

OFFICE OF FAIR TRADING

NATIONAL COMPETITION POLICY REPORT

ON

THE REGULATION OF MOTOR DEALER BROKERS

October 2000

Contents:

Executive Summary	1
1.0 BACKGROUND	3
1.1 Title of Legislation	3
1.2 Reasons for Review	3
1.3 Review Methodology	4
1.4 Motor Dealer Brokers – Operating Environment	4
1.5 Issues	6
2.0 RESTRICTIONS AND OBJECTIVES	8
2.1 Objective	8
2.2.1 Restrictions on Market Entry	8
2.2.2 Restrictions on Conduct	10
2.3 Impacts of Base Case	10
2.3.1 Consumers	10
2.3.2 Industry	11
2.3.3 Government	11
2.4 Options – Alternatives to Regulation	12
2.5 Unregulated Market	12
2.5.1 Impact of Unregulated Market on Consumers	12
2.5.2 Impact of Unregulated Market on the Industry	13
2.5.3 Impact of Unregulated Market on Government	14
2.5.4 Conclusions on Unregulated Market	14
2.6 Negative Licensing – Code of Conduct	14
2.6.1 Impact of negative licensing on Consumers	15
2.6.2 Impact of negative licensing on Industry	15
2.6.3 Impact of negative licensing on Government	16
2.7 Full Regulation	16
2.7.1 Impact of Full Regulation on Consumers	16
2.7.2 Impact of Full Regulation on Industry	17
2.7.3 Impact of Full Regulation on Government	17
3.0 REGULATION IN OTHER STATES	17
4.0 ANALYSIS	18
4.1 Stakeholders	18
4.2 Impact Analysis – Base Case	19
4.3 Comparative Analysis – No Regulation	19
4.4 Comparative Analysis – Negative Licensing Option	20
4.5 Comparative Analysis – Full Regulation Option	20
4.6 Analysis of Regulation in other States	21
4.7 Employment Impact	21
5.0 CONCLUSION	21
5.1 Summary of Impact Analysis	21
5.2 Conclusions and Recommendations	22
5.2.1 Conclusions	22
5.2.2 Recommendations	22
Motor Dealer Brokers – Industry Snapshot	Appendix 1
Questionnaire for Vehicle Brokers	Appendix 2
Summary of Impact Analysis	Appendix 3

MOTOR DEALER BROKERS

DRAFT PUBLIC BENEFIT TEST REPORT

Executive Summary

A major NCP review was completed on the Auctioneers and Agents Act 1971 and its proposed replacement, the *Property Agents and Motor Dealers Bill 2000* (“the Bill”). Following its completion a legislative policy decision to incorporate motor dealer brokers within the definition of “*motor dealer*” in the Bill was developed and proposed for incorporation in the Bill.

The legislative policy decision would result in a requirement that motor dealer brokers would need to be licensed under the new legislation.

This necessitates a further NCP review of that legislative policy decision, prior to consideration of the Bill by Parliament. A minor Public Benefit Test was therefore carried out.

The licensing model proposed in the policy decision, utilising minimum entry standards that still delivered consumer protection, was considered as the “base case” against which a number of alternative options to regulation were compared and assessed.

Those alternative options were –

- An unregulated market;
- A negative licensing model; and
- A full regulation option applying the same entry standards as for motor dealers.

Preliminary assessment revealed that the unregulated market option fails to meet the objective of the legislation, being consumer protection, and was rejected without proceeding to cost/benefit analysis.

The negative licensing model was able to meet the objective of the legislation, but at a reduced capacity, compared with the base case. It also imposed marginally more cost on the community than the base case.

Full regulation, applying existing entry standards required by applicants for motor dealer licences, was considered to be the most restrictive of the options. The benefits of this option did not outweigh the costs and therefore should be rejected under NCP guidelines.

The Public Benefit Test shows that the base case, the proposed legislative model, as best meeting the objectives of the legislation and that it was assessed against the other options as more effectively delivering benefits to the community.

Flowing from the review were several policy issues for which recommendations have been proposed. Those recommendations are –

- That the competencies developed for brokers should be the very minimum which ensures consumer protection from incompetent service without establishing unnecessary entry barriers.
- That in the development of the code of conduct for motor dealers and brokers, attention is given to addressing the issues of conflicts of interest for dealers acting as brokers, disclosure requirements to clients for those motor dealers acting as brokers and the potential for acceptance of secret commissions.

1.0 Background

1.1 Title of legislation

This review takes into consideration a proposed inclusion to the following legislation:

a policy proposal to amend the definition of motor dealer to include motor vehicle brokers within the *Property Agents and Motor Dealers Bill 2000*. (“The Bill”).

1.2 Reasons for Review

The *Auctioneers and Agents Act and Regulation* (“the Act”) were identified for National Competition Policy (NCP) purposes as containing measures that restrict competition.¹

Consequently, a major review of the Act and subordinate legislation was undertaken to meet the Queensland Government’s commitment under the Competition Principles Agreement (CPA) including the guiding principles under clause 5(1) of that agreement. A Report on the NCP Review of the Auctioneers and Agents Act was completed by PricewaterhouseCoopers, endorsed by the Auctioneers and Agents NCP Review Committee and approved by the Queensland Treasurer in August 2000.

Subsequent to that review, a legislative policy initiative was developed to incorporate motor vehicle brokers within the definition of “*motor dealer*” in the Bill that intends to replace the Auctioneers and Agents Act.

This policy initiative would lead to a proposed requirement that motor vehicle brokers be licensed under the Bill and be subject to the motor dealing code of conduct. Therefore a review of that policy initiative was conducted to satisfy NCP requirements. Currently, this sub-industry is not regulated in Queensland therefore any attempt to impose restrictions needs to ensure that it would result in a net benefit to the public.

The review has been conducted in accordance with Queensland Treasury criteria, with a view to assessing costs and benefits of any restrictions on competition contained or proposed in legislation and considering alternate means of achieving the desired outcomes.²

The guiding principles for reviews under paragraph 5(1) of the CPA are that legislation should not restrict competition unless it can be demonstrated that:

- the benefits of the restriction to the community as a whole outweigh the costs to the community; and,

¹ Queensland Legislation Review Timetable July 1996 p 19

² Queensland Treasury Public Benefit Test Guidelines October 1999

-
- the objectives of the legislation can only be achieved by restricting competition.

1.3 Review Methodology

In accordance with the Queensland Treasury Public Benefit Test Guidelines for Legislation Review, the review was conducted by the Legislation Review Unit of the Office of Fair Trading. A minor Public Benefit Test was conducted due to the fact that:

- Only a small number of participants currently operate as motor dealer brokers in Queensland. It is estimated that approximately 30 – 35 motor dealer brokerage firms exist, employing a total of approximately 90 persons, so the relevant market is not large;
- A major review of the overarching legislation, including the licensing of regulated occupations has already been conducted. Similar principles were assessed and, in the case of motor dealers, the same market as for brokers applies;
- The restrictions are not controversial and are expected to have minimum impact on consumers, motor industry operators and a small impact on brokers.

In accordance with Queensland Treasury guidelines, approval of the Public Benefit Test Plan was sought at Queensland Treasury officer level. A formal request from the Director-General, Department of Equity and Fair Trading to the Under Treasurer was submitted for approval of the Public Benefit Test Plan. The Under-Treasurer's approval to proceed was given on 15 September 2000.

In order to collect data necessary to complete the review, a questionnaire was developed to assist in the conduct of telephone interviews with every Queensland motor dealer brokerage firm that could be identified and located. Twenty-three (23) brokerage businesses were contacted between 4 September 2000 and 15 September 2000. These brokers provided information for the review. A summary or snapshot of the industry responses is provided in appendix 1. A summary of the questionnaire used to seek out industry responses is shown in appendix 2.

1.4 Motor Dealer Brokers – Operating Environment

Motor dealer brokerage in Queensland is predominantly a client-focussed service relying heavily on client referrals and testimonials rather than advertising or other marketing strategies to attract business.

Motor dealer brokers operate by providing clients with advice on the types of vehicles available and the location of specific types of vehicles. Brokers may negotiate or assist in the negotiation of the purchase of a motor vehicle from motor dealers on behalf of purchasers and assist in the disposal of trade-in vehicles (the purchaser's previous vehicle) either through the selling dealer or other dealers. Some brokers provide additional services associated with the purchase of a vehicle, including

financial advice, financial brokerage, supply of accessories, and/or arrange insurance and warranty packages.

Most brokers have developed networks of licensed motor dealers through whom they locate suitable vehicles for clients. Most brokers rarely access the private market.

There are approximately 30-35 brokerage firms operating in Queensland compared with approximately 2000 motor dealer outlets. Brokers therefore represent approximately 1.5% of the retail motor market. The exact number cannot be identified as some brokers operate part-time and/or from mobile phones and without advertising in papers and journals utilised by some brokers (Trading Post, Motor magazines, Industry, Union and financial journals). Anecdotal evidence suggests that there are a further 7-12 brokers that would fit into this category.

Almost all brokers operate in the Brisbane metropolitan area with one broker on the Sunshine Coast and two brokers on the Gold Coast. Figure 1 illustrates the growth in motor dealer brokerage in the past 21 years.

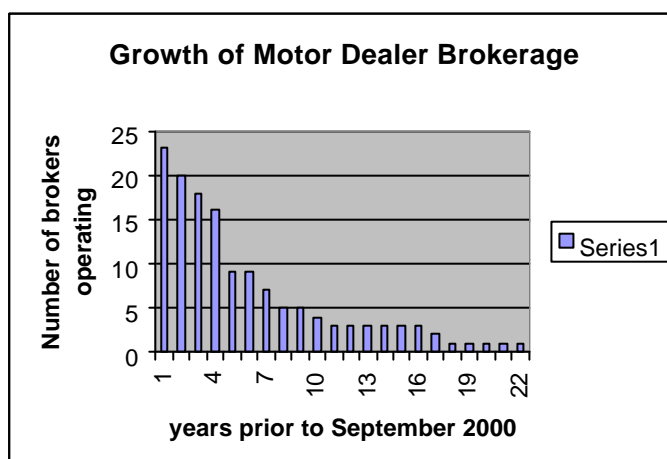


Fig.1

As Fig.1 indicates, the motor dealer brokerage industry is a relatively recent development in Queensland. When the *Auctioneers and Agents Act* was introduced in 1971, there were no brokers and the legislation did not provide for or anticipate their emergence as a sub-set of the retail motor dealing industry. Although one brokerage firm has existed for over 21 years and two others for 16 years and 15 years respectively, most brokerage firms have been established less than five years³.

³ The average period of establishment for the 23 firms participating in the questionnaire is 5.187 years.

Although several brokerage firms are substantial in size, turnover and employment, the typical brokerage firm is small, operating as one or two person businesses⁴.

Of the 23 brokerage firms participating in the consultation, six (6) had licensed motor dealers in the partnership/company and one has a symbiotic relationship with a motor dealer/auctioneer.

While brokers represent the interests of their clients, ie the public, with one exception, motor dealer brokers receive their fees from the selling motor dealers rather than from the client. Clients do not pay additional fees to brokers over and above the price of the vehicle, except for the supply of accessories, transportation of the vehicle or other additional services provided by the broker.

Most brokers indicate that they tend to avoid dealing with vehicle inquiries for vehicles valued at less than \$5000.00. This is not related to their fees but is more a quality assurance issue.

Brokers negotiate their fees with the selling dealers, usually as a flat fee ranging from \$100 - \$1500, averaging between \$400 and \$500 per vehicle (regardless of the value of the vehicle).

Based on vehicle registration transfers⁵, brokers handle 2.78% of the dealers' retail motor sales market or 1.5% of the entire market, inclusive of private sales.

Brokers need to negotiate their fees for service from the selling dealer, which results in unfettered price competition on the level of fees obtained by brokers.

The prices obtained by brokers for client/purchasers compare favourably with the motor dealer's retail pricing on motor vehicles for sale. As the brokers' fees are lifted from the dealers' profit margin on each vehicle, the brokers' fees represent an income transfer from dealers to brokers, rather than from consumers/clients.

Motor dealer brokers not only compete with each other for business, but also are in competition with motor dealers. Some motor dealers have responded to the brokers' challenge in the market by extending their services to compete directly with brokers in the location and provision of motor vehicles to prospective purchasers.

1.5 ISSUES

- There are no legislative restrictions on present operating processes for motor dealer brokers. Equally, there is no consumer protection (other than those general consumer protection measures of the *Fair Trading Act 1989* that apply to

⁴ Average employment through 23 firms interviewed is 3.65 persons or a total of 84 persons who are employees/owner operators.

⁵ Registration transfers derived from AADA's *Motor Industry News* – June 2000 edition.

all traders) currently provided by the *Auctioneers and Agents Act 1971* for consumers who deal through motor dealer brokers.

- In the past three to four years, there has been a rapid growth in the number of motor dealer brokers entering and continuing to operate in the retail motor vehicle industry.
- Because of the growth in motor dealer brokerage and the increased contact with motor dealers, there are increasing concerns by motor dealers regarding the current unlicensed status of brokers. Dealers consider that brokers, being in the same market, ought to be subject to the same conditions and rules as applies to licensed motor dealers. Motor dealers, through the MTAQ have advocated the licensing of motor dealer brokers.
- As a response to the growth in brokerage, some motor dealers have established themselves as brokers or provide some of the services expected from brokers. Additionally, at least one broker has sought and obtained motor dealer licensing under the *Auctioneers and Agents Act 1971*. As brokers and dealers service the retail motor market in different ways, there has emerged the issue of possible conflict where a dealer acts as a broker, or appears to act as a broker. In these circumstances there would exist a lack of consumer/client awareness of the true nature of the relationship between the client and the dealer/broker. Some disclosure requirements would assist information symmetry in the instance where dealers act as brokers.
- Based on the present definition of “*motor dealer*”⁶ under the Act, some brokers’ services or actions may already require to be licensed. For example: as there is no definition of “*buy*” in the legislation, negotiations for the purchase of motor vehicles could be caught within the definition of “*motor dealer*”. Also the way in which brokers may assist in the disposal or sale of trade-ins could come within the definition of “*selling*”. In any event, the legal position concerning brokers’ current activities is unclear. The inclusion of brokers’ functions as motor dealing activity would clarify the law and places motor dealers and brokers on an equal footing with respect to the market and the law.
- If licensing is to be introduced for brokers, competency levels for licensing will need to be assessed against the government’s commitment to competency-based training and qualifications. It is also necessary to apply the minimum competency requirements necessary to ensure consumer protection against unlawful or incompetent performance by licensed brokers, without imposing inappropriate entry barriers that would prevent brokers from entering or continuing in the brokerage market.
- The growth in brokerage activities and the number of participants has concerned the motor dealing industry, brokerage firms and Government. Increased and uncontrolled activity of motor dealer brokers might lead, in some cases, to

⁶ Section 2, *Auctioneers and Agents Act 1971* - Definitions

consumer detriment through inappropriate or incompetent advice, receipt of secret commissions from motor dealers or other conduct issues.

2.0 RESTRICTIONS AND OBJECTIVES

2.1 Objective

The Review of the *Auctioneers and Agents Act 1971* and *Auctioneers and Agents Regulation 1986* established that the objective of the legislation was –

“ Comprehensive consumer protection is the objective against which any restrictions on competition imposed by the Act, or regulatory alternatives, should be assessed; having regard also to Clause 5(1) of the Competition Principles Agreement (CPA).

Clause 5(1) of the CPA requires that legislation should not restrict competition unless it can be demonstrated that:

- The benefits of the restriction to the community as a whole outweigh the costs;
- and
- The objectives of the legislation can only be achieved by restricting competition.”

The Auctioneers and Agents NCP Review Committee accepted this objective as an appropriate criterion to measure the legislation and alternative options under review.

The legislative proposal to incorporate motor dealer brokers within the definition of motor dealer in the Property Agents and Motor Dealers Bill 2000, and alternative options for regulating motor dealer brokers are examined against this legislative objective. The principles of regulatory restrictions assessed in the Auctioneers and Agents Act review are the same as the principles for regulating brokers.

2.2 Base Case – Licensing/Regulation of Motor Dealer Brokers

The base case for the review is the legislative option to license and regulate motor dealer brokers through the motor dealing provisions of the *Property Agents and Motor Dealers Bill 2000* which has been introduced into Parliament and awaits debate.

2.2.1 Restrictions on Market Entry

The proposed Clause 267 (1)(e) of the *Property Agents and Motor Dealers Bill 2000* provides that a motor dealers’ licence authorises the holder of the licence to – “negotiate, under a consultancy arrangement, for a person who is not a motor dealer or auctioneer for the purchase of a motor vehicle for the person.”

The proposed Clause 267 (3) defines “*consultancy arrangement*” meaning an arrangement under which a person advises someone else where or from whom the other person can buy a motor vehicle.

The Bill refers to consultancy arrangements for the negotiation for the purchase of a motor vehicle, which is in industry terms - “brokerage”, which is the term used throughout this report.

The insertion of clause 267(1)(e) in the Bill would have the effect of requiring motor dealer brokers to hold licences as motor dealers.

If the provision becomes law, brokers would be required to obtain motor dealer licences and their broker employees would need to hold certificates of registration as motor salespersons. Brokers would be required to comply with all relevant provisions of the legislation, including the motor dealer’s code of conduct.

The Policy and Legal Unit of the Office of Fair Trading, which has responsibility for the development and administration of the legislation, recognises the different services and requirements for conducting brokerage and motor dealing business. Accordingly the appropriate eligibility for obtaining a broker’s licence as a motor dealer would be different from the eligibility requirements for obtaining a motor dealer’s licence.

In line with existing Government policy to apply competency-based qualifications which are the minimum required to ensure consumer protection against illegal or incompetent performance, the eligibility requirements would focus on client service issues and product knowledge rather than selling competencies or experience. Suitability criteria, including no relevant criminal convictions or bankruptcy would apply.

Should the Bill become law, brokers will need to apply for a Property Agents and Motor Dealers licence and pay the application and licence fees. This fee is likely to be at the same level as other categories of Property Agents and Motor Dealers licences – Approximately \$400 per year and approximately \$100 for salespersons’ certificates of registration.

Each applicant will be checked to ascertain if they have any relevant criminal record, assessed for the required competencies and if meeting all application requirements would be issued with a motor dealer’s licence, restricted to “consultancy arrangements”. As with other licence categories for which the licence reduction and extension program may apply, an option to renew the licence for up to three years will be provided. In summary the proposed entry restrictions would be -

- Good character, no criminal convictions;
- Not bankrupt;
- Meets required competency standards;
- Payment of application/licence fee.

The entry restrictions for broker employees, requiring registration would be lower than for licensees. No experience, competency testing or training requirements would be imposed on employees seeking registration. These restrictions would be limited to –

- Good character, no criminal convictions;
- Employed by a licensed broker;
- Payment of registration fee.

2.2.2 Restrictions on Conduct

It should be noted that some of the motor dealing provisions, particularly those directly related to conduct and record keeping issues for the sale of used motor vehicles would not and could not apply to brokers. For example, clause 318 – requirement to keep a transaction register excludes brokers as (a) they do not directly sell the vehicle and (b) the selling dealer is required to keep a transaction register, so any additional requirement for brokers would be unnecessary duplication.

Brokers would be subject to a proposed motor dealers' code of conduct that would form part of the regulation to the principal legislation. This code would not be anti-competitive in content and would seek to define and guide motor dealers' and brokers' conduct in their professional relationships with clients.

Specific broker conduct issues such as secret commissions and disclosure requirements to clients for motor dealers who act as brokers would be addressed in the proposed code of conduct.

Whilst the proposed code of conduct may substantially assist consumers it is not considered to be a significant determinant of or imposing significant impact on market competition and has thus been excluded from the NCP analysis.

2.3 Impacts of the Base Case

2.3.1 Consumers

The impact on consumers as a result of licensing brokers would be both positive and significant. As consumers place significant trust in brokers providing appropriate, accurate and independent advice concerning the purchase of motor vehicle, good character and competency testing of practitioners is an important safeguard to minimise dishonestly and other negative conduct issues, detrimental to consumers.

Licensing brokers should not significantly reduce the client's choice of brokers or brokerage services.

Coupled with the ability, through licence registers, to identify and locate particular brokers and enforcement of conduct issues through a proposed mandatory code of conduct, the proposed legislative option of licensing confers a moderate to high benefit on consumers. Furthermore this measure supports the objective of the principal legislation.

2.3.2 Industry

For brokers, the proposed licensing option imposes restrictions on entry in the form of competency requirements, character testing and the payment of licence fees.

Competency standards would focus largely on client service issues and be established as the minimum level of competency required to provide consumer protection against incompetent service or advice. It is expected that most existing brokerage practitioners would possess satisfactory competencies to be licensed and that the competency standards would not greatly impede market entry. Therefore this requirement does not appear to have a significant impact on competition in the market.

The proposed character probity test imposes no additional cost on the industry and would result in few applications for a licence or certificate of registration being rejected. A small benefit to the industry is derived from the screening of applicants and filtering out those with criminal histories, improving the industry's reputation and encouraging greater consumer confidence in dealing with licensed brokers.

The proposed payment of an application fee and subsequent renewal fees imposes a small cost on the industry. (Yearly licence fee of approx. \$400.00 compared to yearly operating expenses of between \$15,000 and \$150,000 is relatively small). Without exception, brokers consulted, supported or agreed to the licensing of the industry. It follows that they would accept and absorb the licence fee as a part of their operating costs.

Licensing of brokers would remove a perception held in the motor industry that by not licensing or regulating brokers, they enjoy a benefit not conferred on the industry generally and have an unfair advantage over dealers in the provision of their services.

A licensing regime for brokers would also facilitate transfers of licensing under mutual recognition for Queensland brokers moving or expanding into regulated jurisdictions such as NSW, Victoria, Northern Territory or Western Australia.

Overall, the licensing option would impose a very small net cost to the brokerage industry.

2.3.3 Government

The main impact on government from the proposed licensing option is incurring expenditure on administering the licensing, registration and compliance activities of brokers. This is offset by revenue from application/licence fees representing an income transfer from brokers to government.

Additionally establishment costs are diminished by utilising existing infrastructure (established licensing registers, investigation and processing staff).

Overall the government derives no net benefit or cost from this measure, other than the further satisfaction of the objectives of the legislation.

2.4 Options - Alternatives to Regulation

The options that will be assessed against the base case are –

- An unregulated market;
- Negative licensing and code of conduct;
- Full regulation requiring a motor dealer's licence.

2.5 Unregulated Market

Motor dealer brokers locate specified vehicles and provide clients with advice on the types and prices of vehicles available. Brokers negotiate or assist in the negotiation of the purchase of a motor vehicle from motor dealers on behalf of purchasers and assist in the disposal of trade-in vehicles either through the selling dealer or other dealers.

Brokers provide their services to clients by accessing motor vehicle stock held by licensed motor dealers.

Brokers are currently not regulated, although some concerns have been raised in the motor dealing industry that some activities of brokers may be considered motor dealing activity and which would require licensing under the *Auctioneers and Agents Act*.

Brokers are free to enter and exit the industry without legislative impediment. Natural entry restrictions such as establishment costs are small⁷.

2.5.1 Impact of Unregulated Market on Consumers

Consumers accessing motor dealer brokers in an unregulated market have access to the widest possible choice of brokerage service.

However consumers have no particular means of making informed decisions about the engagement of a particular broker other than to observe that most consumers select brokers on the recommendation or referral of other users of brokerage services.

Consumers are currently exposed to some risk in that they place reliance on the skills and advice of brokers to locate and negotiate the best possible deal for the purchase of a motor vehicle and to handle arrangements for the disposal/trade-in of previously owned vehicles.

⁷ Establishment costs ranged between \$2,000 and \$50,000. The average establishment costs are \$10,353, based on the 17 responses provided to the interview/questionnaire.

Unlike other motor dealing transactions with licensed dealers, there are no mechanisms to prevent market failure and should any market failure occur which directly impacts on consumers, they must look to their own resources to seek remedies or redress.

Forms of market failure which could impact on consumers, both from an economic or social perspective are –

- Inappropriate advice on the type, availability, suitability or price of motor vehicles for the consumer's needs;
- Brokers acting in the interest of themselves or dealers, instead of the consumer/purchaser;
- Secret commissions paid to brokers to improperly advise purchasers about a particular vehicle or vehicles;
- Conflicts of interest for motor dealers in the circumstances where they acting as or holding out that they act as brokers as well as selling their own stock.

The resultant loss for consumers from market failure imposes negative economic and social impacts. While this is offset to some degree by the fact that OFT has not had any formal complaints about brokers other than from dealers, the recent growth of the industry, together with market conditions in other States suggest that the potential risks to consumers is likely to increase.

2.5.2 Impact of Unregulated Market on the Industry

Brokers would benefit from not be required to pay fees or meet other legislative entry requirements under a deregulated model.

An inability to control, in any way, unsuitable persons (ie: persons with criminal records or bankrupts) from entering the industry and who may threaten consumer confidence in brokerage services has a small negative impact on the industry.

The other sector of the industry – motor dealers – perceive that if brokers remain unregulated, then a benefit is conferred on that sector of the industry by not being required to be licensed, pay licence fees or be subject to official scrutiny in regard to their conduct. Further, the “grey” area between dealing and broking activities will continue in an unregulated environment.

Overall there is a small net benefit for brokers to operate in an unregulated market.

2.5.3 Impact of Unregulated Market on Government

There is no net costs or benefits for government resulting from an unregulated market. However, the objective of providing consumer protection cannot be achieved in the unregulated model. This reflects negatively on the Government's Priority Outcomes, particularly Skilling Queensland, promoting safer/supportive communities, promoting better quality of life and providing strong leadership by delivering improved and integrated Government services. It is reasonable to assume that complaints by dealers about brokers will continue in an unregulated environment.

2.5.4 Conclusions on unregulated market

The option of no regulation fails to meet the objective of providing consumer protection and, additionally, it appears to convey a benefit on one sector of the industry that is not available to other sectors of the industry.

Because the unregulated market fails to meet the objectives of the legislation, fails to provide any consumer protection and fails to address the confusion and uncertainty about certain brokerage processes being unlicensed motor dealing activity, the option of an unregulated market is not considered appropriate.

2.6 Negative Licensing – Code of Conduct

The negative licensing model used for the review establishes no legislative entry barriers, regulates conduct issues through a proposed mandatory code of conduct and provides an exit process which prevents defaulting practitioners from continued operation in the brokerage field.

The difference between a negative licensing regime and either of the licensing options is that entrants to the industry would not have to satisfy any competency or qualifications requirements nor be character tested. Entry into the brokerage industry would be the same as in an unregulated market, but there would be conduct regulation and exit processes where market failure has occurred.

A mandatory code is included in the option, rather than a voluntary code because:-

1. A voluntary code is difficult to enforce. Non complying practitioners could merely elect to vacate the scheme and this would not achieve the objective of consumer protection;
2. There is no industry association or interest group existing, or, considering the small size of the industry, likely to exist in the near future, which could provide the infrastructure to develop, maintain and administer a voluntary code of conduct for the brokerage industry.

The mandatory code would address the same conduct issues as for a mandatory code applying to either the base case or the full regulation option and would meet the objectives of the legislation.

The exit process would be in the form of an injunction or other Court Order process sought under legislative provisions for enforcing the code of conduct and which would prevent respondents from continued operation within the brokerage industry.

2.6.1 Impact of negative licensing on Consumers

Consumers would receive a measure of consumer protection both from the deterrence aspect of exit processes preventing or prohibiting a person from continued practice as a broker. However because the measure deals with market failure from the back end, rather than up front as in the case of licensing, then inevitably some consumers will suffer loss before particular market failures are rectified.

As there are no entry barriers for brokers, consumers/clients could expect a marginally greater range of brokerage firms and services to choose from under negative licensing in fact a similar range as would result from an unregulated market.

However consumers have no appropriate information to choose brokerage firms based on competencies or character. There are no safeguards preventing unsuitable persons with criminal records holding out as brokers. This is relevant also in that consumers can only expect remedial, rather than preventative action in situations where a broker might abuse their position of trust and act against the interests of the consumer.

It is assessed that consumers would receive a moderate benefit from a negative licensing system, but significantly reduced from that offered by the base case or the full regulation option.

2.6.2 Impact of negative licensing on Industry

Brokers would benefit under a negative licensing scheme by savings on licence and renewal fees, and having to meet neither entry requirements nor costs in acquiring competencies.

As there are no safeguards preventing unsuitable persons with criminal records holding out as brokers, consumer confidence in dealing with brokers could be reduced or damaged by unsuitable persons destroying the position of trust that brokers rely on in their dealings with consumers.

Overall the brokerage industry would enjoy a small benefit. The magnitude of this benefit is the same as the cost to industry under the base case.

2.6.3 Impact of negative licensing on Government

There is a cost to government from negative licensing in that government must provide the resources for compliance and enforcement of the conduct regulations/code of conduct. This cost is not offset by licence/registration fees, as there would be none.

A further cost to government of a negative licensing system is the establishment of different systems of regulation for brokers and motor dealers, which is not unlike the issue raised in the unregulated option whereby brokers had a benefit not conferred on the rest of the industry.

2.7 Full Regulation

The option of full regulation refers to the process of defining brokers as motor dealers and requiring them to meet the same entry requirements as motor dealers. The difference between this option and the base case is that brokers would require the same qualifications/competencies as motor dealers. This raises the standard of entry compared with the base case.

All other entry requirements and conduct issues, including the code of conduct would apply in the same manner as in the base case.

Brokers and motor dealers operate in the same market, with the same clients (motor vehicle purchasers) and dealing with the same product. However the broker's focus is on service to the client in providing appropriate, accurate and independent advice about vehicle and to negotiate or assist in the negotiation for the purchase of motor vehicles by consumers.

The motor dealer's focus is to sell those vehicles in stock or which can be readily acquired following a client inquiry. The dealer's concern does not usually extend to assisting other dealers sell motor vehicles by advising or directing clients to a rival dealer.

Both brokers and dealers need a good knowledge of the product and both require appropriate skills in negotiating deals. However the dealer's core business requirements are selling motor vehicles and keeping appropriate records relating to motor vehicle transactions. The broker's core business is to locate and assist in the acquisition of the most appropriate vehicle at the best possible price for a client. This is where the competency requirements for dealers and brokers part.

2.7.1 Impact of full regulation on Consumers

Full regulation requiring brokers to exhibit equivalent qualifications to motor dealers would significantly reduce the number of brokers operating in and entering the industry, thereby reducing the range of choice of broker that the consumer might access.

Full regulation offers consumers the same range of protection as the base case in terms of character testing. Therefore full regulation would meet the objective of the legislation.

Consumers would derive similar benefits from full regulation as for the base case, except that the benefit is reduced by the fact that there would be a reduced choice of brokers and reduced choice of services.

2.7.2 Impact of full regulation on Industry

There are 30 – 35 motor dealing brokerage firms operating in Queensland. If the entry requirements for brokers were the same as for motor dealers, the likely immediate effect would be to reduce the number of brokerage firms to approximately 8 – 9. Six brokers are already licensed as motor dealers and it was assessed from the background information provided by brokers that only two or three of the other existing brokers would currently be qualified to obtain motor dealers' licences.

Additionally, the entry requirements would considerably reduce the growth of new brokerage firms.

The impact of full registration would not only reduce the number of brokerage firms but would cut employment in this industry by approximately 50%.

Some brokerage firms would close because they could not comply with licensing requirements. For those brokers who would seek to obtain necessary competencies or other qualifications that would enable them to be licensed as motor dealers, the measure would impose additional compliance and training costs.

The net cost to the brokerage industry would be substantial.

2.7.3 Impact of full regulation on Government

The administration, compliance and investigation costs for government in implementing a full regulation option would be approximately the same as for the base case. However with the reduction in eligible applicants for licences, licence revenue would be lower.

Therefore there would be a small net cost to government for this option.

3.0 Regulation in Other States

In New South Wales thirty-five (35) brokers are licensed as motor vehicle consultants as a sub-category of motor dealing. The proposed scheme to define brokers in Queensland as motor dealers is similar to the New South Wales model and even uses the same expression "consultancy".

Brokers are captured in legislation under the motor dealer category of licensing in Northern Territory, Western Australia and Victoria and require motor dealing experience/qualifications to be granted a licence. These licensing models are considered more restrictive than the NSW law or the proposed Queensland legislation.

In the case of the Northern Territory, there are no brokers currently licensed or operating. Victoria has approximately 30 brokers licensed as motor dealers. Western Australia was not able to provide a dissection of the number of brokers, licensed as motor dealers, from other licensed motor dealer operatives.

There are currently moves to provide a separate category of licence for brokers under Western Australian motor dealing legislation.

There is no regulation of motor dealer brokers in South Australia or the Australian Capital Territory. The licensing authority in South Australia could not confirm whether motor dealer brokers existed in that State and the licensing authority in ACT indicated that although there were 100 licensed motor dealers in ACT, there were no brokers.

In Tasmania neither motor dealers nor motor dealer brokers are regulated and consultation with the Office of Fair Trading in that State indicates that there are no brokers operating in the retail vehicle market in that State.

In those States where motor dealer brokers/consultants are known to operate, the number of brokers operating in the retail motor vehicle market is very small compared to the number of motor dealing practitioners as is the case in Queensland.

In all States and Territories, no adverse comments regarding compliance or conduct issues concerning brokers were reported.

Mobility between States and Territories by brokerage firms is not evident. However, should Queensland introduce a licensing regime for brokers, then transferability of brokers to other regulating States and Territories would be facilitated. It also accords with the policy direction of all Australian Governments in facilitating ready access across borders and markets through the Mutual Recognition Principle.

4.0 ANALYSIS

4.1 Stakeholders

The stakeholders considered in this review were –

- Current brokers and their employees
- New entrants into the brokerage business
- Motor dealers
- Consumers/purchasers of motor vehicles utilising brokerage services.
- Government

4.2 Impact Analysis – Base Case

The “without change” state for motor dealer brokerage is the existing unregulated market. With the rapid growth in brokerage and the increased potential for consumer detriment, the unregulated market cannot meet the objective of the legislation relating to motor dealing activity, that is: consumer protection.

The base case consists of regulating brokers by requiring a licence under the legislative umbrella of motor dealing without imposing the higher, unnecessary standard of entry requirements. Brokers would become subject to conduct requirements under the motor dealing code of conduct.

What the base case provides is –

Character suitability assessment;
Competency assessment; and
A Code of Conduct

Which together promotes consumer protection and consumer confidence in dealing with brokers.

Licensing of brokers is not expected to impact on consumers as it is anticipated that the licensing regime will not significantly reduce the pool of brokers operating or entering the motor dealer brokerage industry. At the same time a moderate to high benefit is expected to flow to consumers from the application of character testing, competency requirements and conduct provisions designed to provide consumer protection.

The negative impact on industry will be very small. The licensing cost of \$400 per licence amounts to a total cost of approximately \$12,000 per year to the industry. This small cost is off-set by benefits such as increased consumer confidence in service delivery and broker integrity, transferability of licensing between States and placing motor dealers and brokers on an “even playing field” with regard to industry regulation.

Overall the base case delivers a net moderate benefit to the community. The base case satisfies all requirements in meeting the objective of the legislation.

4.3 Comparative Analysis – No Regulation

The no regulation option fails to meet the objective of the legislation in that it provides no protection for consumers against market failure caused by information asymmetry, misrepresentation or conflict of interest.

Further, because there are no regulating controls, the unregulated market cannot address the emerging risk of market failure developing from the rapid growth in brokerage.

Finally, an unregulated market confers a benefit on brokers which is not available to the rest of the industry (ie, motor dealers).

Therefore the continued non-regulation of the industry is not sustainable.

4.4 Comparative Analysis – Negative Licensing Option

Negative licensing would result in a saving of \$12,000 pa in licensing fees for the brokerage industry and easier accessibility for new entrants into the brokerage industry. Consumers would have a slightly enhanced choice of brokers to select from. However this is traded off against a substantially reduced measure of consumer protection, an increased inability for consumers to make informed choices about the brokerage firm or services available and an increased risk of economic loss to consumers when market failure occurs.

The potential cost to industry is a loss of consumer confidence in brokerage services, should there be market failure.

There is also a cost to government from providing compliance infrastructure without any offsets in the form of licensing fees.

Whilst there is a marginally increased opportunity for competition under the negative licensing option compared to the base case, the capacity of this option to meet the objective of the legislation by delivering consumer protection is diminished.

In agreement with the conclusion on negative licensing for motor dealers in the NCP Review Report on the *Auctioneers and Agents Act 1971*, negative licensing for brokers is assessed as having a small net cost to the community as a whole. The NCP Review Report on the *Auctioneers and Agents Act* concluded that negative licensing was not a suitable option to apply to the regulation of motor dealers. It is difficult to justify a different conclusion with regard to negative licensing of brokers.

Negative licensing of brokers does not compare favourably with the base case where the net benefits to the community exceed those for negative licensing.

4.5 Comparative Analysis – Full Regulation Option

The full regulation option confers similar benefits as for the base case, with one important exception being the different standards of entry requirements regarding competencies/qualifications.

The application of higher, possibly unnecessary or inappropriate entry standards would result in a substantial reduction in the number of brokers in the market place. It would reduce or stymie the current growth in brokerage services by preventing new participants from entering the industry, and impact adversely on the employment prospects for at least half of currently employed brokerage staff.

It is assessment that this would be the option that restricted competition more than any other option, including the base case and fails under NCP guidelines to be considered an appropriate alternative to the base case.

4.6 Analysis of Regulation in other States

In the case of those States and Territories that do not regulate motor dealer brokers, no discernible broker activity occurs and therefore the activity does not require regulation.

Western Australia, Northern Territory and Victoria regulate brokers by requiring them to be licensed motor dealers in a similar manner as the full regulation option discussed in this report, thereby providing a more restrictive model than the Queensland proposal.

New South Wales provides licensing for motor dealer consultants as a sub-category of motor dealing. This is a less restrictive model and is similar to the Queensland proposal.

4.7 Employment Impact

The optimum level of employment is demonstrated in the unregulated market option. There are presently approximately 90 persons employed in the brokerage industry, located in the Brisbane metropolitan and south-east corner of the State.

Several of the brokerage firms, larger in terms of turnover and employment resources are already licensed as motor dealers, so licensing regulation would have little or no effect on their current operations or employment levels.

It is not anticipated that the smaller firms, usually consisting of one or two persons, would be adversely affected by the negative licensing option or the base case.

However, the full regulation model, because of its higher entry requirements would significantly affect many current operators from qualifying in terms of competencies or other qualifications and it would be expected that many would no longer be able to operate within the law if full regulation were to be applied. It is projected that if this model were adopted, then approximately 73% of brokerage businesses would close and reducing employment opportunities by approximately 50%.

5.0 CONCLUSION

5.1 Summary of Impact Analysis

Refer to Appendix 3.

5.2 Conclusions and Recommendations

5.2.1 Conclusions

The NCP guidelines require that the examination of regulatory options be assessed against:

- the objective of the legislation
- the overall net benefit/cost from each option, and
- the principle that restrictions to competition should only occur where the objectives of the legislation cannot be met by less restrictive approaches.

With these criteria in mind, the option to maintain an unregulated market cannot be sustained because, although it is less restrictive to competition than other options, it cannot provide or meet the objectives of the legislation at all.

The negative licensing option, like the unregulated market would allow greater competition than other options. However the cost of this increased competition is reduced consumer protection. Overall, this option does not deliver benefits as great as the base case.

The full regulation option is the most restrictive of all options and creates the greatest net cost on the community as a whole.

The base case is assessed as having a very low impact on brokers, promotes and enhances consumer protection and is assessed to be the option which best achieves the objective of the legislation without undue restrictions on competition or imposing significant costs on any part of the community.

There appears to be no impediments to immediate implementation of this measure. Transitional arrangements to allow brokers time to comply with the new licensing requirements may need to be considered.

5.2.2 Recommendations

It is recommended that the base case, proposing to define brokers through the *Property Agents and Motor Dealers Bill 2000* as motor dealers be endorsed and adopted. This measure would require licensing which would take into account appropriate competencies for brokers and enabling a licence conditional to the conduct of consultancy (brokerage) to be issued to suitable applicants.

The competencies developed for brokers should be the very minimum which ensures consumer protection from incompetent service without establishing unnecessary entry barriers.

It is also recommended that attention is given to addressing the issues of conflicts of interest for dealers acting as brokers, disclosure requirements to clients for those motor dealers acting as brokers and secret commissions in the development of the code of conduct for motor dealers and brokers.

Motor Dealer Brokers – Industry Snapshot⁸

APPENDIX 1

Licensing	Vehicle Referrals	Persons engaged in brokerage Employee/partner	Fees	Conduct Issues	Operating Costs	Market Share
<p>Motor dealer brokers are not presently regulated.</p> <p>Six brokers are licensed as motor dealers or have licensed persons within their businesses.</p> <p>Without exception, brokers support or agree with the concept of licensing for brokers – providing the entry requirements (qualifications) are appropriate.</p>	<p>Brokers rely heavily on client referrals for new and repeat business.</p> <p>Collectively, brokers receive approximately 2500 vehicle inquiries per month. The average level of successfully concluded transactions is 20% of inquiries.</p>	<p>Most brokerage firms are one or two person operations, with several larger operators employing multiple staff.</p> <p>The total employment / operators in motor dealer brokerage in Queensland is approximately 85 persons.</p>	<p>With one exception, brokers negotiate their fees with the participating dealer.</p> <p>The fees range from \$100 - \$1500. The average is \$400-\$500 per vehicle.</p> <p>The broker's fee may be supplemented by accessories sales, and other services and supplies.</p>	<p>The perception within the brokerage industry is that there are a lot of “cowboys” in the industry with only a few ethical operators.</p> <p>There have been no recorded consumer complaints about brokers.</p> <p>Brokers appear to be client-focussed in their approach to vehicle sales.</p> <p>General agreement that brokers who are motor dealers should be required to disclose to clients that they are licensed motor dealers.</p>	<p>The range of operating costs disclosed* ranged from \$15,000 pa to \$150,000 pa</p> <p>*Not all brokerage businesses were able or prepared to provide data on operating costs.</p> <p>14 brokerage firms (61%) provided information on operating costs.</p>	<p>Brokers numerically represent 1.5% of the retail motor market.</p> <p>Motor dealer brokerage services represent approximately 2.78% of vehicles sold by motor dealers within Queensland or 1.5% of total vehicle sales.</p>

⁸ The information gathered to draw up this snapshot was collected in the weeks 4 – 22 September 2000 and does not take into account exits from the industry.

APPENDIX 2

QUESTIONNAIRE FOR VEHICLE BROKERS

The following questions were asked of motor dealer brokers by phone following an introduction that included – explanation for call – examination of policy initiative to licence motor dealer brokers - NCP review. Brokers were told that answers would be treated as “Commercial in Confidence” only to be used for the NCP process.

1. Is your organisation already licensed as a motor dealer?
2. Is the organisation connected with a motor dealership?
3. Is the organisation connected to one or more financial institutions?
4. How long have you operated this brokerage business?
5. Is the business run in conjunction with any other business?
6. Who engages yours services?
7. What do you do? Break down of services offered.
8. How do you attract business? Advertising etc?
9. Who pays for your services?
10. How are your fees for services calculated? How much – average?
11. How many vehicle referrals would you make – on a monthly basis?
12. What is the success rate of your referrals?
13. What is your attitude about licensing of motor dealer brokers?
14. What, if any, are the impediments to your business's growth?
15. What standards for business conduct?
16. How do you currently deal with complaints?
17. Are you a member of an industry association?
18. How many employees in your brokerage business?
19. What are the approximate set up costs – premises/ phone/office equipment/employees?
20. What is your average yearly operating costs?

Summary of Impact Analysis

Appendix 3

Code:
 EF= Efficiency Gain
 IT=Income Transfer
 MI=Market Improvement
 ML = Market Loss

Stakeholder	Base Case		Negative Licensing		Full Regulation	
	Benefits	Costs	Benefits	Costs	Benefits	Costs
Consumers	Competency testing: (EF) Character testing: (MI) Licence register providing accessible identification and location of brokers: (EF) Enhanced consumer protection. (MI)	Marginally reduced choice of brokers to select from: (ML)	Consumer protection. (MI)	Competency testing: (ML) Character testing (ML) Redress rather than prevention (ML)	Competency testing: (EF) Character testing: (MI) Licence register providing accessible identification and location of brokers: (EF) Consumer protection: (MI)	Significantly reduced choice of brokers: (ML)
Magnitude of Impact	Moderate	Small	Small to Moderate	Small	Moderate	Moderate

Code:
EF= Efficiency Gain
IT=Income Transfer
MI=Market Improvement
ML = Market Loss

Stakeholder	Base Case		Negative Licensing		Full Regulation	
	Benefits	Costs	Benefits	Costs	Benefits	Costs
Brokers	Character testing and consumer confidence: (MI)	Licence Fees (IT) Costs of competency training: (ML)	Saving on Licence Fees: (IT) Costs of competency training; (IT)	Reduced consumer confidence from no character or competency testing: (ML)	Character testing (EF)	Licence fees: (IT) Costs of Competency training: (ML) Restriction on competition (ML)
Magnitude of Impact	Small/Moderate	Small	Small	Small	Small	Moderate to large

Code:
EF= Efficiency Gain
IT=Income Transfer
MI=Market Improvement
ML = Market Loss

Stakeholder	Base Case		Negative Licensing		Full Regulation	
	Benefits	Costs	Benefits	Costs	Benefits	Costs
New Entrants	Character testing and consumer confidence: (MI)	Licence Fees (IT) Costs of competency training: (ML)	Saving on Licence Fees: (IT) Costs of competency training; (IT)	Reduced consumer confidence from no character or competency testing: (ML)	Character testing (EF)	Licence fees: (IT) Costs of Competency training: (ML) Restriction on competition (ML)
Magnitude of Impact	Small/Moderate	Small	Small	Small	Small	Moderate to Large
Motor Dealers	Equitable treatment under the Law (MI)	NIL	NIL	Inequitable treatment under the Law (ML)	Equitable treatment under the Law (MI)	NIL
Magnitude of Impact	Small	N/A	N/A	Small	Small	N/A
Government	No Net benefit	No Net cost		Compliance/enforcement costs: (IT)	No Net benefit	No Net cost
Magnitude of Impact	N/A	N/A	N/A	Small	N/A	N/A