



California New Car Dealers Association

March 3, 2016

Federal Trade Commission
Office of the Secretary
600 Pennsylvania Avenue NW, Suite CC-5610 (Annex B)
Washington, DC 20580

**Re: Comments of California New Car Dealers Association regarding FTC
workshop on state automobile distribution regulation**

Dear Commission Members:

The following comments are respectfully submitted for the record in the matter of the workshop on state automobile distribution regulation conducted by the FTC on January 19, 2016 (the "Workshop") and are submitted on behalf of the California New Car Dealers Association ("CNCDA"). CNCDA is a non-profit organization whose members are California new motor vehicle dealers. Over 1,100 dealers are CNCDA members, representing approximately 85% of all California new vehicle dealers.

The Workshop panels addressed four major areas: dealer termination and RMA (relevant market area or "encroachment") laws; warranty reimbursement regulation; laws prohibiting direct retail sales by manufacturers; and new developments and future trends. The common thread running through all of the panels, however, was the impact of state laws on automobile distribution.

The nation often looks to California to lead in regulatory matters. In this area, California does in fact offer an excellent example of how the predominance of state law in these areas maximizes fairness, flexibility, and consumer protection to the benefit of consumers and all other stakeholders. The following introductory section to recent legislation, adopted by California's Legislature and Governor, summarizes the continued public policy behind (and need for) reasonable and flexible vehicle franchise laws:

"The new motor vehicle franchise system, which operates within a strictly defined and highly regulated statutory scheme, assures the consuming public of a well-organized distribution system for the availability and sale of new motor vehicles throughout the state, provides a network of quality warranty, recall, and repair facilities to maintain those vehicles, and creates a cost-effective method for the state to police those systems through the licensing and regulation of private sector franchisors and franchisees." California Statutes, 2015, Chapter 526, Section 1(b).

Dealer termination and RMA laws.

Contrary to comments by some Workshop participants, state laws addressing a manufacturer's proposed termination of a new vehicle dealer's franchise or proposed addition of a new dealer within the market area of an existing dealer ("add point") neither prohibit nor unreasonably condition the manufacturer's freedom to act.

In California, contractual rights to terminate dealerships and to create add points are fully available to a manufacturer, subject to a dealer's right to protest those actions under Vehicle Code sections 3060 (termination) or 3062 (add point). These protest rights simply provide a forum for the dealer to seek an independent evaluation of whether good cause exists to terminate the dealer or whether good cause exists to prohibit the manufacturer from adding a new dealership. Note that in the latter case, it is the dealer who has the burden of proof to affirmatively demonstrate good cause sufficient to prevent establishment of the new dealership, Vehicle Code § 3066(b). In an add-point protest, the New Motor Vehicle Board is mandated by statute to consider whether "the establishment of an additional franchise would increase competition and therefore be in the public interest." Vehicle Code § 3063(e).

Some commentators contend that the franchise laws impose undue restrictions on manufacturers or have outlived their usefulness. However, it is important to remember that these laws:

- By definition examine all existing circumstances, including changed circumstances.
- Provide a process, not a pre-determined outcome.
- Employ balancing tests to arrive at a reasonable outcome, considering the interests of the consuming public, dealer, and manufacturer.

California dealer franchise termination and RMA laws do not dictate outcomes but instead provide a dynamic process (given the broad reach and scope of the matters to be considered). As such, while permitting significant flexibility and not standing as roadblocks, the laws provide a degree of stability that benefits consumers: because of this stability, dealers are willing to make significant investments to acquire, maintain, and update facilities, personnel, technology, tools, inventory, and training necessary to meet competition and consumer expectations. Satisfied customers mean repeat sales and brand value that inures to the benefit of dealers and manufacturers alike. The aggregate economic impact of this investment and economic activity provides dividends at the local, state and national levels.

Given the importance of these laws, their flexibility to adapt to changes at the micro and macro level, and their demonstrated success over generations, it would truly be unthinkable for any proposal to be put forward, especially at the national level, to remove or drastically change these state laws.

Warranty Reimbursement Regulation

California's legal framework for warranty reimbursement for labor and parts is consistent with its approach to franchise terminations and add-points. The law provides procedures for assuring the parties are operating on a reasonable basis and that due process is

observed and available where disputes or misunderstandings arise.

Specifically, Vehicle Code section 3065 requires manufacturers to properly fulfill every warranty agreement made to consumers and to adequately and fairly compensate dealers for labor and parts used to perform warranty diagnostics, repair, and service. The statute also provides for reasonable time limits respecting the warranty claims submission, payment, audit, and chargeback process. To foster cooperation between the manufacturer and dealer, and to minimize the need for formal legal proceedings, the statute provides that manufacturers shall adopt reasonable appeal procedures concerning warranty claim disputes. Audits and chargebacks of paid warranty claims are permitted, but may be challenged by the dealer if unwarranted.

While not flashy, these basic fairness protections provide the framework for a stable, secure, and first-class warranty repair and recall system. Regardless of the size of the dealership or dealership group, the dealer bears the burden of “fronting” the cost and capital necessary to actually provide service and repair under the manufacturer’s warranty each and every day. The manufacturer, holding the power of the purse, is in a position to improperly deny, delay, condition, or otherwise renege on paying the compensation rightfully due the dealer. Without the statutory framework, even isolated incidences of manufacturer overreach could call into question the reliability of the prospects for due compensation, and thus diminish the confidence dealers require to provide timely and high quality warranty service.

Laws prohibiting direct retail sales by manufacturers

California does not prohibit direct sales of vehicles by manufacturers. Consistent with its approach in the other areas discussed above, California law instead takes a balanced approach by addressing the potential for competition between dealers and manufacturers at the retail level. Generally, the law makes it unlawful for a manufacturer to “compete with a dealer in the same line-make operating under an agreement or franchise from a manufacturer or distributor in the relevant market area.” Vehicle Code section 11713.3(o)(1). “Relevant market area” is defined in Vehicle Code section 507 as “any area within a radius of 10 miles from the site of a potential new dealership.”

Exceptions permit factory ownership even within the relevant market of any dealer where necessary for factory-sponsored dealer development programs (many of which help support diversity among dealership owners) or for a limited time period for purposes of permitting the sale of an existing dealership to an independent operator. Even participants at the Workshop who were hostile to bans on direct manufacturer sales could not dispute that franchised dealers would be unfairly harmed if they faced direct competition from their own vehicle manufacturers.

New developments and future trends

Several Workshop participants suggested that the existing vehicle franchise laws impose limitations and constraints on competition, at least with respect to new developments, such as autonomous or other new-technology vehicles and ride sharing services. Not only are these views wholly unsupported, they also fly in the face of any fair and reasoned analysis of the laws and facts.

Panelists and commentators who view the vehicle franchise laws as anachronistic and outdated will often point to significant changes in consumer product retailing in recent years, and the ascendancy of online retailing. Vehicle franchise laws are seen as a roadblock to vehicle sales being treated the same as other consumer product sales. This view would instantly topple if any one of the many fallacies propping it up were removed.

Principal among these fallacies is that what applies in the realm of general consumer products and consumer product sales should also apply to vehicles and vehicle sales. The clear reality is, however, that vehicles (and virtually everything associated with them) differ greatly from other consumer products, a fact recognized in innumerable laws at the federal, state, and local level, including, as mere examples, laws pertaining to vehicle insurance, vehicle registration and license plates, mandatory equipment requirements, warranty and “lemon” laws, driver licensing, and penal statutes such as “grand theft, auto.” The vehicle franchise laws are an essential part of the enormous web of laws governing the automobile. Significant changes to any part of this web will have serious repercussions in other parts.

Moreover, those commenting against vehicle franchise laws fail to recognize the dramatic changes that have seamlessly occurred (with the franchise laws in place) in the distribution and service of vehicles, especially as to the prominence of online and new technologies. There is intense competition at both the interbrand and intrabrand level to provide consumers with exactly the experiences they seek, which more and more often involves mobile and online technologies. The franchise laws did nothing to stop this innovation, and nothing suggests that other innovative steps manufacturers (and/or dealers) actually wish to take have been stopped.

In addition, the view that vehicle franchise laws need to be scrapped in order to make room for innovation is not only wrong for the reasons stated above but is also completely blind to the realities of state-law based consumer and business regulation: if the common sense flexibility already built into state franchise laws is insufficient to accommodate a new development, state legislators and regulators are extremely nimble and can accommodate needed statutory or regulatory changes in a fraction of the time generally needed at the federal level.

Finally, notwithstanding the fierce interbrand competition in the vehicle industry, and the enormous change in all industries (and lives) occurring over the past 25 years, there is not now nor has there been any evidence of a desire or plan on the part of any material segment of vehicle manufacturers to scrap or dispose of the existing network of thousands upon thousands of vehicle distribution and service center locations across the United States. In essence, the commentators speaking against vehicle franchise laws may be suggesting a (poor) solution (scrapping the laws), but they are still in search of a problem.

Conclusion

California law does not restrict markets or market action regarding the distribution of motor vehicles. Instead, it provides a framework within which its licensed motor vehicle dealers and licensed motor vehicle manufacturers may organize their relationships with a degree of stability and confidence and with the assurance that the interests of all constituents,

including the consuming public, will be taken into consideration whenever a desired course of action is subject to challenge. As California shows by example, the states have been and remain best suited for regulating in this area. Moreover, the franchise laws are an integral part of the overall web of state law respecting the automobile. The FTC is urged to refrain from moving toward a position that would undermine these important, legitimate, and real-world tested state police power regulations.

Respectfully submitted,


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California New Car Dealers Association

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