

Parliamentary Joint Committee on Corporations and Financial Services
ANSWERS TO QUESTIONS ON NOTICE
Department of Industry, Science, Energy and Resources
The operation and effectiveness of the Franchising Code of Conduct

AGENCY/DEPARTMENT: DEPARTMENT OF INDUSTRY, SCIENCE, ENERGY AND RESOURCES

TOPIC: Car dealership agreements

REFERENCE: Question on Notice – Senator O’Neill

QUESTION No.: 1

Please provide a policy response as to the benefits of a voluntary principles based guide versus a mandatory principles based guide to improve the transparency and fairness of car dealership agreements as noted in the Government response?

ANSWER

There have been a number of important recent regulatory changes to franchising arrangements, including automotive specific changes, which will provide a stronger legal framework for the industry by strengthening the Australian Consumer Law and the Franchise Code of Conduct.

The reforms and other review processes currently underway, and which have yet to properly take effect across the industry, include:

- The Australian Government’s 1 June 2020 automotive specific amendments to the Franchising Code of Conduct,
- Recently announced reforms arising from the Government response to the *Fairness in Franchising report*, and
- Treasury-led processes on a mandatory scheme for access to motor vehicle service and repair information, unfair contract terms, consumer guarantees and supplier indemnification.

To better support these reforms the Government has offered to facilitate with industry peak bodies the development of a possible set of best-practice guidance principles on compensation and tenure which could assist franchisees and franchisors in meeting their obligations when developing new automotive franchise agreements.

An industry-driven approach, which is based on shared expectations developed using the expertise and experience of franchisees and franchisors, is likely to be more efficient and effective than uniform standards at a time where business models are responding to changing commercial pressures, and where the circumstances between brands and dealers can vary considerably.

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TOPIC: Car dealership code

REFERENCE: Question on Notice – Senator O’Neill

QUESTION No.: 2

Please provide a policy response as to why you are not proposing a specific standalone 'Car Dealership Code'?

ANSWER

The Government took the decision to introduce automotive elements via amendments to the Franchising Code of Conduct (the Franchising Code) rather than developing a stand-alone automotive code. This was based on feedback from industry consultations and advice from a number of Government departments that a stand-alone code would result in duplication and potential divergence due to any subsequent updates to the Franchising Code.

It was considered that amendments to the Franchising Code would provide the same regulatory effect as a stand-alone industry code.

On 20 August 2020, the Government announced reforms to the Franchising Code to help ensure fairness and accountability for both franchisees and franchisors, including those in the automotive retailing sector.

This builds on the Government’s 1 June 2020 automotive-specific reforms to franchising arrangements to make the system fairer for consumers, dealers and manufacturers. The reforms were made to:

- Increase End of Term notification periods
- Improve transparency for capital expenditure requirements, and
- Clarify options for dispute resolution.

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TOPIC: Breach of Franchising Code of Conduct

REFERENCE: Question on Notice – Senator O’Neill

QUESTION No.: 3

The ACCC recommended the maximum penalty for a breach of the Franchising Code be in line with the civil penalties of the ACL.

The committee in its final report made the same recommendation to increase the civil penalties for the Franchising Code to be in line with the recent changes to the ACL.

- a) Please provide a detailed policy response as to why the Government hasn't followed the ACCC and the Committee's recommendation?
- b) Specifically, what effects, intended or unintended, would increasing the penalty regime have on Franchisors and Franchisees?

ANSWER

The Government has committed to a doubling of penalties for breaches of the Franchising Code. The maximum penalty will be increased to \$133,200 (or 600 penalty units).

The doubling of penalties is considered an appropriate increase to act as a strong deterrent against breaches while aligning with the framework of industry codes.

The ACCC can still seek larger penalties (under Australian Consumer Law) where a franchisor engages in misleading, deceptive or unconscionable conduct. For corporations, the maximum penalty will be the greater of:

- o \$10,000,000
- o three times the value of the benefit received, or
- o 10% of annual turnover in preceding 12 months, if court cannot determine benefit obtained from the offence.

For example, in 2019 the ACCC successfully sought civil penalties of \$2 million against Ultra Tune for breach of the Franchising Code and the Australian Consumer Law. Doubling of the penalties for breaches of the Franchising Code will further enhance compliance with code to the benefit the franchising community.

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TOPIC: Franchisee involvement in decision making processes

REFERENCE: Question on Notice – Senator O’Neill

QUESTION No.: 4

1. In regard to greater franchisee involvement in decision-making processes, please provide a detailed policy response as to why there isn't a recommendation to adopt the McDonald's 'three-legged stool' approach?
2. In addition, please provide any policy or actions that the Government proposes which will increase franchisee involvement in decision-making processes.

ANSWER

The Parliamentary Joint Committee did not recommend the adoption of the 'three-legged stool' approach to decision-making.

Franchisors are obliged to act in good faith in their dealings with franchisees and should generally consult with franchisees and consider their interests as part of the decision-making process. Best practice is for franchisees to be involved in decision-making in the franchise. Many franchise systems have advisory committees that can benefit both the franchisor and franchisee when established and run appropriately. Franchisors are best placed to decide the composition of their boards and how to ensure franchisees are involved in decision making.

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TOPIC: Unintended consequences of increasing the franchisee decision-making process

REFERENCE: Question on Notice – Senator O’Neill

QUESTION No.: 5

In your response you refer to the unintended consequences of increasing the franchisee decision-making process within franchising.

- a) Please provide a summary of the unintended consequences of increasing the franchisee decision-making process in respect to regulating franchising as a general partnership co-investment model compared to any benefits it would achieve?
- b) In addition, please provide any unintended consequences or benefits of increasing the franchisee decision-making process without regulating franchising as a general partnership co-investment model.

ANSWER

Regulating franchising as a general partnership co-investment model would be a fundamental change to franchise systems and existing relationships between franchisors and franchisees.

Franchising and partnerships are distinct business structures in Australia and there are a number of potential unintended consequences from regulating franchising as a partnership model. Regulating and redefining franchising as a partnership in Australia would potentially:

- increase the regulatory burden on franchisors and franchisees by effectively banning the current model of franchising and requiring them to adapt to a completely different model,
- allow franchisees to have greater involvement in the management of the business but ultimately greater liability for its debts,
- require significant upheaval to established regulatory structures and could potentially lead to a fragmented regulatory approach if some states and territories become involved in regulating such partnership arrangements (which are not regulated by the Commonwealth),
- create unwieldy businesses with hundreds of partners with different needs and interests,
- be a barrier to entry for new firms and stifle innovation and choice,
- result in existing franchisors moving to other business models.

A key attraction of franchising in Australia is that franchisees purchase an established brand and receive support in managing the business from the franchisor. Franchisees rely on a business system that maintains consistency in terms of important factors such as operations, marketing, consumer experience and product offerings.

Alternative co-investment models that may unduly interfere with franchisor control undermine the foundations of franchising. It can also disadvantage franchisees, particularly smaller single-system owners, who may be forced to undertake actions influenced by other franchisees.

Industry codes are designed to allow industry participants to develop regulatory structures suitable for the sector. Franchising is a diverse sector and any potential regulation should consider impacts the whole sector.

Franchisors are obliged to act in good faith in their dealings with franchisees and likely consult with franchisees and consider their interests as part of the decision-making process. Best practice is for franchisees to be involved in decision-making in the franchise. Many franchise systems have advisory committees that can benefit both the franchisor and franchisee when established and run appropriately. Advisory committees that are poorly structured and managed can become problematic and ineffective. Franchisors are best placed to decide the composition of their boards and how to ensure franchisees are involved in decision making.