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ResearchReport

Arguments For and Against Direct Sales by Motor Vehicle Manufacturers

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Issue

Discuss the arguments for and against allowing motor vehicle manufacturers to sell their vehicles directly to consumers rather than through franchise dealerships.

Summary

State law generally prohibits motor vehicle manufacturers from selling directly to consumers and instead requires them to sell through a franchise dealer (CGS §§ 14-52b and 42-133cc(8)). (Under an exception to this prohibition, manufacturers may operate a dealership for up to one year, or two years if authorized by the motor vehicles commissioner.) However, the General Assembly is currently considering legislation to allow licensed manufacturers to sell their vehicles directly to Connecticut consumers under certain conditions (HB 7142). It considered similar legislation in each of the last four sessions (see HB 5310 (2018), HB 7097 (2017), SB 3 (2016), and sHB 6682 (2015)).

There is considerable debate about allowing motor vehicle manufacturers to sell their vehicles directly to consumers rather than through franchise dealerships. Proponents, including the Federal Trade Commission's Bureau of Competition and manufacturers such as Tesla, generally argue that the direct sales model lowers end prices for consumers, increases consumer choice between industry brands, and gives manufacturers greater control over marketing and sales. Opponents, including the National Automobile Dealers Association and the Alliance of Automobile Manufacturers, argue that the model reduces price competition, lowers consumer safety, and is less committed to investing in local communities.

Arguments in Favor

Below is a summary of four main arguments typically made by proponents of the direct manufacturer sales model.

1. ***Reduced Vehicle Prices.*** Eliminating dealers as an extra layer to the distribution system reduces transaction costs, such as dealers' price markup to cover their expenses, resulting in lower prices for consumers. Manufacturers have little incentive to mark-up prices beyond what the market will withstand since demand and profits would decrease.

2. ***Increased Consumer Choice***. Allowing manufacturers to directly sell vehicles that would otherwise be unavailable in the Connecticut market through franchise dealerships increases choice between industry brands.

3. ***Greater Control over Sales Process***. Under the dealership model, manufacturers cannot completely ensure that dealers dedicate sufficient resources to the promotion and sale of their brand. Direct sales provide manufacturers more responsibility for and influence over the sales process, including the manner of marketing and customer interaction.

4. ***Wider Availability of Certain Vehicles.*** Certain manufacturers of electric vehicles indicate that their businesses would not be sustainable to traditional dealer franchisees because their cars require less service than those with gas-powered engines, and dealers depend on profits generated from service work. Direct sales are necessary to offer their vehicles on the market and turn a profit.

Arguments in Opposition

Below is a summary of four main arguments typically made by opponents of the direct manufacturer sales model.

1. ***Decreased Price Competition.*** In the absence of multiple dealers competing for a consumer's business, a manufacturer selling directly could have a monopoly on its brand and the ability to set non-negotiable pricing. Manufacturers must charge higher vehicle prices in order to cover the expenses of their retail and service operations, which may include staff, buildings, delivery, and inventory costs.

2. ***Product Development.*** Manufacturers that sell directly must budget for their retail and service operations; the franchise system allows manufacturers to focus on their core competencies and invest more of their capital into designing, engineering, and producing vehicles.

3. ***Consumer Safety.*** Manufacturers have less incentive to issue recalls or incur warranty expenses if there are no franchise dealerships. Dealers are more likely to report issues and act on consumers' behalf because they profit from recall and warranty work, which is paid for by a manufacturer. They also provide an extra layer of accountability for public safety and coverage if a manufacturer goes out of business.

4. ***Local Economic Benefits.*** Profits generated by manufacturer-owned locations flow up to out-of-state shareholders rather than staying in the local community. Independent franchise owners are more invested in the community, and less likely to close their dealerships and move on.

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