The January 19, 2016 Federal Trade Commission Public Workshop on Auto Distribution

Enlightenment or Failure?

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The FTC Workshop attempted to explore competition, in the context of regulation, of motor vehicle distribution, and how those regulations affect consumers. It was hoped the government would have produced a "principled discussion of significant policy issues by providing balanced analyses of different points of view, . . . and that the arguments for and against the regulations would be addressed, including their alleged need, as well as their impact on the parties to the distribution relationship, the competitive process and the consuming public." (See American Bar Association, Section of Antitrust Law, Monograph 17, Franchise Protection: Laws Against Termination and the Establishment of Additional Franchises.) That was not the case. A review of the four workshop presentations revealed the absence of any automobile dealer, although the affected constituents were the governments which regulate, the consumers who buy, and the dealers who sell. There was not one economist or academic who spoke on behalf of the current system, or from the point of view of the dealer. Neither was this one-sided approach presented by any economist or academic with more than a rudimentary understanding of the industry. The inclusion of four biased economist/academicians provided by the government, each of whom appeared to vigorously oppose regulation of the relationship between the automobile manufacturer and the seller of the manufacturers' products resulted in a one-sided, unbalanced exploration of the industry. One of the economists had spent time as a secret shopper investigating auto repair shops, had written and lectured about user behavior in auction "including non-rational herding, quasi-endowment effect, escalation of commitment and irrational limited attention base of field experiments" involving the eBay marketplace. This panelist had also studied "lemon problems" in the used car market and the role of leasing in the new car market. There was no indication this panelist had studied, in granular detail, the manufacturer dealer relationship, manufacturer intrusion into the dealer's business, or understood the vulnerability of a dealer to the manufacturer, nor the fundamental difficulty of the weaker party from effectively protecting itself or its customer. On the contrary, there was an impression that some of the regulation victimized the manufacturers.

Neither did any of the economist academics explore the fundamental terms of every Dealer Agreement which effectively grant the manufacturer "the authority to exercise near life and death economic power over" the dealership. (See *Manhattan Motorcars, Inc. v. Automobili Lamborhini, S.p.A., et al.*, 2007 U.S. Dist. LEXIS 49641.) Neither did any economist discuss the significance, pro or con, of the manufacturer requirement that every dealer provide regular, excruciatingly detailed monthly reports to the manufacturer concerning their sales, inventories, customer data, profit, cash on hand, cash in the bank, used cars and trucks available, economics and figures regarding the real estate used by the dealership, expenses, salaries of owners, supervisors, clerical and other employees, employee benefits, office supplies, advertising, contributions, to name a few. Neither did any of the economic academics present or discuss relevant or detailed information regarding manufacturer requirements that dealerships make available and turn over proprietary information to the manufacturer on an ongoing basis with the use of third party computer companies hired by the manufacturer to install intrusive, overbearing computer software allowing manufacturers and their vendors to unilaterally look into every aspect of a dealer's business including customer base. These are the very same manufacturers portrayed by the Workshop economists as victims of government regulation . Neither did any of the economists give arguments for or against the manufacturer's practice of requiring, with severe economic penalty, regular massive facility changes and upgrades with complete manufacturer control of everything and everyone in the process, including the required manufacturer architect, the required manufacturer vendor for every material component from signage outside and inside, to floor treatment and window dressing.

Another of the economists announced at the beginning of his presentation that he had little knowledge of the automobile industry. Another was described as a public advocate, and a third spent a fair amount of her presentation defending criticism of some of her earlier research which had been handed out to attendees. This earlier research included a 2010 paper which, among other things, discussed "Outcomes of Car Dealership Regulations", and in referring to a 1956 description of the evolution of the car industry, pointed out that Kessler, in 1957, "foreshadows some of our later discussion by *emphasizing how the Dealer Day in Court law was likely to cause problems in the long term by limiting flexibility.*" (See *Markets, State Franchise Law, Dealer Terminations, and the Auto Crisis*, by Francine Lafontaine and Fiona Scott Morton, *Journal of Economic Perspectives*, Volume 24, Number 3, Summer 2010, pages 233-250). Had the author contacted any dealer lawyer about the Dealer Day in Court Law, she would no doubt have discovered how largely useless and ineffective is the Dealer Day in Court Act, an act which, certainly did not limit any manufacturer's flexibility. The failure of the Federal Trade Commission economists and academicians, with all their gravitas and credentials, to present both sides of issues regarding the relationship between auto dealers and auto manufacturers was fundamental and misleading. The current and continued imbalance resulting from the overwhelming economic power of billion dollar manufacturers over auto dealers is alive, well and flourishing, mitigated only slightly by some of the state franchise laws. This imbalance continues in spite of some of the consolidation in the industry. For example, manufacturers currently limit the number of inter brand stores a public company may own, and they are now exploring limitation of the market areas in which those public companies can own more than one store, thus unfairly depressing the value of any dealership seeking to sell to a public company. Furthermore, since the manufacturers control ownership through restrictive provisions, including rights of first refusal, control over who a buyer might be, and furthermore can terminate the dealer for multiple different reasons, the life of a dealer is wholly controlled by the manufacturer, and the dealer's options are generally limited to swallowing the control, and following the rules, which incidentally, the manufacturers have the right to and do unilaterally amend with frequent addenda.

In addition, certain manufacturers withhold "niche" models and give them to "favored nation" dealers, certain manufacturers threaten to restrict model, price, options and color unless dealers take what they tell them to take (although certain states prohibit this kind of dumping, the subtlety of how manufacturers accomplish this, without audit or written trail, was not discussed by any of the academician/economists). Had there been a dealer on the panel willing to talk about these manufacturer processes, that person would have been concerned about the threat of retaliation. Neither was the audience educated regarding the adhesive nature of the dealer agreements. In over twenty-five years of representing automobile dealerships, this writer has never had the opportunity to revise the printed form or the Standard Provisions of a manufacturer in connection with the appointment of a dealer. What does this say about the bargaining position between manufacturer and dealer? No dealer tells a manufacturer what its Dealer Agreement will say. These are true contracts of adhesion, and the more popular the manufacturer brand, the more adhesive the contract, the contract addenda and the manufacturer control.

The manufacturer also has control over to whom a dealer may sell its dealership. If the manufacturer does not like the buyer, it can reject the buyer, and a lawsuit ensues. If a dealer wants to leave his dealership to his heirs, in the form of a trust, state laws do not protect that right, and manufacturers are not required to allow such an estate plan. If a dealer does not place appropriate signage on a bathroom door, or put the appropriate furniture, computer or coffee machine in the waiting room, the manufacturer is free to withhold product and various significant economic incentives from the dealer. If a dealer attempts to figure out how the manufacturer is allocating its cars, the byzantine manufacturer process is guarded and the truth rarely comes out. The great Honda Scandal, in which the manufacturer chose favorite dealers to whom they gave special cars, or open points, in exchange for bribes of gold watches and bags of cash, gives an indication of the power of the manufacturer.

Which economist on the panel explained that the life blood of the dealer was the proper flow of product from the manufacturer, and that this unilateral control was so overwhelming that regardless of government regulation the average dealer has neither the money, nor the courage to sue or threaten to sue a manufacturer, for fear of reprisal? Which academic told the audience about the practice of manufacturers requiring frequent facility upgrades coupled with profit per vehicle? Did the audience understand that a dealer refusing to spend ten million dollars on a facility upgrade at the whim of a manufacturer every six to ten years would be met with overwhelming economic penalty? Some states have prohibited a manufacturer from requiring these upgrades within a certain number of years. There are numerous stories of dealers in the middle of a required multi-million dollar factory upgrade necessary to compete with other inter brand dealers, only to find the factory facility specifications were changing, so that upon completion, they were confronted with other dealers having a more modern upgrade, thus forcing compliance with the new standard in order to compete. The overwhelming power of the manufacturer to control the sale price of its product, and even, in spite of antitrust laws, to give special pricing to those dealers who accomplish certain facility upgrades, makes clear the imbalance between dealers and manufacturers. Finally, it must be obvious even to all the economists who oppose regulation, that the manufacturer which controls the pricing is not particularly concerned about the consumer. What concern for the consumer has been shown by the manufacturer now faced with billions of dollars of damage regarding cheating on the diesel emission standards? What is that manufacturer doing for the consumer other than controlling damage and attempting to get out of a mess as cheaply as possible?

Why does the consumer benefit from a relatively small and halfhearted amount of manufacturer dealership franchise regulation regarding a product as basic and essential as their automobile? Because without the regulation which the FTC Workshop economists and academics oppose, the consumer would have to rely on the good faith of the manufacturer to protect the consumer's interest. Would an educated consumer want to rely on the people who gave us the diesel cheating scandal, the ignition switch scandal, the air bag scandal, "Hondagate", the rollover scandal, the unintended acceleration scandal, the bankruptcy scandal, the constant recall scandal?

At the least, the Federal Trade Commission, charged with the duty of "Protecting America's Consumers", had an obligation to present its constituency with a balanced discussion of both sides of the issue. The economists and academicians hand picked by the FTC did not do that, nor is there any indication the FTC sought such a view.