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Dealer Performance Review Programs

By Michael McKean
OCD Consulting, LLC / O'Connor & Drew, P.C.

From an Aesop Fable

A scorpion and a frog meet on the bank of a stream and the scorpion asks the frog to carry him across on its back. The frog asks, "How do I know you won't sting me?" The scorpion says, "Because if I do, I will die too."

The frog is satisfied, and they set out, but in midstream, the scorpion stings the frog. The frog feels the onset of paralysis and starts to sink, knowing they both will drown, but has just enough time to gasp "Why?"

Replies the scorpion: "It's my nature ..."

When I see some of the programs manufacturers devise to "help dealers better understand and manage their performance", I ask myself why and the fable of the scorpion and the frog always comes to mind. Recently, two new initiatives announced by Nissan and Mercedes Benz fit into this category and your dealer clients should be paying attention to them.

Nissan has announced that it is transitioning its sales effectiveness metric from a Regional Sales Effectiveness score to a State Sales Effectiveness Represented score. Nissan's stated reason for this change is that they want "to use a more localized standard for evaluating dealer sales effectiveness." Like the frog, I am suspicious and would like to ask why.

All measures of sales effectiveness, no matter

what cloth they are cut from, are by definition, irrational. So, why make the effort to change from a regional score to a state represented score? I believe the answer is in a letter sent by Nissan to each of its dealers describing the new metric. In it Nissan provided the old RSE score and the new SSER score with the suggestion that dealers whose performance deteriorates under the new system will need to come up with a plan for corrective action. My guess is because the new system excludes open points or unrepresented areas, many dealers will see their scores go down and will soon be feeling the sting of the scorpion, in this case Nissan.

How the same dealer can be "good" under one system but "bad" under another makes no more sense than the scorpion stinging the frog but it is

the nature of what manufacturers like to do. If you have a Nissan dealer in this predicament he needs to respond forcefully and in writing.

The Mercedes Benz program, the Dealer Performance Review is not new but it is being re-launched with new enthusiasm. The program is designed to help identify “underperforming” dealers, now by using nationally-standardized metrics. These include; operating profit, customer satisfaction scores, registration and sales effectiveness scores, customer paid parts sales, and service retention. This program is important to dealers because those who are deemed to be “poor performers” will see a significant decrease in incentive money paid to them by Mercedes Benz. Like many factory performance management schemes, this one has the underlying assumption that no dealer can be below average and gives no consideration to differences in the geography or the demographics of any particular market.

Under the DPR program, dealers who score in the bottom 10% of all dealers nationally are put on a watch list and are provided “assistance” from factory personnel. At the Ford Motor Company we used to call this the “Stair-step” program, which of course was nothing more than a path to termination. Mercedes Benz dealers on the DPR watch list need to be paying attention because this program is not going away.

It is not that I think manufacturers don't have the right to expect good performance from their dealer body because they do and it is important that all dealers strive to perform at the very highest lever. But all too often, the systems that factories devise to measure and manage dealer performance are conflictive, subjective, irrational, and unfair. Dealers who find themselves being harassed under these kind of programs, should fight back and they should be looking to you for help. ■

Michael McKean is a life-long retail automotive professional. He is the founder and president of OCD Consulting, an automotive management development and brokerage firm with clients nationwide. OCD Consulting is a joint venture of O'Connor & Drew, P.C., New England's largest independent automotive CPA firm.

Reminder!!

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Travel Plans:

Please arrange your travel to join NADC at the opening cocktail reception on Sunday, April 27th from 6:00 – 7:30 pm. The conference will conclude on Tuesday, April 29th at 3:30 pm. If you plan on spending some extra time in Laguna Beach please note that the group rate will be made available three days pre (April 24, 2014) and post (May 2, 2014) based upon hotel availability.

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Dealer Franchise and Licensing Laws – More Important Than Ever

By Mike Charapp
Charapp & Weiss, LLP

Feature Article

State dealer franchising and licensing laws face increasing challenges. Online lead merchants who want to become online vehicle sellers think the laws are unreasonably restrictive. New manufacturers who claim that their self-propelled four wheel vehicles are somehow totally different from the self-propelled four wheel vehicles dealers sell claim that the laws are unfair. As a result, there are increasing questions about the regulation of retailing motor vehicles. “Why are the franchising and licensing laws necessary?” “Aren’t the laws outmoded?” “Aren’t the laws stifling innovation?”

Those in the business know that the laws are more important than ever. We should catalog the benefits of the laws in case we must defend them in court, before a state legislature, or even at a cocktail party. Here are some thought starters.

Why do the franchise laws and the licensing laws even exist?

State legislatures have enacted the laws to protect consumers and to ensure healthy competition. Vehicles are the largest consumer product purchase for most Americans. When consumers are upset with their purchase experiences, they look for help – and expect the government to have answers. Over time, state legislatures have determined that it is best to have in place laws regulating vehicle sales.

Franchise laws protect consumers? Absolutely! Lawmakers recognize that it is best to have dealer owners with local knowledge, ties, and interests. When the going gets tough, a multinational giant can simply close up a local outlet and go away. That’s not an option for a local business person who owns a car dealership. When the going gets tough, a local business person just can’t close the doors and move on. The dealership probably represents the bulk of the dealer’s assets, and closing the doors is likely to be ruinous. The franchise laws present the best opportunity to ensure local ownership and operation of dealerships.

Local dealers will be there for customers through good times and bad. When there are problems with the customer’s car, the dealer will be there to solve them. The dealer will provide warranty service. If recall repairs are necessary, the dealer will perform them. When the manufacturer refuses to respond on a warranty or a safety issue, the dealer is there to advocate for the customer and sometimes to pick up the tab to maintain a customer’s goodwill. If a manufacturer fails and must cease production, the dealer will still there to provide any support it can for a customer. Local business people have incentives to serve their neighbors that multinational manufacturers may not.

But today, there are public dealership groups. Doesn’t this detract from the claim about the benefits of local dealers? Not at all. The majority of dealers around the country are privately owned, not publicly owned. But even for those publicly owned, the franchisors require that they have in place operators who are attuned to local conditions and understand their customer base. Some franchisors even require that those local operators have equity interests in the businesses that they run.

With the impact of the internet, why are brick and mortar dealers necessary? Can’t manufacturers sell directly over the internet? Selling a motor vehicle is a complex activity. No other sale of a consumer product involves state and federal laws as heavily as vehicle

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Shouldn't We Be Talking?



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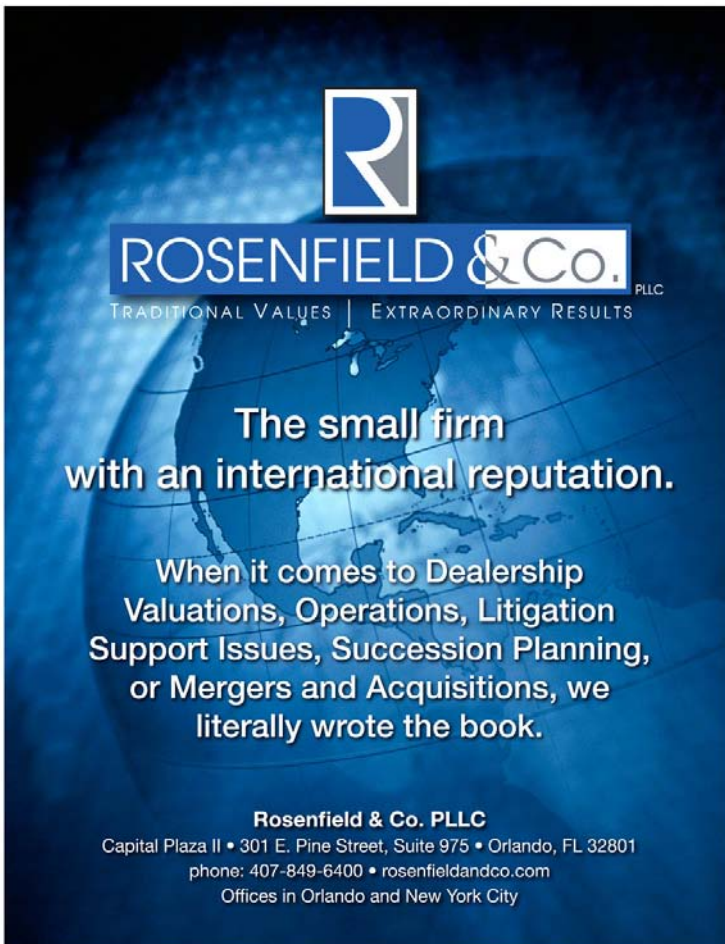
sales; specific and detailed legal requirements must be followed. More importantly, a vehicle sale involves a number of related activities. A brick and mortar dealer is best suited to serve and satisfy customers.

- *Display, Test Drives, and Deliveries.* A minority of customers may be happy buying a car sight unseen, but most want to see and drive what they may buy. When they buy, customers want to learn the complex features of the new vehicle from a trained and experienced salesperson at delivery.
- *Financing Services.* Because of the size of the investment, most customers finance their vehicle purchases. Dealers are there to present the financing alternatives and to help customers obtain suitable financing.
- *Related Products.* Dealers understand the products and services that can help customers protect and enjoy their investments. A dealer representative can work to understand a customer's needs and to sell the products and services individually tailored to the buyer.
- *Government Services.* In most states, dealers lighten the burdens on local governments. Dealers arrange for registration of vehicles, collect taxes, and do other services related to vehicle ownership. This reduces the burden on state transportation agencies and tax collectors and saves customers time and effort in registering their vehicles.
- *Trade-ins.* Most consumers must sell their existing vehicles to buy new vehicles. Dealers provide a ready market for a customer's trade.
- *Warranty Repairs and Recall Services.* If the customer's vehicle breaks in some manner, the dealer is there to provide warranty services. If the manufacturer issues a recall, dealers are there to provide the necessary fix.
- *Maintenance and Repair Services.* Today's vehicles are more complex than ever. Dealers have technicians trained to provide the maintenance and repairs customers need to protect their investments.
- *Local Sales and Service.* Dealers are available where customers live so that they don't have to have their cars delivered by drop shipment and they don't have to flat-bed their cars for warranty service, repairs and maintenance.

Can't manufacturers do these things themselves? Yes, but the investments by the manufacturers in creating the retail distribution and repair capabilities would be in the billions. That is why the franchise system developed. The domestic manufacturers and the distributors of foreign nameplate vehicles understood that they could not themselves do retail distribution, ensure customer care, deliver warranty services, and provide the other benefits dealers offer – the investments would have been too great, the personnel counts too staggering, and the management responsibilities too daunting. Local entrepreneurs invested their own funds to develop dealerships to build a sophisticated vehicle distribution and servicing model. And dealers independent of factories and distributors enhance the sales process by providing interbrand and intrabrand competition.

Interbrand competition? Most dealers are single point stores or have limited numbers of brands in dual stores. They must convince buyers that the vehicles they sell and the sale terms offered are superior to those for competitive nameplate vehicles sold by neighboring dealers. Dealers compete best by knowing their markets, understanding the interests of their customers, and challenging their local competitors.

Intrabrand competition? Dealers provide transparency for vehicle buyers. There are a number of internet sites (and before the internet, pricing books) where a customer can learn exactly what a dealer pays



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for the new vehicles it is selling. As a result, dealers compete to provide the best prices and services. Try to find out what a vehicle costs a manufacturer. There would be no transparency or intrabrand competition in factory direct sales.

Aren't the franchise laws for protection of dealers? Yes, that is an element. But what is wrong with that? There is an economically defensible reason for today's franchise system. Manufacturers and distributors depended on dealers to invest the money and effort to build an efficient retail and service model. Dealerships developed to provide the retail and service capabilities that manufacturers could not or would not fund themselves. The system saved manufacturers billions and allows them to concentrate on what they do best – building vehicles – while dealers concentrate on what they do best – retailing vehicles and serving customers. Why should dealers who risk their family fortunes run the risk of having their franchises terminated and their businesses ruined at the whim of a franchisor that wants to profit from the dealers' sweat and investment? Why should dealers be subjected to competition of direct manufacturer sales when factories think it suits them? Why should dealers be starved of popular models the manufacturer wants to distribute directly while being left with those the manufacturer can't sell as readily?

Don't the franchise laws cost consumers money? One of the greatest misconceptions held by critics of the motor vehicle franchise system is that dealers add costs into the distribution chain. Nothing could be further from the truth. If a factory owns a dealership, it still must invest millions on which its shareholders will expect a return, hire and pay personnel, pay for rent, utilities, taxes, and maintenance for facilities, and pay for everything else required to operate the business. Retail distribution, warranty services, customer relations, and vehicle maintenance will still have to be provided. If anything, dealers save money for the manufacturers. Operations by remote multinational giants would likely raise the costs of doing business over those of local dealers who understand how to control expenses. Moreover, dealers provide an immediate outlet for vehicles and parts by paying for them before they even arrive at the dealership. Manufacturers don't have to carry the costs of inventories on their books. Far from injecting additional costs, dealers represent a cost savings to the overall system.

Why are licensing laws still important? Licensing laws developed over the years for reasons similar to those leading to enactment of franchise statutes. If sales and servicing of vehicles are not handled properly, consumers stand to lose a lot of money. If they lose money, they want to know what the government will do for them. The licensing laws are a reaction to that. At their simplest, licensing laws provide regulatory agencies with enforcement powers. A dealer who is not licensed cannot sell vehicles. Dealers work hard to avoid regulatory action that could threaten their licenses. When a problem arises, the regulator has the ability to take action against the dealer's license. And the licensing process itself provides revenue to provide the enforcement process.

Why are there standards for dealers to be licensed? Simple. After many years, legislators have determined that certain business characteristics best lead to consumer protection. Almost all states require that a dealer that is selling to consumers meet certain standards denoting stability. State requirements may vary. However, they exist to maximize the chance that a dealer will be around and will adequately serve customers. Whether a state law requires a brick and mortar presence, licensed salespeople, an area for display and parking, signs, furniture and equipment, or a number of other requirements varying from state to state, the purpose is protection of the public interest.

But doesn't the internet make licensing statutes outmoded? Quite the opposite. The internet is the wild west. There is little regulation. Protections can be illusory. State and federal laws work only when a bad actor can be found. For every solid reputable company on the internet, there are others that are out to scam the public. There is no assurance that those who hold themselves out as dealers over the internet have the stability that state laws were implemented to ensure. The web page a consumer is browsing may be for a billion dollar company, or it may be for scammer operating out of a parent's basement. The internet is a breeding ground for the very problems that licensing laws were developed to prevent – lost deposits, entire payments for vehicles stolen,

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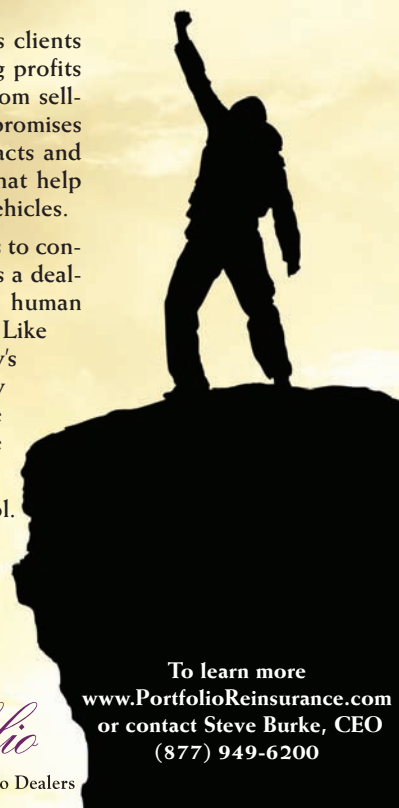
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sales of unsafe vehicles without remedy, and the like. The potential for vehicle retailing on the internet makes licensing more important than ever.

Don't dealers stifle innovation? Nonsense. As an example, just consider the internet. When the internet began to grow, it was rumored that it would be the death of dealers. Rather than be overcome by the internet, dealers adopted it. Today, some of the most advanced marketers on the internet are car dealers. Car dealers will be just as adaptive with any sort of product that is developed. As long as vehicles are self-propelled and they roll, dealers will want to sell and service them. Whether they are gas engined, diesel powered, flex fuel, hybrid, electric, or hydrogen-celled, and whether they have two wheels, three wheels, four wheels or more, a dealer will be there to market them and work on them. Dealers embrace innovation. It is how they make their dealerships more efficient and effective. It is how they better serve their customers. ■

Michael G. Charapp is a lawyer in the Washington, D.C. metro area who represents car dealers and dealer associations. He is editor of the Defender. He encourages submissions for publication, and he can be reached at: mike.charapp@cwattorneys.com.

NADA Fair Credit Compliance Policy & Program



by Paul Metrey, *Chief Regulatory Counsel, Financial Services, Privacy, and Tax, NADA*

On January 24, NADA, AIADA (American International Automobile Dealers Association), and NAMAD (National Association of Minority Automobile Dealers) released to their members the NADA Fair Credit Compliance Policy & Program. As stated in the cover memo that accompanies the publication, it provides auto dealers with an optional fair credit compliance program template that (i) establishes a fair credit policy which states the dealership's unambiguous commitment to fair credit compliance, and (ii) creates a general framework for the dealership to promote compliance with fair credit laws. It is modeled on the approach to fair credit compliance that is contained in two 2007 consent orders that the Department of Justice entered into with Philadelphia area dealerships. The publication and the cover memo are available at www.nada.org/faircredit and will be explained in detail by NADA Chief Regulatory Counsel Paul Metrey during the NADA Update at the upcoming 2014 NADC Conference in Palm Beach, FL.



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Executive Director's Message



Erin H. Murphy
NADC Executive Director

2014 has been an eventful year so far for NADC. We enjoyed another successful show at the 2014 NADA Convention & Expo in New Orleans, LA January 25-27, 2014. The NADC booth's close proximity to the NADA Pavilion allowed us to visit with many of our current members and to meet many new and prospective members. We enjoyed visiting with all of you!

We also released the 2014 NADC Attorney Directory at the NADA Convention & Expo and recently mailed a copy to all of our members. We've organized the directory by state to assist you when you are looking for a referral. NADC Associate Members are listed alphabetically at the end of the directory. We hope you will find the directory a useful tool and an easy reference guide to the NADC community. Should you need additional copies, or an electronic version, of the Attorney Directory please contact Charlotte Valentine at cvalentine@dealercounsel.com.

The new year is a busy time for membership renewals. I would like to thank all of our members for their continued support. I would also like to remind our members of the NADC membership pledge. The following is the pledge that all attorney members review and sign on their membership application.

NADC Membership Pledge

- I certify that I represent the interests of vehicle dealers engaged in the retail sales and service of motor vehicles ("dealers").
- I do not represent, and agree that I will not undertake to represent in the future, the interests of consumers in lemon law claims or lawsuits, in other claims or lawsuits against dealers arising from consumer transactions, nor will I represent the interests of manufacturers or distributors in disputes with dealers.
- It is possible that from time to time a law firm with which I am or may be associated may represent a manufacturer in the defense of a consumer claim. I acknowledge that, in the defense of such claims between the manufacturer and a consumer, other members of the law firm with which I am or may be associated may be called upon to assert claims against dealers in defense of the manufacturer client on such claims. I agree that I shall disclose to the NADC whether any other members of the law firm(s) that I am associated with are engaged in the defense of claims on behalf of any manufacturers, and agree that, to the extent applicable, I shall inform each such member engaged in defense of such claims of my NADC membership get their acknowledgment that they shall not, under any circumstances whatsoever, attend or participate in any NADC meetings or workshops, access any portion of the NADC website and/or the NADC list-serve, review any publications of NADC including, but not limited to, the Defender, or any printed or computer generated materials utilized in connection with any and all membership presentations or seminars held at any membership meetings or workshop meetings of the NADC. I acknowledge and agree that it will be considered a breach of our commitment to NADC members if we communicate NADC information to any of our manufacturer clients or otherwise use such information against dealers.
- I understand that my membership is subject to termination in the event I engage in such consumer or manufacturer/ distributor representation in the future.

If at any time you feel that you can no longer adhere to the membership pledge please contact Executive Director Erin Murphy immediately at emurphy@dealercounsel.com or 202-293-1454. Violations of the membership pledge will result in membership termination.

We hope to see you all at the Four Seasons Resort in Palm Beach, FL for the **2014 10th Annual NADC Annual Member Conference, April 27-29, 2014**. For more information, please call 202-293-1454 or email info@dealercounsel.com. ■

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