

Smash Repair Inquiry  
Productivity Commission  
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## **INQUIRY INTO THE RELATIONSHIP BETWEEN SMASH REPAIR AND INSURANCE INDUSTRIES**

The Small Business Development Corporation (SBDC) welcomes the opportunity to make a submission to the Commission's Inquiry into the relationship between the smash repair industry and the insurance industry.

The SBDC is a Western Australian statutory government agency incorporated under the Small Business Development Corporation Act 1983. The SBDC provides advice and assistance to new and existing small businesses in Western Australia. The SBDC also monitors and comments on policies and legislation that impact on the growth and development of the small business sector in this State. In addition, the Corporation supports a network of 35 independent Business Enterprise Centres across the State.

In Western Australia, the relationship between smash repairers and insurance companies since the early 1980s could generally be characterised as 'adversarial'. There have been ongoing disputes regarding hourly rates paid to repairers, the development by insurance companies of accredited or preferred repairer schemes and slow or late payments to repairers. These issues have been exacerbated as a result of ongoing structural changes in the industry, including improvements in technology and training, together with changes in the market for insurance products and heightened consumer expectations regarding the quality and efficiency of repairs.

The SBDC believes that the sustainability of small business body repairers is essential, and in the wider community interest, to ensure there is a competitive and efficient market for repair work. In such a market consumers will be the ultimate beneficiaries of reliable, safe and prompt repair work and competitively priced premiums. Viable and harmonious working relationships between insurers and repairers are essential to deliver these desired outcomes.

It is in the interests of repairers and insurers alike that contractual arrangements entered into between them are perceived to be equitable and fair by both sides, with mechanisms in place to ensure transparency and accountability across the whole commercial relationship. Currently, this does not seem to be the case. The SBDC believes that development of a national industry code of conduct represents the best option to address contentious issues, as an alternative to expensive litigation processes or regulatory intervention by governments.

The SBDC considers the following issues are of major concern to industry participants - insurers, repairers and consumers.

### 1. Preferred smash repairer schemes

Repairers have complained about insurers directing motor vehicle repair work to businesses that are part of an accredited or preferred repairer network. The repair industry believes that consumers are part of a tri-partite arrangement between insurers, repairers and customers and consequently should be able to choose their own repairer, irrespective of whether they are part of a preferred network. The repair industry is concerned that small firms outside the preferred network will struggle to remain viable if arbitrarily excluded from participation in insurance repair work, particularly if the criteria used by insurance companies for accreditation lacks objectivity and transparency.

The Australian Competition and Consumer Commission (**ACCC**) indicated that preferred repairer arrangements do not constitute a breach of the third line forcing provisions of the Trade Practices Act (TPA) because the repair services are generally obtained by the insurer, rather than the policy holder, and therefore the policy holder enters into a single contract with the insurer. A recent Federal Court decision (*Australian Automotive Repairers' Association v Insurance Australia Limited*) also upheld the position that there is no tripartite customer relationship because the customer remains with the insurance company and there is no contract between the repairer and the policyholder.

Notwithstanding these views, and while the SBDC believes that while preferred repairer arrangements have introduced benefits for consumers, there are legitimate concerns from repairers that some insurers are using these **schemes** to force rationalisation on the industry. Insurers have sought to promote industry rationalisation on the basis of significant decreases in the number of motor vehicle accidents across Australia with consequently less work being available for repairers generally.

The SBDC is also concerned that criteria for accreditation used by insurers varies across the industry, lacks transparency and can be used subjectively to keep particular repairers, or classes of repairers, out of the network with potentially devastating economic consequences for those firms. Opportunities for membership of preferred repairer schemes should be open to all repairers that

can meet the required (published) standards and there should be an appeal process, whether industry or individual insurer based, to determine claims against unfair exclusion by repairers. Insurers should, if requested, be compelled to provide reasons for decisions made where a repairer is unsuccessful in being granted preferred status.

Repairer groups have noted that preferred repairer schemes have some characteristics akin to franchising, including purchase of badging material and the use of insurance company branding. The SBDC, while not seeking to confer franchise status on these arrangements with access to the dispute resolution and disclosure processes available under the Franchising Code, nevertheless believes that repairers are entitled to some similar forms of protection under preferred scheme arrangements. The simplest way to achieve these objectives would be to incorporate dispute resolution, disclosure and appeal processes into an industry code of conduct.

The SBDC also shares repairers' concerns to ensure that consumers are not misled about the capabilities and skills of those repairers that are not part of the preferred scheme network, particularly as it is probably not economically feasible for every repairer to become a member. The SBDC supports the ACCC's view that the industry needs to reach consensus on the terminology used to fairly describe and categorise non-member suppliers.

Insurers do have a commercial right to limit membership of preferred schemes, depending upon each insurer's needs and requirements, but in tandem with that right is an obligation not to create a misleading or deceptive impression about highly skilled and qualified repairers that are not part of the network, for whatever reasons. The SBDC believes that these issues can only be addressed as part of a national industry code of conduct.

## **2. Consumer choice**

Consumer groups have indicated that the issue of choice of repairer is not a fundamental concern to the majority of consumers - they care more about whether the vehicle is repaired quickly, efficiently and to a high standard of workmanship. At the same time, consumers want to see harmonious and effective relationships between insurers and repairers which will deliver benefits to them by way of quality repairs and competitively priced premiums.

The introduction by insurers of preferred repairer schemes and valet repair services has further removed consumers from a direct relationship with repairers. While not disputing that some consumers would prefer insurers to take control of all aspects of the repair process, the SBDC is concerned that consumer choice has been eroded unnecessarily - to the detriment of consumers and repairers alike.

Some of the major insurers operating in WA allow consumers to seek quotes outside their preferred repairer schemes, thereby acknowledging that consumer demand exists for alternative repair arrangements. There are, however, disincentives placed in the way of consumers seeking to go this route. Insurers will only pay out a cash settlement for repair work to the value decided by its own assessors. There is no capacity for the consumer to challenge the insurer's assessment as being unfair or too low by accepted industry standards. Suggestions have been made that consumers opting for a cash settlement could find their policies cancelled by the insurer after payout, and possibly experience difficulties finding another major insurer willing to provide cover, simply because they opted for a cash settlement rather than use a preferred repairer.

The SBDC is concerned that the risk of policy cancellation could adversely impact on consumers' willingness to exercise a right of choice (if available), and that the 'steering' of consumers to particular repairers through preferred repairer schemes could significantly affect the viability of other repairers performing high quality and cost competitive work, but who are not part of a preferred scheme.

The SBDC believes that this issue must be resolved within the context of ensuring selection criteria for preferred repairer schemes are transparent and accountable, and re-visiting the idea of incorporating appeal mechanisms for repairers, and/or the right to an independent vehicle assessment where the consumer and their non-preferred repairer dispute an insurer's pay-out figure.

### **3. Job pricing and hourly rates**

Repairers dispute claims by insurers that the hourly rate paid is not the predominant factor in determining the value of a particular repair job, rather they (insurers) accept quotes that reflect the total cost of repair taking into account all the relevant elements (paint, parts, specialist services). Repairers believe that when the total cost of repair is broken down, the only way to cost out the job is to use hourly rates.

Repairers are concerned that the hourly rate paid by insurers for jobs works out in most cases to be at a lower rate than that at which the repairer can sustain its workforce. They also believe that the systems used by insurers for estimating repair costs are not transparent and are consequently likely to be mistrusted by repairers.

In Western Australia, RAC Insurance has conceded that its hourly labour and paint rates are in need of a review. The Motor Trade Association of Western Australia (MTAWA) claims that insurers have not reviewed or offered hourly rate increases to repairers for ten years.

The Victorian Automobile Chamber of Commerce (VACC) body repair division claims that it has been 13 years since the last hourly rate rise, and that the

current rate of \$23 per hour conflicts with charge out rates of around \$120 per hour which repairers need to charge for 'private' work. Both the MTAWA and the VACC have expressed concerns that the low hourly rates paid by insurers can only lead to cost-cutting which will effectively mean putting dangerous cars back on the road.

The SBDC is not in a position to confirm the accuracy of assertions made by the MTAWA and the VACC about inadequate hourly rates but the issue is of major concern to the majority of small business repairers. The SBDC believes that the Productivity Commission should as a matter of priority undertake an analysis of hourly rates paid across the industry to determine whether small operators can remain economically viable. An assessment should also be made as to whether insurers are using hourly rates as a means of imposing further rationalisation on the industry by effectively forcing small firms to close their doors, irrespective of their efficiency or economic viability.

The SBDC believes that the problem of hourly rates could be partially addressed through the ACCC allowing collective negotiations by repairers, through their industry associations, and enshrining this 'right' in an industry code of conduct. It would not be feasible to try and establish one uniform hourly rate across the industry, however, as different cost structures would apply to particular insurers and repairers.

The SBDC believes that a collective negotiation process could be used to strengthen and enhance the quotation system across the industry. The current system of hourly rates used by insurers is inefficient because it effectively adopts a 'one size fits all' approach and ignores extra benefits that could be provided to customers (via the insurer) through additional, but more costly services such as:

- a priority repair system providing rapid repairs (for a premium or priority rate);
- more sophisticated (and expensive) equipment delivering higher quality finish on panel and paint repairs;
- 'valet' services for pick-up and return of customers' vehicles on a door-to-door basis;
- increased workshop capacity to undertake more repairs in the same timeframe; and
- guaranteed use of premium parts on high performance vehicles.

It would be more efficient, and more realistic, for the quotation system to be 'reformed' so that quotes actually specify total costs of parts, labour, paint, etc instead of just an hourly rate giving no indication of the range of services to be performed and the appropriate costs.

This measure would significantly strengthen the quotation system by adding much-needed transparency to the insurer/repairer relationship, particularly at the

assessor level. It would also serve to strengthen the position of small repairers who differentiate themselves from 'the pack' by offering better customer service through things like extra attention to detail, better quality control and more flexible customer service - albeit at a higher cost which would go unrecognized (and unrewarded) under an inflexible hourly rates approach.

The SBDC believes that the problems associated with the quotation system and hourly rates schedule must be addressed as a matter of priority because these issues are pivotal to the survival of the industry.

#### **4. Vehicle parts**

Repairers are increasingly concerned with insurers promoting the use of non-genuine or second hand (reconditioned) parts to lower the costs of repairs, without necessarily passing on these cost savings to customers through lower premiums. It is accepted in the industry that parts are one of the largest cost components in the repair process and the exclusive use of genuine parts increases the overall repair cost.

Repairers claim that there is little profit margin to be made on parts and the use of genuine parts is beneficial to the customer and ensures a quality repair job. Repairers also consider this issue is particularly significant when it comes to considerations of 'lifetime guarantees' offered on vehicle repairs.

The SBDC is aware that in recent years there has been a growing range of descriptions used for parts and insurers have specified the use of 'parallel parts', 'original equipment manufacture' (OEM), 'non-badged', 'non-genuine' and 'recycled' parts according to individual repair circumstances. From a repairer's perspective, at best the growing range of part descriptors is confusing. At worst, it represents attempts by insurers to circumvent panel beating by using cheaper, less reliable parts that compromise the repairers efficiency and integrity.

The SBDC believes that the Commission should examine the National Standard (AS 3905.11-1998 Quality system guidelines - guide to AS/NZS ISO 9002:1994 for the motor vehicle maintenance and repair industry) for repair of motor vehicles to determine if provisions relating to parts usage require amendment and updating. The amended Standard could be incorporated into an industry code of conduct to determine the appropriate use of parts by repairers in all circumstances.

#### **5. Lifetime guarantees on vehicle repairs**

Some insurers offer a life time guarantee for repair work on a vehicle, assuring policyholders that if the repair work is substandard the vehicle will be repaired again by:

- the original repairer; or

by another repairer for reasons of insurer preference, the original repairer is no longer in business or is unable to perform the work.

There is some confusion as to the meaning and obligations of a lifetime guarantee - is the guarantee for the lifetime of the repairer business, the insurance company or (logically) the customer's vehicle? (State legislation around Australia was required to determine this issue in relation to 'life memberships' in the fitness and health club industry so the issue is not trivial.)

Questions also arise about the effectiveness and enforceability of such guarantees when ownership of the vehicle is transferred - is the guarantee only for the length of ownership by the policyholder or does it continue with the new owner for the life of the vehicle?

Insurers claim that the guarantee is provided by the insurer to the policyholder. Repairers insist that any guarantee that is offered is supported by the repairer rather than the insurer, as it is the repairer who provides the work and who, in the first instance, is liable for any problems that may occur. Repairers believe that insurers unfairly gain kudos by holding out the benefit of a lifetime guarantee to consumers when in fact all the onus of honouring the guarantee falls on the repairer.

Repairers are also concerned that if a customer chooses to use a repairer who is not part of the preferred repairer scheme then the customer does not receive the lifetime guarantee from the insurer. This in itself has the capacity to create the impression amongst consumers that because the insurer is unwilling to guarantee the work, then the repairer must be deficient in some way and presents a disincentive for consumers to go outside the preferred scheme.

Repairers claim that it is an onerous burden to impose the liability of a lifetime guarantee upon the repairer responsible for the work when generally parts may only carry a 12 months guarantee and paint work two or three years (subject of course to implied conditions and warranties otherwise imposed under the provisions of the TPA).

The SBDC believes that it is essential for this issue to be clarified across the industry for practical commercial reasons as much as promoting viable working relationships between insurers and repairers.

## **6. Payment Terms**

Repairers claim that payment terms from insurers can be as long as 45 to 60 days, even longer if the repairer is not a member of a preferred repairer scheme. Delayed payments for repair work can impact adversely on the repairers' cash flow and its ability to ensure consumers have their car repaired and returned in a timely

manner. The viability of small repair businesses could easily be placed in jeopardy by insurers delaying payments, for whatever reasons.

The SBDC is aware that the VACC conducts regular surveys on payments to repairers by insurers. Recent surveys apparently indicated an emerging issue associated with delayed payments by insurers which conflicted with claims made by insurers that the majority of payments are made within 30 days.

While the SBDC is not able to verify repairers claims of late payments, it nevertheless believes that there is a pressing need to clarify payment terms across the industry and determine the reasons for any delays in payments for completed work. The SBDC would prefer to see this issue included in any proposed industry code of conduct as a matter of priority, particularly as many insurers now have the capacity to pay repairers by electronic funds transfer so there is no excuse for tardy payments.

The code should specify payment terms of no more than 30 days from satisfactory completion of repairs. This would allow the industry to re-establish itself on the right course after years of acrimonious exchanges between repairers and insurers, and would significantly benefit small repairers' cash flow positions. It would also go a considerable way to developing better and more harmonious commercial relationships between insurers and repairers.

## **7. Collective bargaining by repairers**

Repairers have previously sought to collectively negotiate with insurers on price, which placed them in danger of breaching the competition provisions of the TPA.

The Commonwealth Government recently introduced a Bill to implement the recommendations of the Dawson Committee Review of the Trade Practices Act allowing for a notification process to enable small businesses to engage in collective bargaining. (The Bill subsequently lapsed when Parliament was dissolved for the Federal election and will need to be reintroduced by the incoming government).

The SBDC believes that giving repairers the ability to collectively negotiate with insurers on issues such as paint and labour rates would assist in ensuring economic viability for small firms in the industry, particularly those that are part of the preferred repairer networks.

Accordingly, the SBDC recommends that the Commission urge the incoming Commonwealth Government to reintroduce the Bill as a priority in the next parliamentary session and to ensure that mechanisms are put in place to make all industry participants aware of procedures to access the collective bargaining process.

## 8. Codes of conduct

The SBDC believes that the way forward for the industry (insurers and repairers) to reach agreement on ways of providing for fair dealing and dispute resolution is most likely to be achieved through some form of national industry code of conduct.

The ACCC has also indicated that it supports any industry that attempts to develop mechanisms for industry self regulation providing that these do not result in any anti-competitive conduct or detriment to consumers.

There are a range of options that could be considered to address the issues including:

- a voluntary industry code of conduct between insurers and repairers;
- a mandatory code of conduct prescribed under the TPA between insurers and repairers; and
- corporate codes of conduct between individual insurers and repairers.

**Voluntary codes** can be effective, particularly if prescribed under the TPA, but their limitation is that they are only binding on those members of the industry that have formally subscribed to the code. In circumstances where some major players from both sides (insurers and repairers) elected not to be bound by the code, or a worst case scenario where major insurers declined to participate at all, a voluntary code would be ineffective. There are current indications that insurers are unlikely to subscribe to a voluntary code. The SBDC does not believe that a voluntary code could be effective for this industry.

### **Mandatory codes**

The SBDC believes that the mandatory Franchising Code of Conduct has been successful in addressing contentious issues in that industry, in particular the disclosure requirements and dispute resolution mechanisms. The Commonwealth Government implemented the mandatory code after a number of shortcomings in the voluntary code were identified and were unable to be resolved through that process.

The SBDC is aware that the Commonwealth Department of the Treasury, in its policy role, has previously indicated that the Federal Minister will only consider prescribing a code where:

- the code would remedy an identifiable market failure or promote a social policy objective;
- the code would be the most effective means of remedying the problem;
- the benefits associated with the code would outweigh any costs;

- there are significant and irremediable deficiencies in an existing self-regulatory regime; and
- other self-regulatory or quasi-regulatory options have been demonstrated to be ineffective.

The SBDC believes that the smash repair industry, as currently constituted, would satisfy the majority of these criteria.

Smash repairers have called for a mandatory industry code of conduct to regulate dealings between insurers and repairers. In response, the VACC prepared a draft industry code of conduct which repair groups would like to see mandated under section 51AD of the TPA. The SBDC believes that, taken as a whole, the VACC draft code could be a useful starting point for developing a code acceptable to both sides of the industry. The SBDC is, however, aware that insurers do not support the VACC draft code in particular and the push for a mandatory industry code generally.

The SBDC believes that there are a few significant sections of the VACC draft code that would require further discussion and negotiation with insurers to achieve the necessary degree of consensus for the code to be progressed. These are likely to be:

#### 5.5 Insurers

(a) Insurers must not unreasonably refuse a repairer an opportunity of quoting for repair work regardless of whether the repairer is an "accredited repairer" of that insurer.

(Insurers are likely to see this as undue interference in their claims processing procedures, and the 'thin end of the wedge' for their preferred repairer schemes, and consequently have resisted proposals to date).

(j) Insurers must ensure all assessors engaged by the insurer have successfully completed an Approved Assessor Course or have not less than five years full time experience as an assessor.

(Insurers are apparently concerned about the influence of repairer groups in structuring courses and issuing accreditation and consequently are unlikely to support such proposals without detailed discussion and amendments).

#### 6 Insurer accreditation of repairers

##### 6.5 Termination with no breach

Where a repairer is not in breach of an Accreditation Scheme agreement, an insurer may not terminate such agreement unless:

- (a) the insurer provides at least two years notice of its intention to terminate the agreement; or
- (b) the repairer consents in writing to terminate the agreement earlier.

(Insurers argue they require more flexibility to alter accreditation agreements to encompass new technology and changing market conditions and that two years notice is unreasonable).

#### 8 Policyholder choice

(b) A policyholder must be able to approve the repairer to perform a repair subject to the quotation procedure set out in Annexure 2.

(d) Insurers and repairers acknowledge that a policyholder must have the right at all times to discuss with an insurer and/or a repairer the repair work to be carried out on the policyholder's motor vehicle.

(Insurers do not recognise the policyholder as being a contractual party to the repair arrangements and argue that the majority of consumers want insurers to deal with repairers on their behalf).

These issues notwithstanding, the SBDC encourages the Productivity Commission to consider the VACC draft code as a starting point for frank and open discussion between all industry parties, preferably under the auspices of the ACCC's established Round Table process. If these issues of contention with the draft code, and any others, could be addressed first up by all parties, the proposed VACC code might become more acceptable to insurers as the basis of a national industry code.

#### **Corporate codes of conduct**

The SBDC is aware that some insurers have developed their own codes of conduct to deal with the relationship between themselves and repairers. Typically these codes have a number of features including:

- specification of standards;
- dispute resolution mechanism; and
- customer service guidelines.

Insurers therefore believe that these corporate codes preclude the need for an industry wide code of conduct. The SBDC, however, shares the concerns of repairer groups that the corporate codes which currently exist do not specify standards for repairers, have inadequate dispute resolution systems and fail to provide guidance on customer service. The ACCC believes the key features that would need to be incorporated as part of a corporate code of conduct to address industry concerns are:

- disclosure of terms, conditions and criteria for attaining preferred repairer status;

- regular discussions between insurers and repairers about emerging and current industry issues;
- establishing a dispute resolution mechanism available for all parties supplying services to insurers;
- appointment of an independent party to oversight dispute resolution; and
- clear specification of payment terms and remedies available for repairers that don't receive payment within specified time frames.

The SBDC does not support the development of corporate codes of conduct as a 'solution' to the problems in the industry because:

- corporate codes would necessarily vary between insurers and there would be no consistency for repairers dealing with more than one insurer;
- corporate codes are unlikely to include the key features identified as necessary by the ACCC; and
- it is unlikely there could ever be consensus on an industry basis for a multiplicity of codes developed by individual insurers for their own commercial objectives.

## **9. Redress for disputes between consumers and insurers**

The SBDC is aware that consumer organisations are concerned that consumers would be excluded from access to dispute resolution mechanisms incorporated into an industry code of conduct. Some sections of the repair industry also want consumers to be covered under an industry code of conduct, principally because it would support their contention that consumers have a contractual relationship with the repairer, as well as the insurer.

Insurers believe that a business to consumer code, the General Insurance Enquiries and Complaints (IEC) scheme established in 1993, already meets consumer requirements. As a national scheme, free to consumers, the IEC is aimed at resolving disputes between insured claimants and their insurance companies.

The SBDC believes that the IEC should be used by consumers to resolve concerns with insurers without the 'complication' of trying to bring consumers into an industry code of conduct - a course of action which would likely be opposed by insurers and further delay any chance of achieving industry consensus on a code.

At the same time, the SBDC sees merit in the ACCC's proposal that all industry parties should consider how this scheme could be extended to effectively deal with complaints and concerns raised by individual repairers, in the absence (to date) of an industry code of conduct. The ACCC considers the IEC could be

effective in resolving in a timely and efficient manner any issues arising between consumers and insurers relating to the consumers' choice of a particular repairer.

This would alleviate consumer concerns that have been raised previously regarding:

- access to quality smash repairers able to undertake timely and professional repairs;
- choice of repairer without penalty;
- dispute resolution procedures; and
- low and competitive insurance premiums.

## **10. Conclusion**

In conclusion the SBDC believes that, without ignoring the interests of consumers, the significant areas of contention in the smash repair industry concern the relationships between small businesses (repairers) and big businesses (insurers). These must be addressed quickly to ensure the smash repair industry remains viable - smash repairs performed efficiently, at a low (realistic) cost and with harmonious commercial relationships between insurers and individual repairers.

Smash repairers require assistance to achieve the following objectives across their industry:

- opportunities for all repairers meeting necessary standards to join preferred repairer schemes;
- non-discriminatory approaches by insurers to repairers that are not part of a preferred repairer scheme;
- comparable pricing rates for labour hours and paint work;
- payment to repairers within 30 days; and
- dispute resolution procedures that allow repairers quick access to an impartial decision making body.

The SBDC is convinced that the only way to achieve these objectives, and at the same time make certain insurers are able to maintain viable and harmonious relationships with repairers and consumers, is the development of a national industry code of conduct. The code must be mandatory and prescribed under the TPA. Only in this manner could the industry, which (in WA) has been unable to resolve its most contentious issues for 20 years, move forward.

The SBDC recognises that development of an industry code requires a bi-partisan approach and accordingly recommends that the ACCC be directed by the Commonwealth Government to resume its Round Table consultations and discussions with the industry to address outstanding issues.

The ACCC should take a proactive approach to discussions directed at development of a national code, ideally using the VACC model as a starting

point. There would be incentive for cooperation between industry participants because in the event that agreement is not reached, the ACCC could recommend government intervention by way of mandating an industry code that would be 'imposed' on the industry for the benefit of the community at large.

The SBDC appreciates the opportunity for input into the Commission's inquiry to date and looks forward to the release of the draft report and a chance for further comment later this year. Should you wish to discuss these issues further please contact Cassandra Bate, A/Director Policy and Business Liaison on 9220 0260.

MANAGING DIRECTOR

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