MICHIGAN AUTOMOBILE DEALERS ASSOCIATION

Driving Your Success

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TWENTY-TWO for '22

At the end of our article last year on Twenty-One issues for '21, we wished for motor vehicle dealers a 2021 as free from unpleasant surprises as possible. What we got was a year that was Dickensian -- one best described by the opening phrase from Charles Dickens' A Tale of Two Cities, "It was the best of times, it was the worst of times…."

Some of the worst aspects of 2021 for dealers are easy, but painful, to list:

- Severe vehicle inventory shortages due to COVID work interruptions and chip unavailability;
- Dealing with the uncertainties of a new federal administration dedicated to ending all programs of the previous administration whether they worked or not;
- Continuing to keep the doors open to serve customers with concerns about COVID; and
- Keeping reasonable staffing levels with worker shortages made worse by COVID and employee concerns such as quarantining for suspected COVID infections and arranging schedules for children required to stay home and pretend to learn virtually.

The best aspect for dealers is also easy to list: while new vehicle inventory shortages and shortages of used vehicles were significant problems, they drove dramatically increased pricing unlike anything dealers have seen or are likely to see again in their lifetimes, with resulting record profitability.

What can dealers expect in 2022? More of the same for the first few months, with changes as the year progresses. Vehicle supply shortages are likely to continue for several months, and the latest Omicron hysteria suggests that COVID fears may last for some time as different variants develop. As we go into later 2022, one can only hope for increased new vehicle availability, easing of the used vehicle shortages, and some taming of COVID. But the challenges will remain, and one hopes some measure of the profitability dealers enjoyed in 2021. Here are twenty-two issues for '22. They are not listed in order of importance; they are all important.

The Future

1. Challenges of selling and servicing electric vehicles. Electric vehicles are here to stay. There are many consumers, and even several industry observers, who question whether electric vehicles will replace ICE vehicles. Some of the more aggressive electric vehicle support programs of the federal government are in the Build Back Better bill that has not passed, and if it ever passes it is likely to be drastically trimmed. None of the skepticism or failing to fund federal programs as the Biden administration wants matters however. Manufacturers are "woke" to the electric vehicle future, and they already have dealers changing their marketing, advertising, and training priorities on sales of electric vehicles. The manufacturers have decreed that electric vehicles are the future, and that is a tune to which franchised dealers will dance in 2022.

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2. Marketing and selling online. Keeping the doors open for full scheduled hours despite the pandemic was often a struggle in 2021. If the state government wasn't flirting with shut downs for "non-essential" sales operations, personnel issues were challenging, and it was difficult to get many consumers to leave their homes. The answer? Online marketing and selling. Dealers were already ahead of the curve before the pandemic hit, but COVID kicked the necessity to be cyber into overdrive. Today, dealers have learned to work with OEM and supplier programs to better acquaint customers with what they offer. And they have developed the means to communicate with customers and sell them vehicles online. That is a trend that will not reduce post-COVID.

3. OTA upgrades and repairs. "We want to be like Elon," is a phrase driving OEM behavior. They ignore that Tesla sales were driven by third or fourth vehicle buyers willing to pay exorbitant prices for vehicles with quality issues so their neighbors could judge them virtuous. The market cap for the company and the subscription fees are seductive. Some OEMs are predicting huge, if unrealistic, futures of subscription fees with over the air installation of upgrades and over the air repairs, particularly for recalls. So what will be the dealers' role in an OTA world? If it is up to the OEMs, there will be no role for them. But not all repairs and implementation can be done OTA, and even for those that can be, dealers are likely to be consulted by customers for upgrades they do not understand or that do not fully take. Dealers must be prepared to fight for compensation for their roles in OTA implementation.

FRANCHISES

4. Challenges to the franchise system. You have heard it for years. "Dealers are dinosaurs!" If so, why are the so-called disruptors opening dealerships? They love dealerships they own. It is the inconveniences of horizontal price competition and independent business people who understand what customers in their market want that they do not want to deal with. That, briefly, is why the franchise system will endure. Dealerships are important. OEMs conserving limited capital and management talent to do what they do best – design, manufacture, and market vehicles – is the reason the franchise system was developed. The convenience and deal-making of the local dealership built on the dealer's investments of capital and talent, despite stereotypes, are why consumers will continue to look to dealers.

5. Question every document you are asked to sign. It happens to dealers every day. The rep comes in with a franchise document to sign. Most dealers realize that the factory is their partner if they do what the factory demands. Ask questions, and the partnership ends. Asking questions is what you should be doing when faced with a new document. How does it affect you? What benefits does it provide? Do the benefits outweigh the detriments? Are the requirements realistic? Can you meet the requirements? Do not get stuck with bad deals just because your "partner" asks.

6. Be prepared to challenge misbehavior. Your franchisor may know well the law in your state, but it simply does not care. Sometimes it just wants to see what it can get away with. An audit beyond statutory deadlines? Improper chargebacks? Unfair allocations? Some manufacturers will push until you push back. First, you may challenge using the franchisor's internal process. Then you can follow your state procedures for a hearing on the validity of the franchisor's behavior. The Key: make sure you have the documents you need. Be careful to keep your dealer agreement, all exhibits and schedules, any amendments, performance reports, programs, and correspondence from your OEM. Those are the first things your lawyer will request if you challenge OEM misbehavior.

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7. Performance Threats. Franchisors took a brief hiatus from threatening dealers over what they deem as insufficient sales during the height of the pandemic, but the threats by manufacturers are back. Each dealer had to face its own challenges from COVID. All dealers have had to face the problem of new vehicle inventory shortages for every OEM. Dealers without new vehicle inventory at a level they will need to make manufacturer set targets will not meet them. Measuring sales performance in this atmosphere is wrong. Threatening dealers deemed sales ineffective is ludicrous. When you receive communications critical of your sales performance, point out the absurdity of the OEM measuring sales effectiveness since the onset of the pandemic with accompanying inventory shortages, and reject the factory threats. Factory sales performance measures were affected by COVID-19 and inventory shortages, and they will continue to be unreliable for some time.

8. Post-Pandemic Operations and Franchisor Facility Requirements**.** Reduced inventories since the pandemic have led to questions about continued manufacturer demands for larger facilities. One hopes those shortages will be transitory. One legacy of pandemic operations likely to endure, however, is increased dealer digital sales activities. Dealers have had to increase their digital operations to serve customers reluctant to visit the dealership. Those increased digital services are likely to continue, and these are what undercut the factory arguments for ever increasing dealership facilities demands. These demands for larger and more luxurious physical facilities are more manufacturer ego driven than business driven given the changes in how dealers sell and will sell vehicles. It is more important than ever when facing facility demands that you understand your state law protections and agree only if facility upgrades make economic sense in a post-pandemic world.

9. Be Sure Recall Repairs Are Performed. Manufacturers are under pressure from the federal government to make sure vehicle defects are remedied. Dealers are a critical part of the process, because dealers do the work. Unfortunately, there have been several cases where recall repairs were claimed but were not performed because the problem may have seemed unimportant to the technicians. How do you know that your technicians are doing the work they report to you is being done for a recall? Train technicians regarding each type of recall repair and how the work is to be done.

   - Regularly self-audit recall repairs done in your service department.
   - Review the time spent by your technicians. The time allotted by manufacturers is seldom generous. If your technicians are significantly beating factory time allowances on recall repairs, investigate whether they are actually spending the time to do the work to completion.
   - Require all old parts to be returned on every job.
   - Maintain the old parts along with the records on each recall repair.

10. Succession. Manufacturers want to know who will take over in the event a dealer dies because they want to prevent control fights and they want to control who will be operating their franchisees. If you do not have a succession plan, expect to face pressure for one. Succession is no longer just an issue for a dealer's accountant and estate attorney. Make sure your plan makes clear who will be in charge if something happens to you, and be prepared to share that with your franchisor.

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FEDERAL ENFORCEMENT

11. It's a New World – enforcement of laws against unfair and deceptive acts or practices**.** The Federal Trade Commission's basic authority is to protect consumers against unfair and deceptive acts and practices. Control of the FTC is changing, and it will soon be under new management – management that one must expect to be zealous in using the power of the FTC to transform the way dealers do business. Expect FTC oversight of dealers to increase in 2022, especially regarding F&I practices as the Commission challenges activities it deems unfair or deceptive.

12. Use a Fair Lending Policy During the Obama administration, the Consumer Financial Protection Bureau challenged dealer reserve practices. The CFPB actions were highly controversial and ultimately led to Congressional disapproval of the CFPB's attempt at regulation. But the concerns over the fairness of pricing vehicle financing have gone on for years, and the criticisms are only expected to increase. To deal with the criticisms, the National Automobile Dealers Association developed a template program for fair lending. It requires a dealer to establish a standard starting point above buy rate for all customers, with downward deviations for non-discriminatory factors. Fair lending oversight at the federal level will increase in 2022. If you did not adopt a policy, or if you adopted one and stopped using it because of lack of emphasis after the Obama administration ended, take steps to adopt the NADA Fair Lending Policy.

13. Establish a Policy for the Sale of VPPs. During the Obama administration, the federal government was reviewing pricing practices for voluntary protection products such as extended service contracts and GAP. The regulators claimed that inflated pricing was evidence of credit discrimination, since one has to analyze the overall costs of lending for a vehicle buyer under credit discrimination laws. To answer the criticisms, NADA, along with the NAMAD and AIADA, developed a template program for sale of voluntary protection products. Federal agencies under the Biden administration will reinstitute investigations into pricing of voluntary protection products. Use the NADA/ NAMAD/AIADA program to protect against charges of discrimination in sale of VPPs.

14. Advertising. Dealers can expect that the Federal Trade Commission will enhance its enforcement activities against dealers in 2022. Whenever the FTC concentrates on dealer activities, the main focus is advertising. Enforcement of the Truth in Lending Act and the Consumer Leasing Act advertising requirements are the cornerstone of enforcement activities. The requirements are black and white. If you use a trigger term, you must make follow on disclosures. If you do not, the FTC has you on a clear cut violation and it can compel you to stop activities it labels "bait and switch" that are less clear cut in consent orders. The FTC expects advertised prices and offers to be available to all unless limitations are clearly and conspicuously disclosed. If limitations make a price or offer unavailable to all, the advertisement must clearly and meaningfully disclose the terms customers must meet to obtain the advertised benefits.

EMPLOYMENT

15. Dealers Create Jobs. If you believe the regulatory environment for employment matters whipsaws based on the administration, you have been paying attention. Republicans view businesses as creating jobs, while Democrats see governmental policy as creating jobs with businesses being the beneficiaries of those policies. For dealers, 2022 will see the manifestations of this view in full as Biden appointees assume full control of the federal agencies with regulatory impact on personnel

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matters. Preventing businesses from taking steps to protect their personnel policies that can be viewed as infringing worker rights in any conceivable way will be the policy that will drive federal personnel law enforcement. Attention to federal pronouncements, being sure documents like personnel handbooks are up to date, and training management personnel in proper actions in this restrictive atmosphere will be important.

16. #MeToo and discrimination and harassment**.** The #MeToo movement may not be getting daily headlines, but that does not mean it has lost its power to affect personnel decisions daily. Just as business, including dealers, will see more restrictive federal personnel policies, they will see more proactive enforcement of perceived claims of discrimination against and harassment of women employees. Is your process for investigating and taking action on complaints of harassment and discrimination established and in use? Remember the key points in any investigation:

- Maintain a neutral demeanor with a complainant.
- Gather facts from the complainant, the subject of the complaint, and witnesses.
- Remind all of the company’s policies on limited confidentiality and against retaliation.
- Evaluate the facts, given important factors:
  - Was there wrongdoing?
  - The severity of activities;
  - The positions of employees;
  - The continuing nature of conduct;
  - The effect on the person complaining; and
  - How were similar situations handled?
- Make a decision and share it with the complainant and the subject of the complaint.

17. COVID-19 Vaccination Mandates and Testing. To require employee COVID vaccinations or testing will be the question facing employers in 2022. What do you do? Much will depend on your own business philosophy once the courts answer whether mandates are constitutional. For some employers, there will be no choice depending on the judicial fate of the Biden private business OSHA mandates and state and local mandates. For dealers not subject to those, it will be a matter of business choice. There will be no easy answers.

18. Pay Plans**.** Workers are more willing to change jobs than ever in 2022. Pay attention to what they want. One key issue is their pay. Workers want to know how they will be paid, and they want the ability to check pay calculations. The days of a pay plan on a napkin are over. Have a template for your pay plans, and develop them based on your template.

OPERATIONS

19. Your Information Safeguarding Obligations WILL Get More Expensive**.** After years of consideration, the FTC published the final revised Safeguards Rule on Oct. 27, 2021. Dealers have one year from original publication to implement new procedures under the revised Rule. The new Rule is not dealer friendly. The original Safeguards Rule maintained flexibility for businesses by allowing them to make their own determinations of the best policies and methods to ensure protection of customer data. The revised Rule removes that flexibility, particularly regarding digital consumer data. The revision makes small companies deemed financial institutions under the Rule, like car dealers, implement procedures used by the world’s largest financial institutions. The changes will dramatically increase a dealer’s costs for compliance with the FTC Safeguards Rule.

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20. Training Employees on the Importance of Online Protections**.** The pandemic required dealers to increase online activities to continue their relationships with customers who could not or would not visit the showroom. The new FTC Safeguards Rule will require dealers to ensure greater online protections for dealer data. Have you worked with your DMS provider to be sure you have the most up-to-date digital protections? If you have computers online that do not operate through your DMS system, work with a consultant to be sure you have effective protections in place. Many employees simply do not understand the seriousness of the issues faced by dealers today from hackers, phishers, and other digital miscreants. Regular training of employees is critical. They must not only understand the protections you have put in place and how they must participate, they must understand the reasons protections are critical. Even with the most sophisticated and up to date intrusion protections, employees can unknowingly subject the system to threats.

21. Do Not Be a Victim of Digital Theft**.** Avoid theft of your data. If your data is compromised, your dealership is a victim since your customer base is a valuable asset. If a bad guy defrauds you of a vehicle through identity theft, you will be the loser either from loss of the value of the vehicle or increased insurance rates if your insurance company pays you for the vehicle. Wire transfers are an especially tempting means of victimizing businesses, and emailed wire transfer instructions must always be verified through a known person or through a known phone number before using them.

22. Suppliers**.** Do not get stuck with unnecessary long-term supplier contracts.

- Have a policy for review, approval, and execution of supplier contracts.
- For each contract, a dealer must ask why a lengthy term is required, and whether there is a benefit to the dealer.
- Do not agree to lengthy contract terms unless there is a reason that benefits you.
- Do not agree to automatic rollovers; at the end to the term, except for month-to-month.

Good luck for a successful 2022!

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