House
Legislative
Analysis
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AUTO DEALER BROKERS, FRANCHISES, IMPORTERS

House Bill 4738 as enrolled
Public Act 455 of 1998
Sponsor: Rep. Kim Rhead

House Bill 4740 as enrolled
Public Act 456 of 1998
Sponsor: Rep. Tom Alley

Second Analysis (1-26-99)

House Committee: Commerce
Senate Committee: Economic Development, Trade and Regulatory Affairs

THE APPARENT PROBLEM:

Like many other areas of business, automobile retailing has undergone tremendous changes in recent years. As a result, automobile dealers -- many of whom own and operate family businesses -- have experienced a number of threats to their continued effective functioning as independent small businesses. For almost two decades, auto dealers have argued that they have needed statutory protection from the unfair amount of power held by auto manufacturers in their agreements with their dealers. The first state law addressing auto dealers' concerns was Public Act 331 of 1978, which defined in statute "fair dealing" in agreements between vehicle manufacturers and their dealers. As the House Legislative Analysis Section analysis for the bill that became Public Act 331 noted, "In the absence of any such general principles [defining "fair dealing"], the unequal power balance between dealers and manufacturers leaves a great potential for arbitrary and unilateral decisions by manufacturers about contract arrangements. Dealers believe there should be some statutory guidelines outlining the rights and responsibilities of both parties in such dealer agreements." Despite passage of Public Act 331 of 1978, however, some people believed that dealers' problems with manufacturers still remained and that dealers needed further protection. As a result, in 1981, Public Act 118 replaced Public Act 331 of 1978, creating a new act to regulate dealings in new motor vehicles between motor vehicle manufacturers and dealers. As the Senate Analysis Section analysis of the enrolled bill said, in part, the new act replaced Public Act 331 of 1978, "incorporating and expanding many of that law's provisions, especially provisions stipulating the actions manufacturers would be prohibited from taking and provisions outlining what constituted 'good cause' for termination of agreements between manufacturers and dealers." Two years later, in the wake of the recession that resulted in the closing of 200 dealerships in those two years, it was felt that the surviving auto dealers should be afforded further protections. Consequently, the new auto dealers franchise act (as Public Act 118 of 1981 came popularly to be known) was revised, because, as the Senate Analysis Section analysis said, "it [was] believed that, due to manufacturers' relative economic and bargaining strengths, neither the statute [i.e. Public Act 118 of 1981] nor private negotiations [were] adequate to protect dealers." Once again auto dealers have asked for legislation to further increase protection for them in their relationship with auto manufacturers.

Further, in a related matter, auto brokers are independent purchasing or sales agents for consumers who want to buy a car or who have a car to sell. In theory, auto brokers shop for the best prices for their clients from those auto dealers who are willing to work with the broker and pay the broker's fee (reportedly, usually a few hundred dollars) in exchange for the increased volume of sales. However, the state's reported 142 auto brokers, only 10 of whom reportedly broker in new cars, in practice work only with 25 to 30 auto dealers, out of the state total of 850 dealerships, apparently because no other

dealers are willing to work with brokers. According to newspaper reports, 5,000 to 7,000 new and used cars pass through brokers, as compared to the 750,000 new cars sold annually through new car dealerships.

Originally, legislation requested by the auto dealers would have banned third-party auto brokers outright; the legislation was amended in the Senate, instead, to require brokers to make public the names of the new car dealers they worked with and to reveal their brokering commissions.

THE CONTENT OF THE BILLS:

The bills, which are tie-barred to each other, would amend the Michigan Vehicle Code and the automobile dealers' franchise act to address concerns raised by automobile dealers and to extend to automobile distributors (of which there reportedly is only one in the state) the protections afforded dealers under the code. House Bill 4738 would require automobile brokers to record with the secretary of state their names, dealer's license numbers, and commissions, as well as to record the information currently required of new and used car dealers (which would include the names of dealers from whom brokers obtained cars for their clients). House Bill 4740 would add "importer" to the act's definition of "distributor," and "distributor" to the current definition of "new motor vehicle dealer," thereby affording distributors and importers the same current protections afforded dealers under the act and the same additional dealer protections proposed by the bill.

AUTO BROKERS

House Bill 4738 would amend the Michigan Vehicle Code (MCL 257.251) to require brokers to keep certain records, as prescribed by the secretary of state, of each vehicle that was "bought, sold, or exchanged by the dealer or received or accepted by the dealer for sale or exchange."

Currently, the code requires each new vehicle dealer and each used vehicle dealer to keep a record, in a form prescribed by the secretary of state, of each vehicle bought, sold, or exchanged by the dealer or received or accepted by the dealer for sale or exchange. Each such vehicle record must include the following:

** the date of the purchase, sale, or exchange (or receipt for the purpose of sale);

** a description of the vehicle;

** the name and address of the seller, the purchaser, and the alleged owner or other persons from whom the vehicle was purchased or received, or to whom it was sold or delivered; and

**a copy of all odometer mileage statements received by the dealer upon purchasing or acquiring a vehicle and a copy of the odometer mileage statement furnished by the dealer upon sale of a vehicle as prescribed in the vehicle code.

In addition to the information on vehicle information records required of new and used auto dealers, the bill also would require brokers -- but not new or used auto dealers -- to include in the records of the vehicles bought, sold, leased, or exchanged through them both (1) the broker's name and dealer license number (brokers are one of nine dealer classifications under the vehicle code; see BACKGROUND INFORMATION for the vehicle code's definition of "dealer" and list of nine dealer classifications) and (2) the amount of the broker's fee, commission, compensation, "or other valuable consideration" paid by the buyer or lessee or by the dealer, or both.

Broker vehicle records maintained by the secretary of state would have to be in an electronic format determined by the secretary of state.

Finally, the bill also would strike five subsections in this section of the code that expired on July 1, 1994. The stricken subsections contained certain record keeping requirements for vehicle salvage pool operators or brokers, used vehicle parts dealers, vehicle scrap metal processors, and foreign salvage vehicle dealers (subsections 7 through 10) and a subsection requiring the secretary of state to make periodic, unannounced inspections of used or secondhand parts dealers' records, facilities, and inventories.

AUTO DEALERS, DISTRIBUTORS, AND IMPORTERS

House Bill 4740 would amend five sections of the automobile dealer franchise act (Public Act 118 of 1981), and add one new section, to include auto distributors and importers in the definition of "new motor vehicle dealer" and "dealer agreement," but would not define "importer." In addition, the bill would rewrite and extend some of the protections currently given to auto dealers (and, newly, to auto

distributors and importers) in their business dealings with auto manufacturers: Manufacturers would be prohibited from requiring new car dealers (including auto distributors and importers) to pay for manufacturers' refunds or rebates; from "arbitrarily and capriciously" allocating new vehicles to dealers (distributors, importers); from requiring dealers (distributors, importers) to buy certain "essential" service tools unless the manufacturer also gave the dealer (distributor, importer) a good faith estimate of the number of new vehicles the manufacturer was going to allocate to the dealer (distributor, importer); and from preventing a change in the dealer's (distributor's, importer's) executive management unless the proposed change would result in management by someone who was "not of good moral character" or who didn't meet certain "reasonable, preexisting, and equitably applied manufacturer or distributor standards.

Definitions. Currently, the auto dealer franchise act defines, among other terms, "distributor," "new motor vehicle dealer" (which also is one of the nine "dealer" classifications in the Michigan Vehicle Code, but which is not defined in the code), and "dealer agreement". The bill would redefine each of these to include importers and distributors.

Currently, the dealer franchise act defines a "distributor" to mean "any person, resident or nonresident, who in whole or in part offers for sale, sells, or distributes any new motor vehicle to a new motor vehicle dealer" -- or who controls any person, resident or nonresident, who does this, or who maintains a factory representative, resident or nonresident. (Note: The act's definition of "manufacturer" also includes distributors. "Manufacturer" means "any person who manufactures or assembles new motor vehicles; or any distributor, factory branch, or factory representative." In contrast, the Michigan Vehicle Code defines "manufacturer" to mean "a person, firm, corporation or association engaged in the manufacture of new motor vehicles, trailers or trailer coaches or semi-trailers, as a regular business." [MCL 257.28] The vehicle code does not define "distributor.") The bill would redefine "distributor" to mean "any person, *including an importer*, resident or nonresident, who *is engaged in the business pursuant to a dealer agreement*, in whole or in part, of offering for sale, selling, or distributing new *and unaltered* motor vehicles to a new motor vehicle dealer, who maintains a factory representative for such purposes, resident or nonresident, or who controls any person, resident or nonresident, who in whole or in part offers for sale, sells, or distributes new *and unaltered* motor vehicles to a new motor vehicle dealer. *Distributor does not include a person who alters or converts motor vehicles for sale to a new motor vehicle dealer*."

Currently, the act defines "new motor vehicle dealer" to mean "a person ["natural person, partnership, corporation, association, trust, estate, or other legal entity"] who holds a dealer agreement granted by a manufacturer or distributor for the sale of its motor vehicles, who is engaged in the business of purchasing, selling, exchanging, or dealing in new motor vehicles and who has an established place of business in this state." The bill would redefine "new motor vehicle dealer" to mean "a person, *including a distributor*, who holds a dealer agreement granted by a manufacturer, distributor, *or importer*, for the sale *or distribution* of its motor vehicles, who is engaged in the business of purchasing, selling, exchanging, or dealing in new motor vehicles and who has an established place of business in this state."

Finally, "dealer agreement" currently means "the agreement or contract in writing between a manufacturer, distributor, and a new motor vehicle dealer, which purports to establish the legal rights and obligations of the parties to the agreement or contract with regard to the purchase and sale of new motor vehicles and accessories for motor vehicles." The bill would redefine "dealer agreement" to mean instead "the agreement or contract in writing between a distributor and a new motor vehicle dealer, *between and manufacturer and a distributor or a new motor vehicle dealer, or between an importer and a distributor or a new motor vehicle dealer*, which purports to establish the legal right and obligations of the parties to the agreement or contract with regard to the purchase and sale *or resale* of new *and unaltered* motor vehicles and accessories for motor vehicles."

Retail incentives. Currently, section 13 of the auto dealers' franchise act prohibits manufacturers and distributors from requiring new car dealers to do a number of things. (The act defines a "manufacturer" to mean "any person who manufactures or assembles new motor vehicles; or any distributor, factory branch, or factory representative." See above for the current and proposed definitions of "distributor" and "new motor vehicle dealer.")

One of the things that manufacturers cannot do is to require dealers to participate "monetarily," at the dealer's expense, in any advertising campaign or

contest, or to buy any promotional materials, or display "devices," decorations, or "materials." The bill would, in addition, prohibit manufacturers from requiring new motor vehicle dealers (who would include distributors and importers) from having to pay or assume any cost of a manufacturer's refund, rebate, or discount to ("or in favor of") a consumer in connection with the sale of a new motor vehicle, unless the dealer (distributor, importer) voluntarily agreed to do so.

Vehicle allocation. Currently, section 14 of the auto dealers' franchise act prohibits auto manufacturers or distributors from, among other things, doing any of the following:

(a) failing to deliver new motor vehicles, parts, or accessories within a "reasonable" time and in "reasonable" amounts ("relative to the new motor vehicle dealer's market area and facilities"), unless the failure is caused by "acts or occurrences beyond the control of the manufacturer or distributor" or results from a dealer order "in excess of quantities reasonably and fairly allocated by the manufacturer or distributor";

(b) refusing to disclose to dealers the "method and manner" of distribution of new motor vehicles by the manufacturer or distributor; or

(c) refusing to disclose to dealers the total number of new motor vehicles of a given model sold by the manufacturer or distributor in the dealer's "marketing district, zone, or region," whichever geographical area is the smallest.

The bill would delete each of these provisions and instead prohibit manufacturers or distributors from:

(a) adopting, changing, establishing, or implementing a plan or system for allocating and distributing new motor vehicles to dealers (including distributors and importers) that was "arbitrary or capricious";

(b) failing or refusing to advise or disclose to any dealer (including distributors and importers) having a dealer agreement, upon written request from the dealer (distributor, importer), the basis upon which (i) new motor vehicles of the same line make were allocated or distributed to dealers (distributors, importers) in the state and (ii) the current allocation or distribution was being (or would be) made to that dealer (distributor, importer);

(c) refusing to deliver, in reasonable quantities and within a reasonable time after receiving a dealer's (distributor's, importer's) order, vehicles that were covered in the agreement between the dealer (distributor, importer) and manufacturer and which were "specifically publicly advertised in the state by the manufacturer or distributor to be available for immediate delivery." However, the failure to deliver a motor vehicle wouldn't be considered to be a violation of the act if the failure were due to an "act of God," a work stoppage or delay because of a strike or "labor difficulty," a freight embargo, or any other cause over which the manufacturer or distributor had no control.

"Essential" service tools. Currently, a manufacturer or distributor cannot require a dealer to order, or accept delivery of, any new motor vehicle, part or accessory, equipment, or "any other commodity not required by law" that was not voluntarily ordered by the dealer. The bill would specify, in addition, that if a manufacturer or distributor required a dealer (distributor, importer) to buy "essential service tools" (not defined in the bill or the act) costing more than $7,500 in order to receive a specific model vehicle, the manufacturer or distributor would be required, upon written request, to provide the dealer (distributor, importer) with a written good faith estimate of the number of vehicles of that specific model the dealer (distributor, importer) would be allocated during the model year in which the tool was required to be bought.

Dealer management control. The bill would add a new provision that prohibited manufacturers or distributors from preventing (or trying to prevent), "by contract or otherwise," a dealer (distributor, importer) from changing executive management control unless the manufacturer or distributor, who would have the burden of proof, could show that the change would result in executive management by a person or persons who were "not of good moral character" or who didn't meet reasonable, preexisting, and equitably applied manufacturer or distributor standards. If a manufacturer or distributor rejected a proposed change in executive management, it would have to give written notice of its reasons to the dealer (distributor, importer) within 60 days after having received written notice by the dealer (distributor, importer) of the proposed change ("and all related information reasonably requested by the manufacturer or distributor"). Otherwise, the change in executive management would be considered approved.

Applicability. The bill would apply to agreements in existence on, or made after, the bill took effect, and the bill would be given immediate effect.

MCL 445.1562 et al.

BACKGROUND INFORMATION:

The Michigan Vehicle Code defines "dealer" to mean a "person" (defined in the code as "every natural person, firm, copartnership association, or corporation and their legal successors") who does any of the following:

(a) "engage[s] in the business of purchasing, selling, exchanging, brokering, or dealing in vehicles of a type required to be titled" under the act;

(b) "negotiates the purchase, sale, deal, or exchange of those vehicles and who has an established place of business for those purposes in this state";

(c) "engage[s] in the actual remanufacturing of engines or transmissions, or both"; or

(d) "engage[s] in the business of buying vehicles to sell vehicle parts or buying vehicles to process into scrap metal."

Under the act, a "dealer" doesn't include "a person who buys or sells remanufactured vehicle engine and transmission salvageable vehicle parts or who receives in exchange used engines or transmission if the primary business of the person is the selling of new vehicle parts and the person is not engaged in any other activity that requires a dealer license."

The vehicle code lists nine dealer classifications. The code defines four of the nine dealer classifications: "used or secondhand vehicle parts dealer,""vehicle scrap metal processor,""foreign salvage vehicle operator," and "automotive recycler." The vehicle code doesn't define "new motor vehicle dealer" (though it does define "new motor vehicle"), "used or secondhand motor vehicle dealer" (though it does define "used or secondhand motor vehicle"), "vehicle salvage pool operator" (though it does define "vehicle salvage pool"), "distressed vehicle transporter" (though it does define "distressed vehicle" and "transporter"), or "broker."

The nine dealers classifications in the vehicle code are as follows:

(1) New motor vehicle dealer. The vehicle code, unlike the auto dealer franchise act, doesn't define "new motor vehicle dealer," but the vehicle code does define "new motor vehicle" in section 33a to mean "a motor vehicle, which is not and has not been a demonstrator, executive or manufacturer's vehicle, leased vehicle, or a used or secondhand vehicle."

The auto dealer franchise act (Public Act 118 of 1981), in contrast, defines "new motor vehicle" to mean "a motor vehicle which is in the possession of the manufacturer, distributor, or wholesaler, or has been sold only to a new motor vehicle dealer and on which the original title has not been issued from the new motor vehicle dealer." "New motor vehicle dealer," in turn, is defined to mean "a person who holds a dealer agreement granted by a manufacturer or distributor for the sale of its motor vehicles, who is engaged in the business of purchasing, selling, exchanging, or dealing in new motor vehicles and who has an established place of business in this state."

(2) Used or secondhand vehicle dealer. The act doesn't define "used or secondhand vehicle dealer," but does define "used or second-hand vehicle" in section 78 to mean "any motor vehicle to which a certificate of title and license plates have been issued and which motor vehicle has been registered for use on the highways by a consumer or by a dealer."

(3) Used or secondhand vehicle parts dealer (Section 78a) means "a person engaged in the business of buying or otherwise dealing in vehicles for the purpose of dismantling the vehicles to sell used parts and remaining scrap metal or a person engaged in the business of buying, acquiring, selling, or otherwise dealing in salvageable parts."

(4) Vehicle scrap metal processor (Section 79b) means "a dealer engaged in the business of buying or otherwise acquiring vehicles for the purpose of processing and selling the metal for remelting," and who is prohibited from selling "major components or other parts for vehicle repair purposes, unless [the processor] first obtains a used or secondhand vehicle parts dealer license."

(5) Vehicle salvage pool operator. The code doesn't define "vehicle salvage pool operator, but section 79a does define "vehicle salvage pool" to mean "a person engaged in the business of storing and displaying damaged or distressed vehicles as an agent or escrow agent of an insurance company."

(6) Distressed vehicle transporter. The code doesn't define "distressed vehicle transporter," but section 12a defines "distressed vehicle" to mean "a vehicle that has a major component part that has been wrecked, destroyed, damaged, stolen, or missing to the extent that the total estimated cost of repairs to rebuild or reconstruct the vehicle, including parts and labor, is equal to or exceeds 75 [percent] of the actual cash value of the vehicle in its predamaged condition," while section 76 defines "transporter" to mean [a] "every person engaged in the business of delivering vehicles of a type required to be registered hereunder from a manufacturing, assembling or distributing plant to dealers or sales agents of a manufacturer, and [b] every person certificated by the Michigan Public Service Commission to engage in the business of moving trailer coaches or mobile homes."

(7) Broker. The code doesn't define "broker."

(8) Foreign salvage vehicle dealer (Section 17a) means "a person who is a licensed dealer in another state and is engaged in this state in the business of purchasing, selling, or otherwise dealing on a wholesale basis in salvageable parts or vehicles of a type required to have a salvage or scrap certificate of title under the act."

(9) Automotive recycler (Section 2a) means "a person who engages in business primarily for the purpose of selling at retail salvage vehicle parts and secondarily for the purpose of selling at retail salvage motor vehicles or manufacturing or selling a product of gradable scrap metal."

FISCAL IMPLICATIONS:

According to the Senate Fiscal Agency, there could be an increase in administrative costs to the Department of State from new electronic formatting requirements in House Bill 4738 (6-3-98), while House Bill 4740 would have no state or local fiscal impact (5-26-98).

ARGUMENTS:

For:

The auto dealers argue that House Bill 4738 is needed to protect both consumers and the dealers. As the May 22, 1998 *Detroit News* editorial notes, the auto dealers "assert that brokers pose unfair competition to established dealerships, many of them family-owned, and often mislead or defraud buyers." Auto dealers point out that, unlike dealers, brokers are not required to notify their clients of retail incentive programs, and that brokers emphasize price, to the exclusion of quality and service, with no assurance that the brokered price is in fact the lowest available price. In addition, dealers argue, customers have no recourse against brokers who misrepresent prices, financing, servicing, warranties, or the applicability of the auto lemon law. Further, brokers, unlike dealers, do not have to maintain the substantial investment in parts, service facilities, equipment, and staff that dealers must maintain, nor do brokers have the same "knowledge base" of the automobiles to pass on to customers that dealership employees, who are constantly trained and retrained, have.

Brokering also disrupts manufacturers' vehicle allocation and distribution systems, since brokers can choose to deal in only the most desirable cars instead of whole lines of vehicles from a manufacturer. Brokers, moreover, are not subject to the self-correction of the "Consumer Satisfaction Index" (CSI) that manufacturers use to evaluate dealers nor to manufacturer requirements placed on dealers to provide facilities and staff to do warranty service. Brokers also are not subject to the same laws that dealers are, such as the auto dealers franchise law, the auto lemon law, and the odometer law. Finally, brokering hurts car salespeople by depriving them of their commission income, the basis of their livelihood.

The dealers assert that the bill would create "an equal playing field," presumably by requiring auto brokers to meet the same reporting requirements-- including odometer mileage statements -- that new and used car dealers now have to meet under the vehicle code.

Response:

The bill is anti-compeitive and anti-consumer. Even though the revised version doesn't ban brokering outright, as was originally proposed, its "dealer disclosure" requirements would effectively put new car brokers out of business by eliminating their sources of new cars for their clients. For, once brokers are required to reveal the names of the auto dealers from whom the brokers obtain cars for their customers, the 25 to 30 brokers who reportedly currently are willing to work with brokers are virtually certain to come under immense pressure from the auto manufacturers and other dealers to stop cooperating with brokers. The effectiveness of industry pressure against "maverick" dealers already is evident in the campaign by the industry against maverick dealers that successfully kept Detroit dealerships from opening on Saturdays for many years.

As a June 9, 1998, *Detroit Free Press* editorial notes, "the bill originally was an outright ban on brokers. This latest version is an end-around intended to discourage dealers from working with brokers, who say flatly that it would drive them out of business in no time. In the stated interest of consumers, the Federal Trade Commission has repeatedly rebuffed attempts by dealer organizations to ban their members from working with brokers. Car companies and dealer groups still discourage dealers from working with brokers, but some dealers do it anyway, on the quiet, mainly because they like to sell cars. Brokers . . . pursue the best prices from those dealers who are willing to work with them in return for the sales volume. In the overall scheme of car sales, it's not a lot. Brokers sell 5,000 to 7,000 cars a year in Michigan, new and used. Dealers sell 750,000 new cars a year, so brokers can hardly be seen as a threat to them. The threat, brokers say, would be to dealers named in easily accessible public records, inviting the wrath of other dealers and who-knows-what pressures from the same folks who battled the federal government fo 20 years to keep Detroit-area showrooms closed on Saturdays." A May 22, 1998, *Detroit News* editorial notes that "[o]ne of the ways consumers get good prices for themselves is hiring independent auto brokers, who specialize in buying cars for their clients at the best possible price. Brokers say they sell their buying expertise and knowledge of the availibility of models to their customers in return for a fee. Independent brokers handle only a fraction of the state's vehicle trade -- about 5,000 sales annually. But because they have more knowledge of the market than the average consumers, it can be argued that auto brokers help to place a check on prices. Forcing disclosure of broker fees and discounts with particular dealers would expose those dealers to intense industry pressure to end the practice of selling through brokers. Dealers are under no obligation to offer brokers a discount. Those who do evidently have inventory to clear or are willing to trade profits for volume. The anti-broker bills are thus an attempt by the dealer lobby to limit market competition." Even the bill's sponsor is quoted in *The Renaissance Times* (December 15, 1997) as saying that under the revised version of the bill brokers "will pretty much be out of business if the legislation passes. It would be a devastating blow."

As to the dealers' other charges about "unfair competition," some of the requirements placed on the dealers, but not the independent brokers, are done so by the auto manufacturers from whom the dealer holds a franchise. Dealers already are protected from unfair manufacturer practices by the auto dealer franchise act, and the bill's companion bill (House Bill 4740) would strengthen these protections for new car dealers (but not brokers) even further. If the dealers have complaints about having to meet manufacturer requirements -- whether notification of retail incentive programs, manufacturer Consumer Satisfaction Index evaluations, the maintenance of complete lines of manufacturers' vehicles, or manufacturer requirements that dealers maintain facilities and staffing for warranty service -- then the dealers should take this up with the manufacturers. Why <u>should</u> brokers, who are independent agents, be subject to manufacturer requirements in the same way as dealers, who have formal business connections with the manufacturers? Dealers also claim that brokers don't have the same "knowledge base" about cars to pass on to their customers that the dealers' employees have, but both brokers and dealers pass on basic information to consumers. And brokers may even give consumers more, and more relevant, information than car salespeople, who have an obvious incentive to sell cars from their dealerships, do. As the May 22, 1998 *Detroit News* editorial points out, brokers have more knowledge of the market than the average consumer and brokers sell their buying expertise and knowledge of the availability of models to their customers in return for a fee. Just because brokers pose competition to dealers is no reason to eliminate brokering, whether outright or in the round-about way proposed in the bill. And as the editorial concludes, "[a]fter all, if dealers are so worried that brokers are stealing their business, they can fight back by offering better service at more competitive prices. If brokers really are as bad as the dealers say, the consumers can be trusted to figure it out for themselves." While brokers may indeed "disrupt the manufacturers' vehicle allocation and distribution systems," those systems already are under pressure to change, as is evidenced for the reasons offered by the dealers for the need to strengthen their protections from vertically-integrated manufacturer-owned "megadealerships." Further, however, it can be argued that brokers are only responding to perceived needs in the market, only from the consumer's perspective and not that of the dealer or manufacturer. Finally, it also can be pointed out that while changing market demands often are uncomforable for established ways of doing business, such as the current and impending changes in the marketing of cars, if more dealers chose to work with brokers, brokering could actually help dealers. For example, if a dissatisfied customer decided not to buy a car from a dealership, a broker might be able to sell that customer a car obtained from that dealership.

Though this would mean a lower profit for the dealership, a lower profit surely is better than no profit at all.

Reply:

With regard to the possibility that the bill would "afford manufacturers the opportunity to pressure dealers into not dealing with brokers," the December 30, 1998, letter from the governor to the House of Representatives argues, that "even as noted by legal counsel for the Michigan Automobile Dealers Association, there is no way of using such information against brokers. Federal and state anti-trust laws provide strong civil and criminal penalties for two or more persons who conspire to put another out of business. Further, if there were such evidence, the legislature would be quick to act to address any misuse of the process."

Against:

Although the auto dealers argue that House Bill 4730 would simply "level the playing field" by requiring brokers file the same information with the secretary of state that new and used car dealers currently must do, in fact the bill would go further than that and would require the brokers to disclose information that dealers currently are not required to reveal and, under the bill, would not be required to reveal. For the bill would require brokers not only to record the date of the purchase, sale, or exchange (or receipt for the purpose of sale), a description of the vehicle, the name and address of the seller, the purchaser, and the alleged owner "or other persons from whom the vehicle was purchased or received, or to whom it was sold or delivered," and a copy of all odometer mileage statements -- all of which information new and used car dealers currently must record -- it would require brokers, and only brokers, to disclose the amount of their commission ("the amount of the broker's fee, commission, compensation, or other valuable consideration paid by the purchaser of lessee or paid by the dealer, or both"). As the June 9, 1998 *Detroit Free Press* editorial notes, "the dealers say that disclosing the names and commissions will be a help to consumers. More likely, it will be a help to dealers who don't want to deal with brokers, and who, incidentally, are not required to disclose their own sales commission." And as the May 22, 1998 *Detroit News* editorial points out, "Auto dealers certainly don't disclose their mark-up to customers, however. Nor should they have to. Profit margins reflect competitive realities, and savvy consumers are free to comparison shop." At the very least, if brokers are to be required to reveal their commissions, then, so, too, should dealers. Only then, at least with respect to this one point, would the "playing field" be "leveled."

For:

House Bill 4740 is necessary to protect dealers' and their investments, including the many dealerships that have been family-owned for generations. By extension, the bill would protect the communities in which such dealerships play such an important economic and social role. The changing marketplace -- including the proliferation of new automotive products and dealers and the expensive technology that is needed to service these new products -- has put auto dealers at an increasing disadvantage in their dealings with the automobile manufacturers, despite the protections in the current auto dealer franchise act.

For example, given the immense popularity of the so-called "sport utility" vehicles (which, according to one estimate, comprise as much as 40 percent of the new motor vehicle marker), some Ford-Lincoln-Mercury dealers were dismayed to learn that Ford Motor Company planned to limit the availability of its new luxury sport utility vehicle, the Lincoln Navigator, to only those Ford-Lincoln-Mercury dealers whose localities had averaged a minimum of at least 70 annual retail luxury car registrations over the past four years. The January 1997 letter informing those dealers who would be shut out from offering this new product said that Ford's decision was "due to the limited volume of units to be produced" and their plans to focus their marketing and retailing efforts in "those high potential areas where [their] target customers reside." As one dealer from northern Michigan pointed out in a letter to Ford, northern Michigan demographics are such that although people don't usually buy certain luxury vehicles because of the difficulty of driving these cars in the snow, the market for upscale "4x4" trucks and utility vehicles, as well as "highline" conversion vans, is enormous. So to deny northern Michigan Ford-Lincoln-Mercury dealers the opportunity to sell an upscale sport utility vehicle such as the Lincoln Navigator based on the fact that the dealers had not sold enough Lincoln Continentals or Town Cars is not only illogical and absolutely counter to the specific demographics of this area of the state, but prejudicial to northern Michigan dealerships, who will lose their upscale sport utility customers to competing brand dealerships.

However, in addition to this potential threat to small-to-medium sized "outstate" dealerships, dealers have been alarmed by a trend in the automotive industry toward"super-sized" factory-owned dealerships

(sometimes called "megastores"). Although factory-owned dealerships are an anomaly in the United States because factories have preferred to have individual entrepreneurs sell their products, Ford Motor Company recently rocked the world of traditional auto dealerships by indicating that it wanted to acquire control of all Ford and Lincoln-Mercury dealerships in metropolitan Indianapolis. In early May 1997, Ford asked its Ford and Lincoln-Mercury dealers in the Indianapolis market to sell their dealerships to a new company that would be owned by Ford and the dealers and that would reduce the number of dealerships from 18 to five experimental "megastores." The new megastores would be operated as a single company and overseen by a Ford-appointed manager, probably one of the current Indianapolis dealers, and would be supplemented by a new network of four to five free-standing Ford Auto Care retail service centers. While one Indianapolis Lincoln-Mercury dealer believes that what Ford is proposing is ultimately what will happen with all manufacturers, and that inevitably the number of auto dealers will be downsized, the implications for small-to-medium-sized dealerships are certainly less than positive.

Given the economic and social importance of these dealerships in non-metropolitan areas -- which, in Michigan, means most of the state -- this trend could have disastrous effects not only on the dealerships themselves but on the small communities in which they play such an important economic and social role. And from a strictly business point of view, studies of customer satisfaction not surprisingly reportedly all show that small-to-medium-sized dealers have the highest level of customer satisfaction and loyalty, which is certainly in the best interests of the manufacturers. Small-to-medium-sized dealerships know their customers personally, and customers rely on their dealers to provide them not only with sales and services, but with the kind of community participation -- from volunteer community work to running for elected office -- that both sustains and strengthens their communities. Should small-to-medium-sized dealerships disappear, either through loss of customers due to being cut off from offering new automobile products or through replacement by megadealerships located in metropolitan areas, the resulting loss to their communities could truly be devastating.

The bill would address some of these issues by prohibiting manufacturers from capricious or arbitrary distribution of their products to dealers, and by supporting the continuation of family-owned dealerships through guarantees that changes in executive management would not be restricted on arbitrary grounds, as well as adding provisions regarding manufacturer rebates and "essential tool" requirements. The bill is pro-people and pro-small business.

Response:

The bill, like the original 1981 legislation, is an unnecessary and unwarranted government intrusion into the private business dealings between auto dealers and auto manufacturers that has the potential to harm consumers by increasing the prices they have to pay for goods and services that properly should be regulated by the free market.

In a time when many markets are being "globalized", the unfortunate fact is that many traditional ways of doing business -- not to mention working conditions -- have been changed drastically, and automobile dealerships are not -- and should not be -- immune to changing market pressures. If, as many people believe, the free market is the best way to maximize the quality of goods and services available to consumers, then the bill is a step backwards from promoting the rule of the free market.

Against:

House Bill 4740 is anti-consumer, and will raise car prices while reducing competition. On a more philosophical level, the bill -- and the act itself -- is unjust: from the point of view of those who argue that the proper role of government is to protect the rights of property and contract, the increased restrictions on franchise agreements proposed by the bill would use the government to take rights away from one set of persons (namely, consumers) and give them to another (namely, auto dealers). Rather than amend the act to increase protections for auto dealers from competition on the open market, the bill should be decreasing these protections if not outright repealing the act itself.

As a May 1997 paper from the Hillsdale Policy Group, Ltd. ("The Effect of Motor Vehicle Franchise Regulation on Vehicle Prices, Consumer Choice and the Political Process," co-authored by former state Representative Lynn Jondahl and former Michigan Deputy State Treasurer for Taxation and Economic Policy Gary Wolfram), points out, the effects of state restrictions on vehicle distribution that is embodied in vehicle franchise legislation is well-established in economics literature: such legislation creates a monopoly situation that gives dealers the ability to restrict the supply of vehicles and increase vehicle prices. Increases in vehicle prices result in fewer

sales, and fewer sales will reduce employment in vehicle manufacturing and related industries. Thus, by increasing the restrictions on manufacturers in their contractual relationship with their dealers, the bill would serve to increase vehicle prices, increase vehicle search costs for consumers, reduce services, and reduce the number of vehicles sold. Rather than further protecting a special business interest -- the automobile dealers -- the legislature should be benefiting consumers, which would entail doing just the opposite of what the bill proposes. That is, the legislature should be reducing -- or even eliminating -- the franchise restrictions and allowing the market to determine what the individual dealer's market area should be and what should be in the contract between franchisers and franchisees.

More specifically, the paper quotes studies showing that state franchise restrictions increase vehicle prices to consumers anywhere between 6.14 percent and 14.1 percent, a transfer of wealth primarily from consumers to dealers as a result of higher vehicle prices. In Michigan, applying the 6.14 percent figure to new vehicle registrations of 680,713 and an average new vehicle price of $20,000, this transfer from consumers to dealers comes to more than $830 million annually (and obviously, the 14 percent rate would more than double this amount). In addition to a 1986 Federal Trade Commission report supporting these conclusions (which originally were drawn from earlier studies), at least three states -- Florida, Tennessee, and Texas -- also have released reports concluding that laws regulating the relationship between motor vehicle manufacturers and their dealers are unnecessary and result in higher consumer prices. The bill cannot stop the current pressures on auto dealers and should not try to do so. As unfortunate as economic dislocation always is to those directly and adversely affected, the state should not be involved in trying to protect private businesses from the forces of the marketplace.

Against:

As amended by the Senate, House Bill 4740 would give the same statutory protections to auto distributorships (newly defined to include importers) as the law currently provides to auto dealerships, extending already anti-competitive, anti-consumer legislation even further. There not only seems to be no good reason to do this, but this provision reportedly would in fact apply to only a single business located in Grand Rapids, Great Lakes Mazda. In addition, questions have been raised, in the absence of any apparent policy reason for extending current new car dealer protections to this one business, concerning the fact that the owner of the business is a major contributor to one of the two major political parties. Rightly or wrongly, this gives at least the appearance that legislation can be "bought" by political contributions, which should be avoided absent any compelling public policy grounds.

Response:

The Senate sponsor of the Great Lakes Mazda amendment responded to an attempt to delete this amendment in June 4, 1998, remarks on the floor of the Senate as follows: "Our job in this body is to do the best that we can for people, family, employees, labor unions, charitable organizations, community foundations, yes indeed, companies, business to build our state's future. The franchise legislation that we're dealing with involves the relationships of how you sell cars in Michigan that ought to be the auto giant of the 21st century. Franchise relationships carve up market share, allocation of, whether it's Ford Expeditions or Ford Taurus, GM cars, Chrysler, you name it. What we're trying to do is, within this existing structure, have some type of relationships among and between the whole stream of commerce and selling cars. We're doing that in respect to dealers. We're doing that in respect to manufacturers and yes, indeed, a company in Grand Rapids that employs 110 people, roughly, has $50 million of investment in terms of capital that runs their business in terms of distributing cars across the state of Michigan. A third of those employees are teamsters and why we should not have them part of a franchise relationship in Michigan would be a mistake. We're making sure that this business, like any other distributor or any other business in the line of commerce and chain and stream of commerce in cars, has the same protections as any other type of business. To imply that we're doing this because they made political contributions insults everybody in this body. Whether it is Hoote McInery making contributions, the Detroit auto dealers, the Michigan auto dealers, unions who work for those companies, Dirk Waltz Buick, or Mazda Great Lakes, or the people of the families who work there, they can make any decisions they choose. But nobody in this body is making decisions based on who might have done what for whom. I think that needs to be addressed, and I am. We're making this decision by recommendation because Michigan companies, Michigan employees, ought to be afforded in Michigan law in how we govern transactions in franchise agreements in the state of Michigan."

Reply:

As opponents of the original 1981 act argued, the government should not, in fact, be involved in setting the terms and conditions between private businesses in

the first place. The bill would make a bad law worse from the point of view of both consumers and those who are philosophically opposed to government attempts to micromanage the private sector.

Against:

Amending the definition of "distributor" to include "importer," and the definition of "new motor vehicle dealer" to include "distributor, poses potential problems. For, by nesting the definitions of "importer," "distributor," and "new motor vehicle dealer," the very rationale for the act in the first place -- the protection of new car dealers from potentially harmful decisions made by powerful manufacturers and distributors -- would seem to become moot if a "dealer" also could be one of those powerful manufacturers or distributors (the act currently includes "distributor" in its definition of "manufacturer"). Apart from trying to tease out the legal implications of including virtually all of the major players -- manufacturers, distributors, dealers, and now importers -- in each others' definitions, wouldn't the bill give distributor-manufacturer-importers virtual carte blanche in their business dealings while at the same time granting them the special dealer protections currently provided under the act and proposed under the bill? What would this mean in actual practice? For example, what would a "dealer agreement" between a distributor and itself, which apparently would be allowed under the bill, even look like?

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■This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.