Productivity Commission Inquiry

Smash Repair and Insurance

Supplementary Submission in response to the Draft Report by

Allianz Australia Insurance Limited

Introduction

Allianz welcomes the Commission's assessment in its draft report of many of the issues raised by repairers in the vein hope that it might finally put to rest many of the unsubstantiated accusations and bad policy proposals advanced by the repair industry over many years. Examples of these include:

- claims of systematic late payments by insurers to repairers;
- that preferred repairer schemes compromise the safety of vehicle repairs;
- that preferred repairer schemes should be open to all comers;
- that there should be national criteria for access to preferred repairer schemes;
- the use of independent assessors or that assessors should be licensed;
- arguments against the legitimate use of recycled and aftermarket parts;
- the mandating of consumer choice of repairer;
- that consumers have been disadvantaged by restrictions on choice of repairer;
- the time allowed by insurers for repairers to consider preferred repairer contracts;
- repairers' advocacy of anti-steering legislation; and
- that there should be minimum, indexed rates for repair work.

Allianz supports the Commission's recommendation that insurers develop a voluntary code of practise to improve relations with repairers. However, an industry-wide code should form the basis of a framework that includes complementary corporate codes in order to establish an effective response to those legitimate issues raised by repairers.

Allianz is disappointed with the quality of some of the Commission's analysis around the source of concerns underpinning some of the issues raised by repairers and the reasons for a purported 'cost-price squeeze' facing repairers, particularly in relation to the issue of 'funny time, funny money' (FTFM). Allianz also regards the Commission's proposed 'real time, real money', alternative as impractical. That said, Allianz supports a process of consultation between insurers and repairers with a view to examining alternatives to FTFM. However, this will take some time and the development and introduction of an industry-wide code should not be bogged down and delayed by the inclusion of a proscription of FTFM in an industry-wide code.

Reducing tensions between repairers and insurers – making an industry-wide code work

Many of the allegations and proposals advanced by repairers have been found by the Commission to be wrong, unable to be substantiated or bad policy. However, no doubt they will continue to be pursued by repairers and rejected by insurers, ensuring that some level of tension will continue to exist between the industries into the future. Governments, like insurers, need to accept that, while ever repairers and/or their representatives continue to advance minority views, bad policy or baseless allegations, relations between the two industries will remain somewhat tense. For example, at the Commission's public hearings, Mr Ian Rolfe from MTA NSW commenting on IAG's introduction of a policy offering choice of repairer, stated:

> "I would have thought at the end of the day it may have been better to have waited till the outcome of the final report from the commission before introducing anything which was in fact going to probably again create problems in the relationship between the two parties."[1]

If a positive initiative on choice - an issue so dear to repairers' hearts - such as that implemented by IAG, is going to "create problems" in the relationship between repairers and insurers, the attitude of repairer representatives does not bode well for future relations between the two industries, regardless of insurers' response to the Commission's final report.

Allianz was also bemused by MTA NSW's comments on payment times where Mr Rolfe stated:

> "If we look at the payment times, our understanding would be in the main that the payment periods have been brought up to speed. Again, for whatever reason the point is they are no longer the concern that they were pre-Christmas at least in the circles that we're dealing with in New South Wales repairers."[2]

A similar suggestion was made by the Victorian Automobile Chamber of Commerce (VACC), where Mr Gunter Jurkschat said:

> "Terms of payment – we're not going to say too much other than to say if it hadn't been for an active public campaign we doubt very much whether some insurers would fall into place. There were very thankful they have."[3]

This contrasts with repairer bodies' initial submissions to the Commission in which the VACC stated that there was:

> "compelling evidence of a problem with late payments by insurance companies to crash repair businesses."[4]

---

[1] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.55.
[2] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.55.
[3] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Melbourne on Thursday, 3 February 2005, p.144.
[4] Victorian Automobile Chamber of Commerce, *Submission to the Productivity Commission Inquiry into The Relationship Between the Australian Motor Vehicle Smash Repair Industry and the Motor Vehicle Insurance Industry*, Volume 1 of 4, October 2004, p 37.

While the MTA ACT stated:

> "It seems from surveyed evidence of repairers that the payment of smash repairs by insurers continues to be a major source of economic hardship to repairers."[5]

It is laughable to suggest that there has been any change in the way insurers pay smash repairers between the end of 2004 and January 2005. It appears that an inability to provide evidence of a systematic problem in this area has led to a little re-writing of history by repairer bodies.

In relation to dispute resolution, Mr Rolfe from MTA NSW stated at the Commission's public hearings that:

> "I have not seen, as far as a dispute resolution, any insurer say that what we have is at arm's length. All dispute resolutions that insurers have are basically internal."[6]

This statement either represents an example of the common use of inaccurate generalisations by repairer representatives (which Allianz is often on the receiving end of) or demonstrates a staggering lack of knowledge of the industry by representatives that present themselves as experts on repair industry issues. Allianz has used the independent Australian Commercial Disputes Centre (ACDC) for external dispute resolution since the inception of its Network of Repairers some years ago. Moreover, with as much fanfare as we could muster, Allianz in late 2004 launched a code governing our relationship with non-network repairers which also included an external dispute resolution process using ACDC. It is worth noting, however, that Allianz has never had a dispute with a repairer that has required external dispute resolution.

On the issue of the qualifications of assessors and the need for licensing of assessors, repairer representatives made a number of statements. For example, Mr Greg Coli, consultant to MTA NSW stated:

> "I can honestly say, through 32 years' experience in this industry that, currently, most insurers who engage individuals who are licensed motor vehicle repairers … are probably less than 15 percent of their employees nationally."[7]

Other repairers and repairer representatives made similar claims.

This statement does not stand up to objective scrutiny. All Allianz' assessors have trade qualifications in motor vehicle repair. At the public hearings, Mr Arnold from AAMI stated, "We only employ qualified assessors who are ex-tradespersons".[8] Suncorp and IAG also spoke about the training undertaken by their assessors. Allianz sees no need for a licensing regime for assessors. We would also question the value of

---

[5] Motor Trades Association of the Australian Capital Territory, *Submission to the Productivity Commission Inquiry into The Relationship Between the Australian Motor Vehicle Smash Repair Industry and the Motor Vehicle Insurance Industry,* Volume 1 of 4, October 2004, p 13.
[6] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.64.
[7] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.72.
[8] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Melbourne on Thursday, 3 February 2005, p.176.

a licensing regime for repairers. The NSW regime does not appear to have resulted in better standards than other States. Repairer representatives pointed to the need to enforce repairers' compliance with OH&S and environmental regulations. Allianz suggests that this compliance should be enforced directly by the relevant OH&S and environmental agencies and is not sure why a repairer willing to breach these laws would comply with a license condition saying they should comply with them. The only potential value of a licensing regime would be a probity check that may assist in the reduction of fraud and rebirthing.

The repair industry's dire predictions about the profitability of its members need further scrutiny in light of recent data released by the Australian Bureau of Statistics (ABS). The ABS's most recent smash repair sector data (ABS Cat No. 81550.0) show the sector's profitability increased to 7.35 percent in 2002-03 (up from 5.37 percent in 2000-01) and that smash repairers are now more profitable than their counterparts in the motor vehicle retailing and services industry (2.32 percent profitability) and the Retail Trade sector in general (3.47 percent profitability).

These are just a few of the examples of the many unsubstantiated generalisations and accusations that insurers have been subject to by repairer bodies that are at best disingenuous and at worst simply dishonest.

However, Allianz' complaints about the tactics of repairer representatives should not be interpreted as meaning that we do not consider that there are some issues between insurers and repairers that need to be addressed. It has always been Allianz' observation that repairers have some legitimate, though different, issues with individual insurers. It is for this reason that, following the release of the ACCC's 2003 report on the relationship between insurers and repairers, Allianz moved quickly to develop a corporate code to govern our relationship with all repairers, which was tailored to the specific features of our business model. This code contained many of the features of the Commission's proposed voluntary industry code, as well as other issues on which repairers sought clarification, such as:

- transparency in regard to repairer choice;
- responsibility for guarantees;
- the use of parts;
- payment terms; and
- independent external dispute resolution.

Further, in relation to membership of Allianz' network of repairers, our existing service level agreements already addressed issues such as:

- responsibility for quality and safety; and
- independent external dispute resolution , including in relation to the termination or non-renewal of contracts.

In light of the Commission's focus on an industry-wide code, Allianz is still to be convinced that the Commission has correctly identified the precise nature of repairers' concerns, or at least how and where they arise, and hence what the nature of an effective response to them should be. For example, while the high-level issues may be industry-wide, the actual friction points are not. The points of real friction are more often found 'down' within the internal administrative, contractual and commercial relationships between repairers and individual insurers.

For example, some repairers concerns relate to their membership of insurers' network repairer schemes and the perceived fairness of the process or outcomes in relation to their ongoing status within a scheme, the way they are granted the right to repair a vehicle and the remuneration they receive from doing so. The nature and scale of repairers' concerns about these issues differ significantly between insurers depending on how insurers' different approaches impact on repairers. It remains Allianz' contention that only effective corporate codes, whether or not they exist within the overarching framework of a higher level industry-wide code, can effectively address issues at this level.

Allianz, possibly unfairly, described the Commission's proposed industry-wide code as 'hollow' because, on its own, it is unlikely to effectively address the legitimate concerns some repairers have with some insurers. However, on reflection, Allianz does acknowledge that the Commission's proposed code could usefully provide a framework for the content of more detailed and insurer-specific corporate codes. Allianz therefore supports the Commission's proposed voluntary industry-wide code. Allianz has always recognised the positive role that codes can play in advancing good relations between insurers and repairers, evidenced by the fact that we were the first insurer to put in place a code covering all repairers. Allianz has also never been averse to the principle of an industry-wide code in the context of an overall framework that recognised the crucial role that individual corporate codes need to play. Our strong opposition to an industry-wide code in the past was in the context of the code proposed by the Victorian Automobile Chamber of Commerce, which we regarded as highly intrusive, burdensome and anti-competitive.

Allianz sees the Commission's proposed code as something that, in combination with corporate codes, should be able to produce a consistent, comprehensive and effective solution to those legitimate concerns repairers may have. It will be important, however, that insurers' corporate codes and related processes genuinely seek to identify and address the areas of repairer concern that result from the specific administrative, contractual and commercial interactions that arise from each insurer's unique approach to dealing with repairers.

In their submissions on the Commission's draft report and at the public hearings, repairers and their representatives called on the Commission to move straight to a mandatory code, bypassing the option of a voluntary code. In this context, it was stated by Mr Rolfe of MTA NSW, that: "I don't believe that either side of the industry would adhere to a voluntary code."[9] In response, Allianz would say that the Commission's proposed code contains various obligations on insurers. Allianz does

[9] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.65.

not see the need for a voluntary code to contain any obligations on repairers, hence, the adherence (or lack of it) by repairers to a code is not a relevant consideration. For Allianz' part, we would categorically commit to a voluntary industry code that we had signed up to.

In terms of the timeframe for the development of a code, repairer bodies such as the MTAA have argued that the:

> "deadline for the finalisation of negotiations should be 30 September with a commencement date of 1 January 2006. Otherwise, a code should be mandated."[10]

Allianz regards such a timeframe as impractical. As submissions on the draft report and the public hearings have highlighted, insurers and repairers still disagree on fundamental issues in relation to the content of a code (eg, whether choice should be mandated) and even whether the code itself should be voluntary or mandatory. Stakeholders will not know the outcome of the Commission's deliberations on these and other questions until its report is publicly released and the Government's response is known. Allianz understands that the deadline for release of Commission reports is 20 Parliamentary sitting days following the provision of the report to the Government, which in this case is 31 March. On this timetable, the necessary clarity around key issues in relation to a code may not be known until as late as early August.

In light of our closer examination of the Parliamentary sitting schedule, Allianz retracts its statement at the public hearings that a code should be able to be finalised by the end of 2005. Moreover, in light of the Insurance Council of Australia's comments at the Melbourne hearings on the need for a consultative process with all stakeholders, it would take a period of around 12 months to finalise a code. On this basis, Allianz suggests that the earliest time in which a code could be expected to be finalised would be 1 July 2006, with implementation over a reasonable period after that to allow time for insurers to ensure that their corporate codes and other supporting processes and documentation complied with the code. In these circumstances, a commencement date of 1 January 2007 would be achievable. If this code is to address the decades of tension between to two industries, it has to be done properly; it cannot be rushed.

Funny time, funny money

General comments

In Allianz' view, the Commission's analysis of the issues surrounding FTFM is deficient. The Commission's draft report suggests that 70 percent of the industry uses FTFM and that it is largely responsible for a "cost-price squeeze" being experienced by repairers. However, the more important issue when considering whether or not a pricing model like FTFM places unfair financial pressure on repairers is not simply whether FTFM is a part of the process but what it is used for, as well how it fits within an insurer's overall approach to its preferred smash repairer (PSR) scheme.

---

[10] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Melbourne on Thursday, 3 February 2005, p.131.

In the case of some insurers, it is the competitive process used to win work that determines whether the repairer gets a job or not. Competitive tendering for repairs may be against other repairers on a car-by-car basis. In other cases, repairers may be effectively competing against themselves over time through performance monitoring of their average repair costs, or against other repairers in terms of their relative average repair costs. Under these arrangements, repairers know that they must provide a competitive quote to win the right to repair a vehicle or to retain their current status within a preferred repairer scheme in order to continue to be offered vehicles or the same volume of vehicles in terms of number or damage-type.

After assessing the bottom line price a repairer thinks it needs to win a job or retain their current preferred status, a repairer working under such arrangements may be required to write up a quote using the FTFM approach. However, it is more likely the competitive quoting process itself that may drive some repairers to lodge quotes that they themselves know will not fully cover their costs and which may 'squeeze' them financially. This result will occur regardless of whether the repairer is required to prepare the quote using FTFM or real time, real money or whether they quote a bottom line figure, without detailing the model they used to arrive at their price. The pricing model used to write up the details of a quote in a competitive tendering environment is irrelevant. This is evidenced by the fact that some insurers only require the repairer to provide a bottom line price, being uninterested in how the repairer arrived at the price, for example, in terms of the numbers of hours to be worked and that hourly rate for that work. This conceptualisation of the use of FTFM in a competitive tendering environment appeared to by supported by IAG at the Commission's public hearings, where Mr Rick Jackson stated:

> "'Funny money, funny times.' We believe this issue is a moot issue, that the overall cost of repair – which includes procurement of parts, the efficiency of the repairer and the overall end price – is the real issue that we wish to buy on."[11]

Mr Paul Pemberton from IAG expressed similar sentiments:

> "I think the new methods that we've evolved, and that others have evolved, in the industry go more towards total price, and a competitive position on total price means that, generally speaking, if you're a well-qualified, quality repairer you'll get the job if you have a lower price."[12]

These comments appear to suggest that, even though IAG's PSR and ASR agreements contain a "funny" hourly rate, and their repairers are required to prepare a detailed quote using FTFM, they are working within a competitive tendering environment where the overall bottom line price is the key determinant of the outcome. Allianz' taxonomy of the use of FTFM seemed to be further supported by Mr Pemberton's "Yes, indeed." at the Sydney hearings in answer to Commissioner Fitzgerald's question "If you're moving to that system, it's a wholly competitive system, and you, implicitly, by that have moved away from 'funny time, funny money'?"

---

[11] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.6.
[12] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.15.

In Allianz' case, with an unrestricted choice of repairer, all repairers that prepare a quote do so in the certain knowledge that they will be carrying out the repair. They do not have to compete with other repairers in order to win work from Allianz. This arguably puts repairers in a better negotiating position than a competitive process where there is no certainty that they will get work, either in a particular instance or in terms of the future availability of work flowing from their status in a preferred repairer scheme. Moving to web-based tendering systems where many more than a few repairers will have the opportunity to tender for a particular job will likely only increase the competitive nature of the process.

In a question to the VACC, Commissioner Fitzgerald alluded to the balance of negotiating power in a choice environment, which remains a feature of the Allianz approach, asking:

> "It's been put to us during the inquiry that really what's occurred is that a decade or so ago this was an industry controlled by the repairers and that was largely because of unrestricted choice by consumer and their relationship with the repairer and we've now moved, some would say, to a situation where it's an industry controlled by the insurers. … Do you think it's a fair characterisation that that's what's been occurring?"[13]

While Allianz would disagree with the generalisation contained in the second half of the characterisation as it applies to us, we note the response by Mr Howes of the VACC, who stated:

> "Yes, and I think there's probably, in some ways, a justification by the insurers from the action that they have done in that regard, but the real progress from the insurer's point of view in controlling the market has been this fundamental change of directing the customer, the insured, to their repair network."[14]

Allianz points out to the Commission that the "real progress from the insurer's point of view in controlling the market" is not applicable to Allianz given our policy of unrestricted choice.

Mr Howes' colleague, Mr Jurkschat, on the other hand, appears to disagree with this characterisation, stating:

> "Perhaps this would be a good time to debunk that particular myth, by some insurers anyway, that the PSR schemes have in some magical way improved efficiencies and … reduced the cost of repairs … There is absolutely no proof."[15]

However, Mr Jurkschat would only need seek the views of repairers on this issue in order to obtain the proof that alludes him. For example, referring to insurers that do not offer choice, Mr Bova from Parraweena Smash Repairs, stated:

> "They seem, with the preferred repairers, a lot stricter on cost cutting than for non-preferred repairers. They seem to go to their repair shops more frequently and check their quotation, make sure they're keeping their costs down."[16]

---

[13] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Melbourne on Thursday, 3 February 2005, p.133.
[14] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Melbourne on Thursday, 3 February 2005, p.133.
[15] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Melbourne on Thursday, 3 February 2005, p.137.

In response to a question from Commissioner Fitzgerald about his concerns about becoming a preferred smash repairer, Mr Bova said “the bottom line and the profit margin will come down”.[17]

Mr Elmassian from the Australian Automotive Repairers Association said:

> “They control the consumer. … Let me tell you over 40 percent of our members are preferred repairers. They’re saying, “We can’t take these squeezes any more. We cannot do it any more.
>
> They walk in every three to six months, ask for a 5 per cent decrease and if you don’t get that 5 per cent decrease, the tap stops, you’ve got no work for the next month. You then have no choice but just to do it at a very, very discounted rate.” … I’ll say two of the other insurance companies [Allianz and Suncorp] said, “Look, we see a problem in this. Let’s see how we can work with you.”[18]

Allianz does not condone the use of PSR arrangements as a way of placing undue financial pressure on repairers, as alluded to by Mr Elmassian. We are not even convinced that the plight of repairers is, as a generality, as bad as some repairers and their representatives claim, particularly in light of the most recent profit data on the sector from the ABS. What these comments do demonstrate however is that, at least on the face of it, there appears to be a disconnect between the experience of repairers and the rhetoric of some of their representatives.

A number of participants in the Commission’s public hearings provided repairer perspectives on Allianz’ approach to negotiations (including its use of FTFM) which is at odds with the underlying theme in the Commission’s draft report that FTFM, and particularly Allianz’ characterisation of its use, is a key factor in the financial difficulties faced by some repairers.

Mr John Howes, a member of the Body Repair Division of the VACC and vice-chairman of the Australian Motor Body Repairers Association, said:

> “The only truly honest system that works in this system at the moment is the Allianz system, [the] managed repair process...”[19]

Mr George Elmassian, from the Australian Automotive Repairers Association, stated:

> “…I guess one difference between Suncorp and Allianz is that assessors actually come out and talk to you and they do negotiate a price with you. So putting “funny time, funny money” to one side, at the end of the day you do actually negotiate a price… At the end of the day you come up with a bottom line that you’re happy with.”[20]

---

[16] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.95.
[17] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.96.
[18] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.87.
[19] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Melbourne on Thursday, 3 February 2005, p.154.
[20] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.83.

At the public hearings, Associate Commissioner Rendall, questioned the VACC on the nature of the negotiation process between a repairer and an insurer, like Allianz, that offers choice. Mr Rendall asked:

> "… if an insurer insures my car and I say, "I want Fred and Bill Smash Repairs to repair … and then Fred and Bill can't agree or this insurance company … cannot agree as to pricing, what happens at that point, where I have the absolute choice to choose."[21]

Highlighting the fair outcomes produced by the 'single quote' negotiation process in these circumstances (despite the use of FTFM!), Mr Jurkschat from the VACC said:

> "I don't think we've actually found that position.
> …
> … I think we've not come across the situation where that's happened because in the end an arrangement always seems to be made between the assessor and the [repairer]. We don't know of any situation where they've been so far apart they can't come to an agreement and I think that is the other issue. It's not as though the insurance company doesn't have a role to play when there's choice. In fact they still have a role to play and we have companies like Allianz who have their particular method where there is a very involved process. So I think for us that's not a problem, we don't see that as a problem because it just simply doesn't raise its head often enough."[22]

Describing Allianz' process, Mr Frank Bova from Parraweena Smash Repairs, said:

"Allianz is just, really, an assessment is booked in, Allianz will come to our workshop and negotiation between the assessor and our quotation, and that's basically it."[23]

In response to Commissioner Fitzgerald's question:

> "In terms of the jobs that are being quoted, do you believe there would be a significant difference in the price you charge depending on which insurance company your dealing with…",[24]

Mr Bova said:

> "Allianz, GIO, we quote the same… we work on the MTA rate, the MTA book, so they're basically the same. We look at a job and we quote those two jobs… With NRMA, its different because they've got an NRMA times manual … So generally their quote is a lot, lot less."[25]

---

[21] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Melbourne on Thursday, 3 February 2005, p.132.
[22] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Melbourne on Thursday, 3 February 2005, p.132.
[23] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.94.
[24] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.97.
[25] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.97.

Commenting further on how the processes operated by different insurers impact on repairers with particular reference to the different outcome when dealing with insurers (such as Allianz and Suncorp/GIO) that use FTFM in the context of a 'one quote' system , Mr Bova said:

> "If your squeezed, you know you have to make a living. You know you have to make a profit. If the price is getting cut, you will have to cut corners. You have to. In our shop we quote a job and we negotiate with the [Allianz and GIO] assessors. As I said, we're not a preferred repairer, so we don't get intimidated as much, because we don't have to go with the blue, the gold, the red status. We're not on a performance plan. But we're virtually quoting our jobs and then negotiation with the assessor, and we will communicate with the assessor and look at it and go over the job."[26]

Also relevant to these considerations is the views expressed by Gerry Raleigh from Kerry Panels at the Sydney hearings. He appears to lament the demise of FTFM as traditionally used to negotiate an agreed outcome with repairers, stating:

> "… funny money, funny times is a thing of the past. Its dead; it died a slow death … There is no such thing as funny money, funny times, especially with PSRs. It is gone."[27]

Allianz would argue therefore that FTFM is really only used as a mechanism for determining price in the case of insurers that offer unrestricted choice of repairer and, in this regard, the claim that 70 percent of the market uses FTFM is misleading. The market share of insurers using FTFM as a mechanism to arrive at a repair price, that is, those that offer choice of repairer, is more likely to be less than 30 percent. It is difficult therefore to reconcile this fact with the Commission's finding that repairers have been subject to a cost-price squeeze as a result of FTFM, particularly when most of the criticisms of repairers are directed at insurers that do not offer unrestricted choice of repairer.

None of this is to suggest that Allianz has any objections to the use of competitive quoting by other insurers or that the Commission should recommend any changes to it. Having said that, Allianz does regard competitive quoting as a model more likely to cause tensions between insurers and repairers and between repairers themselves and this is the primary reason we abandoned it in favour of our unrestricted choice of repairer and Managed Repair Process. The main point we wish to make is that we do not agree that FTFM is used by 70 percent of the market in the way the Commission suggests. Nor does Allianz agree that the financial pressure some repairers find themselves under is the result of a cost-price squeeze created by FTFM. Allianz simply contends that the market for repair work is highly competitive and in any industry there is a spectrum of participants ranging from the highly efficient and profitable to the inefficient and unprofitable. The latter group will be under financial pressure and unless they can improve their efficiency and profitability they will experience the hardship associated with a struggling business.

[26] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.100.
[27] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Melbourne on Thursday, 3 February 2005, p.194.

Commission criticisms of FTFM

The Commission makes a number of criticisms of FTFM. Some of these and Allianz response to them is set out below.

"it does not reflect the particular costs faced by individual repairers"

This comment highlights a misunderstanding about what FTFM is. When used to determine a price with a repairer that knows they will be doing the job, FTFM is simply a basis for negotiation that uses well-known and understood parameters. In simple terms, the price model comprises two parameters:

- a unit rate,
  - which some repairers and their representatives disingenuously refer to as an hourly rate so they can compare it to 'real' hourly rates used in other industries as 'proof' they are being underpaid by insurers. The rates used by insurers, as the Commission is aware, bear no resemblance to hourly rates and as such Allianz would argue are more correctly referred to as a 'unit' rate[28]; and
- a multiple of the unit rate.

The unit rate is fixed and, in Allianz' case, the repairer and the assessor then negotiate the size of the multiple in order to reach a final figure that is acceptable to both parties. As a negotiating tool, FTFM in these circumstances reflects the particular costs faced by individual repairers as a result of the negotiation around the multiple. For example, all things being equal, the multiples agreed in inner-metropolitan repair shops are generally higher than those agreed in outer-metropolitan or non-metropolitan areas to reflect differences in costs, in particular, rent and wages.

Allianz would argue therefore that using a negotiated price model, such as FTFM, is at least as capable of reflecting the particular costs faced by individual repairers as a competitive tendering approach. Indeed, FTFM may be more reflective than competitive tendering, particularly with the advent of remote tendering technologies, such as the Internet, which allows outer-metropolitan repairers who have the benefit of lower overheads to compete with inner-metropolitan repairers that are subject to higher costs for some inputs.

There is clearly confusion among some stakeholders about the relationship between current unit rates and hourly rates for repair. One option is to raise unit rates to something akin to the hourly rates used in other trades. However, if this was "adjusted as appropriate from time to time" (eg indexed to some inflation or business cost index) as suggested by the Commission, the only way insurers could share the benefits of productivity gains made by repairers would be to extract it through

[28] Allianz generally uses the terminology of 'unit' rates for internal purposes. The term 'hourly' rate was used in our main submission to the Commission to avoid confusion. On reflection, this was a mistake because it seemingly only created confusion as to the true nature of the FTFM pricing model as used by Allianz and other insurers using the so-called "one quote" model (ie those that offer unrestricted choice of repairer).

reductions in the number of hours allowed. In other words, a reintroduction of funny time, albeit artificially low rather than artificially high. This is not an approach Allianz finds attractive. As a hypothetical exercise, Allianz would be interested in the Commission's view on the acceptability of moving to a unit rate of $10, with an appropriate adjustment to multiples. One benefit of this approach is that it would dispel any myths or confusion that the unit rates used by insurers bear any relationship to hourly rates.

The attractiveness of the unit rate/multiple approach to quoting is that it retains the ability of Allianz to remunerate repairers more generously for repair work than for R&R work, providing a positive incentive to undertake less expensive repairs where appropriate. As indicated in our initial submission, Allianz holds to the view that paying the same unit rate in circumstances where real times exist for both repair and R&R will eliminate this incentive effect, resulting in a higher level of parts replacement and consequently higher costs. The higher costs involved with parts was acknowledged at the Commission's public hearings by Greg Henson from Callaghan Collision Centre, who stated:

> "… if you were to supply a new part. There is extra R and R components possibly, and extra paint operations that may need to be done versus repair. That is obviously always taken into consideration on the repair versus the replace."[29]

It should be noted that Mr Henson made these statements in support of his disagreement with the contention that "more parts would be supplied to the repair if the allowance was increased". However, importantly, the "repair versus replace" equation repairers currently consider is one where their remuneration from replacement is artificially low (because low "funny money" is linked to relatively low "real" times from an MTA manual) and their remuneration for repair is artificially high (ie "funny time").

The behavioural incentives created by this remuneration differential reduce the overall cost of repairs for Allianz by reducing the unnecessary use, where appropriate, of expensive parts (and consequent additional R&R and paint costs). Moreover, the artificially high 'repair' remuneration compensates for the artificially low 'replace' remuneration to provide a fair and reasonable overall level of remuneration to repairers under Allianz' approach. Allianz contends that, by changing the "repair/replace" equation facing repairers, a strict "real time, real money" approach would remove the current behavioural incentives that minimise repair costs. It is for this reason any moves away from FTFM need to be carefully considered and assessed, including through the use of pilots to analyse the impact of alternatives.

"the structure of the repair task becomes biased, with the FTFM system artificially inflating or deflating particular cost elements at the expense of others"

As discussed above, it is true that the FTFM price model is one that creates a bias towards the repair of damaged parts where possible and appropriate and away from the more expensive replacement of parts. Allianz provided detailed analysis in our primary submission to highlight this point. Another main conclusion from our

---

[29] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.115.

analysis of the incentives created by FTFM was that it resulted in lower average repair costs. Given that minimising costs is the primary objective and outcome of the competitive tendering model, one would expect a similar 'bias' in favour of repair over replacement of parts to be a feature of competitive pricing models as well. Allianz sees no detriment in an arrangement that provides a bias towards lower average repair costs, particularly in light of the information we have provided that indicates that the alternative (ie real time, real money) would only disadvantage repairers by increasing the proportion of vehicles that are written-off, with a corresponding reduction in the amount of repairable vehicles available to repairers.

"the bottom line is likely to be depressed below 'true' costs"

Allianz is mystified by this comment and seeks further elaboration and explanation from the Commission as to what represents 'true' costs and the evidence the Commission has to substantiate this statement. It is presumed that the Commission is of the view that competitive tendering models are able to correctly identify 'true' cost given that the Commission does not make a similar criticism of such models. The key part of this evidence would be data showing that FTFM produced average repair costs that are consistently and appreciably below those produced by competitive tendering models. Allianz would be interested in repairers views on this matter and whether they concur with the Commission on this point.

Of course, most insurers would probably assert that they have the business model that produces the lowest average repair costs. While various factors impact on the premium for any particular risk, repair costs represent the overwhelming majority of motor insurance claims costs and hence premiums. Thus, one indicative measure of the relative repair costs of insurers would be data on premiums. Allianz notes the results of a recent study conducted by JPMorgan[30], which found that "AAMI is the most price competitive insurer followed by IAG" (p1) and that "Promina [ie AAMI] and IAG are clearly far more price competitive than the other players in the market..." (p2).

On the face of it, this suggests that the insurers using restricted repairer choice/competitive tendering models have lower repair costs than those using unrestricted repairer choice, FTFM pricing models. This is at odds with the Commission's conclusion that FTFM pricing depresses repairers' bottom line below true cost and that the main cause of any cost-price squeeze experienced by repairers is the use of FTFM to price repair work.

"as a system of 'ambit claim', it is subject to manipulation by both insurers and repairers, with the latter especially vulnerable"

Whether it is for the purchase of shares in a takeover of a listed company, a house or an item at a garage sale, ambit offers are a common feature of many negotiation processes. It is no different in principle to a negotiation between an insurance company assessor and a repairer using the FTFM model. In light of this, Allianz is not sure of the substance of the Commission's criticism in its description of the FTFM pricing model as "a system of 'ambit claim'", nor how it is subject to manipulation,

[30] JPMorgan, *Motor Insurance Industry, Patterns and pricing: it pays to shop around*, 2004

unless that is simply a reference to the subsequent negotiation towards a mutually agreed outcome. It is important to remember that when being used to agree a price, a negotiation within the FTFM framework is being conducted by two parties with a good understanding of, and experience in, its use. As to the vulnerability of one or the other of the parties, the information asymmetry in relation to the time to undertake repairs generally works in favour of repairers. Moreover, in an unrestricted choice of repairer environment the repairer is effectively negotiating from the position of a monopolist because they know they are the only one who will be offered the opportunity to repair the vehicle. Allianz therefore questions the Commission’s conclusion that it is repairers that are especially vulnerable in a negotiation using the FTFM pricing model.

“The implication of Allianz’s comments is that FTFM inherently acts to depress the bottom line – that is, it may be systematically generating quotes that understate to true costs of repair”

The relevant Allianz comment referred to by the Commission would appear to be the following:

> “Allianz claimed the following benefits of FTFM:
>
> …
>
> - a reduction in the overall costs of repair – Allianz said that in its experience ‘average repair costs are considerably higher in countries that have adopted a “real time, real money” approach’” (p74).

Allianz would argue that the conclusions drawn by the Commission based on this and related information appear to arise from a deficient analysis and understanding of the material Allianz provided in its submission. In the first instance, it is not at all clear what “bottom line” the Commission is referring to in its comments. Allianz provided analysis that demonstrated that the FTFM pricing model reduces the costs of repair compared to the use of a real time, real money approach. However, our analysis also showed that this resulted in a higher level of remuneration, or ‘bottom line’ for repairers. The reduction in repair costs under FTFM was entirely the result of a reduction in the use of expensive replacement parts in favour of the lower cost repair of damaged parts. The only party potentially suffering a reduced bottom line out of this process would appear to be parts manufacturers.

It is unclear on what basis the Commission makes the statement that FTFM “may be systematically generating costs that understate the true costs of repair”. Apart from providing no evidence or analysis to support this claim, the Commission does not even offer a definition or explanation of what these “true” costs are or how they are determined. It would also be helpful if the Commission could provide further information on the relationship, if any, between its concepts of the “true costs of repair” and the “bottom line”.

Confusion on this point is not restricted to the Commission. In its presentation at the Commission’s public hearings Mr Rolfe of NSW MTA stated:

> “In one breath, we have Allianz saying *the cost of repairs will go down*. In other words, the repairer will make less money on a “real time, real money” scenario than they will on the

> current "funny time, funny money" system. I would find it strange than any insurer would not jump at the chance to take on a program that would save them money."[31] (emphasis added)

This comment demonstrates a total confusion between the concepts of cost of repairs and remuneration to repairers, as well as a lack of comprehension of what Allianz said, both in its presentation at the public hearings and our submission. In fact, Allianz stated that it was concerned that the cost of repairs would go *up*, rather than down, if a move to "real time, real money" disturbed the current incentive to repair rather than replace damaged parts where appropriate. This is due to higher costs associated with the purchase of parts and related additional R&R and paint costs. Analysis in our initial submission also suggested that repairers would receive less remuneration overall due to the lower overall number of hours that could flow from doing less repair work and, in the medium, term less work overall due to a higher rate of write-offs.

Allianz also points to the fundamental flaw in the logic of repairer representatives on the issue of FTFM. On the one hand, it is argued that rates have not been adjusted for ten years (Allianz has increased its rates a number of times over this period by the way), are too low and they need to move to a "real" hourly rate because repairers are unprofitable at current levels of remuneration. On the other hand, it is argued that the bottom line will not change (eg, Mr Coli stated "But if you look at the bottom line, it's 10 hours at 30 [dollars] or three hours at 100 [dollars][32]). It is not clear to Allianz how a move to "real time, real money" can improve the lot of repairers if the bottom line cost to insurers does not change.

"problems with the accuracy of times manuals"

The Commission reported that one "common claim" of repairers was that " the current times manuals contain large inconsistencies and errors" (p72). For Allianz' part, we use the MTA guides developed by repairers themselves. To the extent that these contain inconsistencies and errors, this would appear to be the responsibility of repairers themselves rather than insurers.

The Commission's proposed 'real time, real money' alternative

The Commission's proposed alternative to FTFM is unwieldy and impractical.
The Commission suggests that "times and hourly rates … should reflect realistic times and rates applicable to both the particular job and particular repairer" (Draft Report, p75) but that this quoting arrangement would "differ from the standardised 'real time, real money' model suggested by some repairers" (p76). It is not entirely clear what the difference between "realistic" and "real" times and rates is. Possibly the Commission did not intend to infer any difference, clarification on this point would be useful.

The key difference the Commission appears to be pointing to is whether or not these rates should be standardised, with its recommendation that rates be applicable to "the

[31] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.58.
[32] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.77.

particular job and particular repairer". In support of this, the Commission quotes the MTA of Queensland's concern that the difficulty with a (presumably standardised) real time, real money approach would be that "different repair shops have a different hourly operating cost that could not be applied equitably to the entire industry" (p76).

Thus, the Commission seems to be suggesting that each insurer develop a different hourly rate for each of the 5000 repairers in Australia. Of course, these 5000 individual shop rates also have to be "adjusted as appropriate from time to time" (pXXI). It is not clear how insurers would be able to share in any productivity gains repairers may achieve under this apparent automatic indexation of rates. But assuming the Commission is not arguing that insurers should not share in such gains, presumably different indexation rates would have to be developed for each repairer, given that productivity improvements will vary among repairers due to differences in the timing and scale of any introduction of productivity improving technologies and practices.

The most concerning implication of the Commission's alternative pricing model is that it appears to support the idea that insurers pay higher rates to less efficient repairers (to reflect their higher costs) than they do to more efficient repairers. In Allianz' view, this would effectively encourage inefficiency and reduce the incentives for repairers to invest in productivity improvements in order to reduce costs. Noting that, under the Commission's proposal, insurers should respond to any reduction in costs with a corresponding reduction in the hourly rate paid. This, according to the Commission, "would enhance effective competition between repairers" (pXX). Allianz fails to see how competition between repairers would be enhanced under the Commission's proposal and would certainly welcome more evidence and analysis in support of this contention in its final report.

When used by insurers like Allianz that offer an unrestricted choice of repairer, FTFM is simply a mechanism to negotiate an outcome with a repairer who is effectively a monopoly seller of a service because the exercise of our customer's choice means they are the only one who can carry out the repair in question. Ironically, as simply a negotiation tool, the FTFM model already has the flexibility to tailor payments to provide an acceptable and agreed level of remuneration to individual repairers.

It is more than likely that the Commission's proposal would lead to standard times for all aspects of repair. This is precisely how 'real time' systems used in other countries (eg Thatcham times) work. And with times standardised, while rates may vary between insurers, they are unlikely to vary much. Why would they? With times standardised, any insurer that paid 'above market' rates would simply increase its average repair costs relative to its competitors. The likely result therefore would be a move towards "an industry standard hourly rate" and "industry standard hours for particular tasks" – a notion the Commission rejects. While the Commission states that there was "no justification for regulating" such an outcome, it would probably be the natural market response to the Commission's attempt to force insurers that do not use competitive tendering down a 'real time, real money' track.

The other potential response by insurers that use FTFM as a price negotiation model to the Commission's alternative would be to abandon a model the requires quotes to be negotiated directly with repairers, in other words, the adoption of a competitive tendering model. This would have a detrimental impact on the availability of choice of repairer. As Allianz outlined in its primary submission, unrestricted choice of repairer and competitive tendering are mutually exclusive because an insurer cannot guarantee that their customer's chosen repairer will provide the most competitive quote. As a result, the customer's choice cannot be guaranteed and hence an insurer cannot offer choice of repairer.

Moving forward from FTFM

Despite our view that FTFM works fairly and effectively in the context of its use by Allianz - a view that many individual repairers report to us they share, despite the stance adopted by repairer representatives - we agree that it has problems in terms of transparency, albeit mainly for those not involved in the insurance and repair industry and experienced in its operation. This lack of transparency also clearly allows repairers to make disingenuous claims to governments and others about its ability to provide fair levels of remuneration to repairers through a focus on the unit rate alone. On this point, Allianz welcomes the Commission's acknowledgement that " the adequacy of payment cannot be determined from hourly rates alone" (Draft Report, pXX). It may well be, however, that the lack of transparency of FTFM does not meet modern standards and expectations and has had its day. Although we would agree with Mr Rolfe of MTA NSW, who stated at the Commission's hearings that FTFM "has served the industry reasonably well for 30-odd years."[33]

There may be alternatives to FTFM, however, they will not be developed and introduced overnight. The understanding of FTFM by repairers and insurers is based on more than a generation of its use. Any move into the unknown of a poorly thought through and untried alternative could be highly disruptive to both insurers and repairers. A highly possible outcome of such a proposal would be a move by most if not all insurers to a bottom line, competitive tendering model that does not need to rely on FTFM (or any other price negotiation tool). This would also probably see the demise of unrestricted choice of repairer being offered by insurers given the incompatibility of this with competitive tendering. Allianz doubts this would be in the interests of repairers or consumers.

A number of participants in the Commission's public hearings highlighted the difficulties of moving hastily to implement alternatives to FTFM. For example, Mr Tim Jeffcoat said:

> "Suncorp would like to stress to the commission the complexities involved in dismantling the "funny time, funny money" system … There are high risks for all parties including repairers. Therefore any move to dismantle the system must be done very carefully and will take considerable time to do properly."[34]

---

[33] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.77.
[34] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.42.

Even Mr Coli, consultant to MTA NSW, acknowledged:

> "There will be a learning curve for both sides of the industry, to revert back to what we used to do, because this is what we used to do 30 years ago."[35]

Unlike some commentators, who seem to take a simplistic and impractical approach to the issue of moving away from FTFM, Mr Michael Schumak from Maroubra Automotives acknowledged the practical realities of trying to assess repair times in advance, which FTFM in part addresses, and the difficulty associated with change, stating:

> "I am not one that's particularly against a certain "funny money, funny hours" … I believe today's rate should be around about $50 to $55 an hour, and still be subbed by "funny money", because if you go to "true money, true hours" it's just so difficult, because the insurance companies aren't going to trust the repairers. It's very difficult."[36]

That said, however, Allianz is not attracted to Mr Schumak's proposed alternative, encapsulated in his statement:

> "If there's some sort of price fixing, that they [insurers] all pay us the same money, I don't thing you'd have an issue."[37]

In terms of moving away from FTFM, Allianz draws the Commission's attention to the Government's intention to amend s46 of the Trade Practices Act to allow small business to collectively negotiate with large businesses. In this environment, repairers could orchestrate a move from FTFM by collectively negotiating what they would consider to be 'real rates'. To maintain existing repair costs, insurers using FTFM would then be forced to move to 'real times' in response. In other words, imminent legislative changes may provide an environment that could see the demise of FTFM through market forces. This obviates the need for the Commission to take an interventionist approach in terms of forcing the cessation of FTFM.

If nothing else, Allianz would hope that the discussion of the issues on FTFM in this submission convinces the Commission that the issues surrounding the use of and alternatives to FTFM are complex. They certainly do not lend themselves to a simplistic recommendation that "FTFM be abandoned". Allianz would agree fully with the VACC's comments in this context, where Mr Jurkschat stated:

> "VACC would agree that the current practice of funny money and funny times is perhaps not conducive to having an open and transparent quotation system. Notwithstanding that, I think it should be acknowledged that there are many crash repairers, assessors, independent assessors and even insurers who see this as the only way to go forward, even with its flaws. It has been the practice in this industry for so long that there's some fear and trepidation about moving away from it because nobody really understands what will happen. To some of us, we don't

[35] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.77.
[36] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.125.
[37] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Sydney on Monday, 31 January 2005, p.126.

> think it will be any different; it will be just another version of funny times and funny money, but anyway."[38]

Allianz finds this a refreshingly frank and honest acknowledgment by a repairer body of the concerns felt by some insurers about a forced move away from FTFM. Particularly given that the insurers that offer unrestricted choice of repairer and hence rely on FTFM for the one-on-one negotiation required by the so-called 'one quote' system will potentially be the most adversely affected by any change. And especially as the alternatives to FTFM may not be compatible with the continuation of an unrestricted choice of repairer policy.

Having said that, however, Allianz is committed to seeking an acceptable alternative to FTFM. Allianz can advise that it is commencing a process of consultation with repairers on possible alternatives to FTFM. Commencing immediately, Allianz will initiate a process of putting together a working party comprising Allianz representatives, repairers (both Allianz network repairers and non-network repairers) from all mainland States, and repairer representatives. The objective of the working party will be to identify and assess alternative approaches to the pricing of repairs, including piloting of preferred options, with a view to identifying alternative price negotiation model(s) acceptable to both Allianz and repairers. To the extent that any alternatives comprise hourly rates for labour, Allianz will give positive consideration to the Commission's recommendation that paint be costed separately. While some of the more major materials are already identified separately on quotes, (eg Weld-thru primer, drip check, proof coat and similar items) Allianz is not a supporter of the separate costing of minor material or other inputs (eg, administrative costs of preparing a quote, environmental disposal costs). This is not necessary with other repairers or service providers used by insurers and we are not convinced it should be a necessary part of an acceptable remuneration regime for smash repairers.

Allianz is cognisant of the fact that the Commission may very well suggest in its final report that a process also be established through peak industry bodies (eg, ICA and MTAA) to examine this issue. Allianz would be happy to be involved in such a process. However, Allianz is concerned that such an approach is likely to produce a standardised alternative to FTFM that would reduce the potential for positive competition and innovation among insurers around the pricing of repairer work. Allianz is proud of the good relations it generally has with repairers and their representatives - a relationship built on direct negotiation with repairers (albeit using FTFM) to achieve fair and reasonable outcomes for both sides - and does not want to see this undermined or subsumed by an industry-wide process dominated by much larger players.

Whether through a bilateral or industry-wide process, the development of an acceptable alternative to FTFM, if that is possible, will take time. Allianz strongly urges the Commission to remove the proscription of FTFM from its proposed code of conduct. The inclusion of a proscription of FTFM in an industry-wide code would:

- significantly delay the introduction of a code due to the time it would take to develop and implement an alternative to FTFM;

[38] Productivity Commission, Inquiry into Smash Repair and Insurance, Transcript of proceedings at Melbourne on Thursday, 3 February 2005, p.142.

- result in some insurers being in breach of the code on its commencement; or
- result in some insurers not participating in the code due to their inability, at least in the short to medium term, to comply with it.