which in turn, further empower dealers.

Toyota acknowledges the importance of dealing with car dealers' concerns in respect of their franchising relationships with car manufacturers. However, Toyota is of the view that many if not all of these concerns have been dealt with by virtue of the new June 2020 reforms to the Franchising Code, coupled by the further changes alluded to by the Government in its response to the 'Fairness in Franchising' report. Toyota is surprised that this Senate inquiry has been extended to other manufacturers recently, soon after the implementation of June 2020 reforms and given the ongoing work as a result of the 2019 Parliamentary Joint Committee's 'Fairness in Franchising' report.

As outlined above, Toyota already had in place a number of practices that matched the new Franchise Code requirements. Given the short timeframe since the latest reforms, Toyota believes it is too soon to be considering additional change, and this Inquiry should be mindful of the additional 'red tape' and its impact on business that comes with continual change and a fragmented approach to reform.

Toyota's position has always been that enforcement of the current regulations should be the priority, rather than the introduction of new and over burdensome regulation that will stifle changes determined via market and consumer behaviour. In the event that reform is truly necessary, it should be the result of a coordinated, informed and measured approach in consultation with all relevant stakeholders.

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3. Current and proposed government policy

Toyota is concerned that any further changes to the Franchise Code related to automotive increases regulatory burden which may not be warranted. Consistent with the past, Toyota expects there will be continued changes in market conditions that will bring further market disruption.

Any policy changes should not be based on the Holden experience. Holden Australia's actions were necessary due to several bespoke factors, including a decision made by its parents to cease the production of right-hand drive vehicles. The impact of this decision affected the entire Holden dealer network.

In terms of future policy, the automotive landscape is evolving technologically and in terms of the range of services. As automation and connected services proliferate, there will likely be new entrants to the market, including technology companies that have not traditionally operated in the automotive space, as well as fundamental changes to mobility services that will impact the usership and ownership of vehicles. Future policy will need to take these changes into account to ensure regulations do not hinder the evolution of the market and the inevitable changes that will occur as a result of market and consumer demand, in line with other global changes.

4. Dispute resolution systems and penalties for breaches of the Franchising code

While the Franchising Code already imposes compulsory dispute resolution processes, as at 1 June 2020 (with the changes to the Franchising Code), dealers now have the option to request to participate in multi-franchisee dispute resolution. If two or more dealers each have a dispute of the same nature with a franchisor, the dealers may ask the franchisor to deal with their disputes together.

Depending on the scale and size of the concern, disputes and issues are usually raised individually by dealers, or collectively through the NTDA and its various sub-committees. Multiple dealer disputes can be raised in this forum and communicated back to Toyota via the NTDA. Alternatively, Toyota maintains the presence of regional offices' who are available to assist with specific dealer concerns. As a result of the many avenues Toyota provides dealer to raise and resolve concerns informally and quickly described above, Toyota's dispute resolution provisions in our dealer agreement have only been used 3 times in the past 10 years.

An increased penalty was one of the recommendations that was proposed in the 2019 Parliamentary Joint Committee's 'Fairness in Franchising' report. In response to this report that was released on 20 August 2020, the Government advised that penalties for breach of the Franchising Code will double from 300 penalty units to 600 penalty units, i.e. from \$66,600 per breach to \$133,200 per breach. While this is a significant change, it does not go as far as the recommendation of the 'Fairness in Franchising' report which called for penalties to be similar to those under the Australian Consumer Law, which can be upwards of \$10 million.

This is not surprising given the ACCC's scrutiny into the franchising sector, coupled by the decision in *Australian Competition and Consumer Commission v Ultra Tune Australia Pty Ltd* [2019] FCA 12 (**the Ultra Tune case**), which was the first case in which the ACCC seriously tested the Franchising Code penalty resulting in a penalty of \$2.6million.



The increase in penalties will further deter manufactures from breaching the Franchising Code. If the Inquiry were to accept that there was a theoretical power imbalance in favour of the manufacturers, any attempt to exploit this to the detriment of dealers would be unlawful under a range of other laws coupled by the hefty penalty regimes already existing in Australia (for example under the ACL which was the basis for the above-mentioned Ultra Tune case penalty).

5. Current and proposed business models in selling vehicles

Toyota has no plans to change its dealership model. Notwithstanding this, the automotive industry will inevitably evolve over time due to a range of external factors such as the growth of online sales.

Toyota is committed to an ongoing open and transparent partnership with its dealer network, in which significant decisions are not made in isolation, rather via consultation with the NTDA. Toyota highly values its dealer network. Our success is supported by the strong, symbiotic relationship with our dealers and we view our dealer arrangement as a partnership and that no one party can win at the others expense on a long-term basis. Toyota's approach is to consult closely with its dealer network and collaboratively explore opportunities that benefit the network.

6. Legislative, regulatory, and self-regulatory arrangements found in international markets

Toyota is aware of different practices and approaches in overseas markets; however, our primary focus is the unique requirements of the Australian market and we do so consultatively with our dealer network.

7. The imposition of restraints of trade on car dealers from car manufacturers

Toyota does not believe there is an imposition of this nature on the Toyota dealer network as a significant proportion of Toyota dealers also operate other automotive branded franchises. More generally, franchised dealers in Australia are almost always multi-franchised operations that fiercely compete for potential customers.

Should you wish to discuss any of the above, please contact Andrew Willis, Manager - External Affairs

Yours faithfully

TOYOTA MOTOR CORPORATION AUSTRALIA LIMITED

Matthew Callachor

President and CEO, Toyota Motor Corporation Australia