SUBJECT: Revising the Texas Motor Vehicle Commission Code

COMMITTEE: Transportation — committee substitute recommended

VOTE: 7 ayes — Alexander, Edwards, Hamric, Hawley, Hill, Noriega, Uher

0 nays

2 absent — Siebert, Y. Davis

WITNESSES: For — Gene Fondren, Texas Automobile Dealers Association

Against — Francis Dunne, General Motors Corp.; Jill MacDonald, Alliance of Automobile Manufacturers and Association of International Automobile Manufacturers; Ross Roberts, Ford Motor Company; Kenneth Roche, Jr. and Charlie Ryan, Gulf States Toyota Inc.; Don Thornton

BACKGROUND: The Texas Motor Vehicle Commission Code, art. 4413(36) Civil Statutes, governs the relationships between automobile manufacturers, dealers, and consumers through the Texas Motor Vehicle Board. The board, formerly the Texas Motor Vehicle Commission, consists of nine members appointed by the governor. While part of the Texas Department of Transportation administratively, the board is independent from the Transportation Commission.

DIGEST: CSHB 3092 would make numerous changes to the Texas Motor Vehicle Commission Code including:

- extending the provision restricting manufacturer ownership of dealerships, except in certain limited circumstances, to up to one year and expanding notice requirements for manufacturer ownership interests in dealerships when manufacturer's licenses are applied for or dealer's licences are transferred, assigned or sold;
- regulating manufacturer or distributor incentive programs;
- limiting manufacturer's audits of warranty reimbursement payments to one year from the submission of the claim unless the manufacturer has reasonable grounds to believe the claim is fraudulent;
- modifying the definition of dealers for purposes of appointment to the

board;

- limiting owners under the Lemon Law to purchasers, lessors or lessees, or their transferees or assignees, who are residents of Texas;
- allowing the board to suspend, in the interest of justice, the enforcement of an order until an appeal is finally determined;
- restricting manufacturers from forcing dealers to relocate; and
- making other conforming changes to the statute, including changing references to “commission” to “board.”

CSHB 3092 would take immediate effect if finally passed by a two-thirds record vote of the membership of each house.

Manufacturer ownership of dealerships. Manufacturers, distributors, or their representatives or agents, would not be allowed to directly or indirectly own an interest in, operate or control, or act as a dealership. They could own an interest for up to one year if they had acquired the dealership in order to sell it. They could hold an interest temporarily if the primary purpose of ownership was to broaden opportunities to minorities who would be unable to purchase a dealership on their own when there was a bona fide relationship with a franchised dealer who as made a significant investment, had an ownership interest, and operated the dealership with the expectation of gaining full ownership.

Applicants for manufacturers licenses would be required to list separately each dealer in which the applicant, or an entity owned or controlled by the applicant, had a direct or indirect ownership interest. When the controlling interest in a dealership was transferred, assigned, or sold to another person, the notice required would have to include a statement by the prospective transferee identifying any manufacturer or distributor that had an ownership interest in the transferee.

Incentive programs. Incentive programs would be defined as a temporary program rewarding the dealer, an employee, or customer for the attainment of a sales goal or other objective within a stated time. CSHB 3092 would require manufacturers or distributors to file a copy of the incentive program’s rules with the board within a reasonable time after the program was initiated. The rules would not be considered a public record except to the extent it was introduced in a public hearing. Manufacturers or distributors would be prohibited from recouping money from a dealer unless they could show the

information contained a material mistake that was not discovered before the award was made and caused the manufacturer to make the award, and the manufacturer took reasonable care to discover errors. Audits of incentive program awards would have to be completed within one year of the end of the program unless the manufacturer or distributor had reasonable grounds to believe the dealer committed fraud.

Warranty reimbursements. CSHB 3092 would reduce the time allowed for a manufacturer to audit claims for warranty reimbursement from two years to one year after the claim was submitted unless the dealer had reasonable grounds to believe the claim was fraudulent.

Board membership. CSHB 3092 would provide that of the two dealer positions, one would have to be a licensed dealer or have at least a 20 percent ownership interest in a dealer, and the other would have to be a franchised dealer or have at least a 20 percent interest in a franchised dealership. A person would be ineligible to serve on the board as a dealer if the qualifying interest was in a dealership in which a manufacturer or distributor had an ownership interest.

SUPPORTERS SAY:

The Texas Motor Vehicle Commission Code is constantly subject to revision to deal with the changing nature of the automotive manufacturing, distributing, and sales business. Originally adopted in 1971, the code has been revised by every legislature since its adoption. This session's revision deals with new moves by manufacturers to gain ownership interests in dealerships, clarifying rules for warranty reimbursements and incentive programs and limiting audits of those programs to one year, and making other clarifying changes to board membership requirements and who can use the Texas lemon law. The Motor Vehicle Commission Code provides regulation of the dealer manufacturer relationship and recognizes the disparity that exists between dealers and manufacturers.

Manufacturer ownership of dealerships. Recent moves by certain manufacturers to gain impermissible ownership interests in dealerships in Texas require additional clarification of the law prohibiting such interests. Current law limits ownership by dealers except for the purpose of selling the dealership or when done in a bona fide partnership with a future minority dealer (dealer development program). Such arrangements are required to be

temporary but there is no standard for what is considered temporary.

Requiring dealership held by manufacturers for sale to be held for less than one year would prevent manufacturers from holding such dealership indefinitely. One year would be more than enough time to sell a dealership in this state. Dealer development programs would not be limited to one year because such programs allow for a manufacturer's interest to be held until its investment is paid by the dealer. That repayment often takes as much as three to ten years.

Manufacturer's ownership interests also would be further exposed by additional reporting requirements on application of licenses or transfer of dealerships.

Restricting manufacturer ownership of dealership is essential to the maintenance of competition among dealerships. If a manufacturer were allowed to hold an ownership interest in a dealership, it might be compelled out of self-interest to allow that dealership to succeed ahead of others. At the very least, manufacturers receive financial statements from dealers detailing their sales and profits on every good and service they provide. Manufacturer-owned dealerships with access to this information without comparable data going back to the other dealers would unfairly give the manufacturer-owned dealerships a definite competitive edge.

Manufacturers allege that owning dealerships would provide better service to customers and could reduce prices by cutting distribution costs. However, surveys of automobile purchasers find over 80 percent are satisfied with their dealers. Additionally, a study of automobile prices over the last 10 years shows that while the cost of vehicles to dealers has risen over $9,000, dealers' gross profit has risen less than $400 per vehicle in that time, a decrease in the gross profit percentage.

Incentive programs. The incentive programs under CSHB 3092 would be based on the model provided for warranty reimbursements. The bill would require that rules be filed with the board so that dealers, manufacturers and ultimately the board hearing any disputes could refer to those rules for a clear statement of the duties of each party in these programs. Requiring the rules for such programs to be filed after the program had started would not infringe on the trade secrets or business practices of the manufacturer because these

rules would likely be available to the public at that time. The only reason to avoid filing these rules would be to allow the manufacturer constantly to change the rules, thus making it difficult for many dealerships to keep track of those rules and potentially get charged back for incentives not offered correctly.

Audits of these programs would be limited to one year just like audits of warranty programs.

Warranty reimbursements. CSHB 3092 would reduce the time for audits of warranty reimbursements from two years to one year. One year is a reasonable amount of time to conduct an audit. Allowing audits to be conducted after that amount of time makes it difficult for dealers to properly close their books for the year because they could still be required to send money back as late as two years after the claim was made.

Board membership. CSHB 3092 would clarify the provisions relating to board membership by dealer representatives. Current law is unclear on who qualifies as a dealer because it only refers to an entity, not a person. Limiting the definition to a person would eliminate the ability of a corporate entity to hold this position. Additionally, the dealer requirement would reiterate the commitment against having dealerships partially owned by a manufacturer from holding a dealer's position on the board.

Lemon Law. The current lemon law, allowing purchasers to recover for defects or conditions that present a serious safety hazard or affects the market value of a car, is not limited to purchasers, lessors, or lessees who reside in Texas. This means any vehicle owner in any state can use the Texas lemon law to recover damages without having any connection to the state. Limiting the law to Texas residents would ensure that Texas taxpayers would not be paying for adjudication of lemon law claims by out of state residents.

Suspension of board orders. A final order of the board can be enforced even when under appeal unless it is enjoinable by a court. CSHB 3092 would allow the board to suspend the enforcement of the rule on its own in the interest of justice. Otherwise, the board would have no authority to suspend the enforcement of its own decision when the decision was on appeal.

Restricting forced relocation of dealerships. Manufacturers are currently prohibited from terminating or refusing to continue a franchise with a dealer unless it meets numerous conditions specifically set out in statute including explicit notice requirements. However, some manufacturers, while not terminating dealerships have required dealers to relocate or else lose their dealership. Such relocations can have the effect of terminating the dealership. CSHB 3092 would not prohibit such forced relocations, but would only place them on the same level as forced terminations of franchises.

OPPONENTS SAY:

The Texas Motor Vehicle Commission Code is the most "dealer friendly" statute in the country. The provisions of this bill would extend that inequity by further limiting the rights of manufacturers and distributors in their relationships with dealers.

Manufacturer ownership of dealerships. The current state of the automobile market is one of consolidation both horizontally and vertically. Numerous manufacturers have merged, and many dealers are now owned by several major corporations that own numerous diverse dealerships. However, in Texas, there is a very strict line of prohibition against vertical integration of automobile sales, regardless of the benefits that such integration might provide to consumers through additional knowledge of the products, better service, and potentially better prices with limits on distribution expenses, which can constitute up to 25 percent of the cost of a vehicle.

Manufacturers who have an ownership interest in a dealership have no incentive to favor one dealership over other dealerships because doing so would limit the eventual distribution of their products. Manufacturers can actually offer help to independent dealers at risk of being swallowed up by mega-dealerships by partnering with dealers, at their request, and providing financial help.

Limiting the time a manufacturer would have to sell a dealership to one year would be unreasonably short and may affect the ability of the manufacturer to receive the best price possible for the dealership.

Auditing requirements. Reducing the audit time for these programs to one year would require manufacturers to hire additional auditing staff to review these transactions within the time allowed. This could be a strain on some

smaller manufacturers who would be required to create a special auditing schedule for Texas dealers.

Incentive programs. Even without prior filing of incentive program rules, which was removed from the original bill in the committee substitute, the requirement of filing these rules with a state agency could directly impact the competitive advantage of particular manufacturers and distributors whose incentive programs may be reviewed and copied by competitors if they are made public. The board already has authority to ask for rules if a complaint is filed dealing with an incentive program. This authority is adequate to deal with regulation of incentive programs.

This filing requirement also would be an overwhelming administrative burden to keep such rules and procedures on file because each incentive, which only may be good for a week or a month, would have to be sent to the board, recorded, filed, and stored.

Board membership. Prohibiting board membership to dealers who had a dealership in which a manufacturer had an ownership interest would exclude those in the dealer development programs that allow minority dealers to buy a manufacturer out over time.

Restricting forced relocation of dealerships. A new trend in dealerships is the creation of multi-manufacturer dealerships that sell products from multiple manufacturers. Such dealerships can reduce customer satisfaction because multi-manufacturer dealerships have less product knowledge and brand focus. Currently, manufacturers can promote customer service by requiring dealerships to focus only on one brand, separating them from other manufacturers. Prohibiting manufacturers from doing so would limit their right to promote their products in the manner that best facilitates customer satisfaction.

Lemon Law. Limiting use of the lemon law to current Texas residents may affect the rights of former residents to bring actions under the law.

NOTES:

The committee substitute removed a requirement in the original bill that the rules and procedures of an incentive program be filed with the board prior to its implementation and provided that incentive program rules filed with the board would not be public records.

The companion bill, SB 1250 by Cain, is currently pending in the Senate State Affairs Subcommittee on Infrastructure.