



Texas Department *of* Motor Vehicles

HELPING TEXANS GO. HELPING TEXAS GROW.

TxDMV Board Meeting

8:00 a.m.

Thursday, April 1, 2021

**AGENDA
BOARD MEETING
TEXAS DEPARTMENT OF MOTOR VEHICLES
OPEN MEETING VIA
TELEPHONE CONFERENCE CALL*
PURSUANT TO GOVERNOR'S MARCH 16, 2020, TEMPORARY SUSPENSION OF
CERTAIN OPEN MEETING PROVISIONS**
THURSDAY, APRIL 1, 2021
8:00 A.M.**

THIS MEETING WILL BE HELD REMOTELY VIA TELEPHONE CONFERENCE CALL*

Instructions for accessing the meeting via WebEx:

<https://txdmv.webex.com/txdmv/onstage/g.php?MTID=e85ee814213efb7f6b314458c7820300b>

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United States Toll Free: 1-844-740-1264

Event number/Access code: 133 521 0375

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Link to April 1, 2021, TxDMV Board Meeting Documents: <https://www.txdmv.gov/about-us/txdmv-board-meetings>

*The public can listen to the meeting via the WebEx link or the toll-free number listed above. If you have any technical questions about accessing the meeting, please send an email to Board.Tech.Help@txdmv.gov.

**Action by Governor Greg Abbott pursuant to Texas Government Code Section 418.016

<https://gov.texas.gov/news/post/governor-abbott-allows-virtual-and-telephonic-open-meetings-to-maintain-government-transparency>

All agenda items are subject to possible discussion, questions, consideration, and action by the Board of the Texas Department of Motor Vehicles (Board). Agenda item numbers are assigned for ease of reference only and do not necessarily reflect the order of their consideration by the Board. Presentations may be made by the identified staff or Board member or other staff as needed. The Board reserves the right to discuss any items in closed session where authorized by the Open Meetings Act.

- 1. Roll Call and Establishment of Quorum**
- 2. Pledges of Allegiance - U.S. and Texas**
- 3. Chair's Reports - Chairman Treviño**

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- A. 2020 Chairman's Annual Report to the Governor
- B. Introduction of MVCPA Chairman Miguel 'Mike' Rodriguez
- C. Recognition of Service - Shelley Washburn

4. Executive Director's Reports - Whitney Brewster

- 6 A. [Lifting of Temporary COVID-19 Suspensions of Vehicle Registration and Title Requirements, Including External Communications and Impacts](#)
- 7 B. [Operations and Return to 100% Service Capacity under Governor Greg Abbott's March 2, 2021 Executive Order](#)
- C. Call Center Upgrade Update
- D. Introduction of Motor Vehicle Division Director Monique Johnston
- 8 E. [Awards, Recognition of Years of Service, and Announcements](#)

CONTESTED CASE

- 10 5. [Dealership's Protest of an Application for a New Dealership under Tex. Occ. Code §2301.652. MVD Docket No. 19-0005.LIC; SOAH Docket No. 608-19-2065.LIC. Continental Imports, Inc. d/b/a Mercedes-Benz of Austin v. Swickard Austin, LLC d/b/a/ Mercedes-Benz of South Austin, Applicant, and Mercedes-Benz USA, LLC, Intervenor - \(ACTION ITEM\) Monique Johnston](#)

BRIEFING AND ACTION ITEMS

- 402 6. **Finance and Audit Committee Update - Committee Chair Brett Graham**
 - A. [FY 2021 Second Six-Month Internal Audit Plan and Risk Assessment Report](#) - Sandra Menjivar-Suddeath (ACTION ITEM)
 - 418 B. [Internal Audit Division Status Update](#) - Sandra Menjivar-Suddeath (BRIEFING ONLY)
 - Peer Review Process and Self-Assessment
 - 466 C. [FY 2020 End of Year Reports](#) - Linda M. Flores and Eric Horn (BRIEFINGS ONLY)
 - Annual Financial Report
 - Annual Report of Nonfinancial Data
 - 530 D. [FY 2021 Second Quarter Financial Summary Report Including Cumulative Fiscal Impacts of COVID-19](#) - Linda M. Flores, Sergio Rey, and Brian Kline (BRIEFING ONLY)
 - 553 E. [FY 2022-2023 Legislative Appropriations Request Update](#) - Linda M. Flores (BRIEFING ONLY)
 - 562 F. [Winter Storm 2021 Impacts to TxDMV Facilities and Regional Service Centers](#) - Linda M. Flores and Ann Pierce (BRIEFING ONLY)
- 565 7. [Specialty License Plates](#) - Roland Luna, Sr. (ACTION ITEMS)
 - A. Baylor University-Baylor Bear - Crossover Design proposed under Transportation Code, §504.6011 and §504.851
 - B. Texas Criminal Defense Lawyers Association - Redesign proposed under

Transportation Code, §504.851

570

8. [87th Legislative Session Update](#) - Caroline Love
(BRIEFING ONLY)

CLOSED SESSION

9. **The Board may enter into closed session under one or more of the following provisions of the Texas Open Meetings Act, Government Code Chapter 551:**

Section 551.071 - Consultation with and advice from legal counsel regarding:

- pending or contemplated litigation, or a settlement offer;
- a matter in which the duty of the attorney to the government body under the Texas Disciplinary Rules of Professional Conduct of the State Bar of Texas clearly conflicts with Government Code Chapter 551; or
- any item on this agenda.

Section 551.074 - Personnel matters.

- Discussion relating to the appointment, employment, evaluation, reassignment, duties, discipline, and dismissal of personnel.
- Discussion relating to TxDMV dispute resolution process and recent EEOC complaints and internal Civil Rights Office complaints.

Section 551.076 - Deliberation Regarding Security Devices or Security Audits; Closed Meeting.

- the deployment, or specific occasions for implementation, of security personnel or devices; or
- a security audit.

Section 551.089 - Deliberation Regarding Security Devices or Security Audits Closed Meeting.

- security assessments or deployments relating to information resources technology;
- network security information as described by Government Code Section 2059.055(b); or
- the deployment, or specific occasions for implementation, of security personnel, critical infrastructure, or security devices.

10. **Action Items from Closed Session**

11. **Public Comment**

12. **Adjournment**

The Board will allow an open comment period to receive public comment on any agenda item or other matter that is under the jurisdiction of the Board. No action will be taken on matters that are not part of the agenda for the meeting. For subjects that are

not otherwise part of the agenda for the meeting, Board members may respond in accordance with Government Code Section 551.042 and consider the feasibility of placing the matter on the agenda for a future meeting.

If you want to comment on any agenda item (including an open comment under Item #11), you must send an email to GCO_General@txdmv.gov or call (512) 465-5665 to register with one of the following prior to the agenda item being taken up by the Board:

1. a completed [Public Comment Registration Form](#); or
2. the following information:
 - a. the agenda item you wish to comment on;
 - b. your name;
 - c. your address (optional), including your city, state, and zip code; and
 - d. who you are representing.

You must wait for the chairman to call on you before you verbally make your comment via the link or the toll-free number listed above. Each speaker will be limited to three minutes, and time allotted to one speaker may not be reassigned to another speaker.

Agenda items may be presented by the named presenters or other TxDMV staff.

Any individual with a disability who plans to attend this meeting and requires auxiliary aids or services should notify the department as far in advance as possible, but no less than two days in advance, so that appropriate arrangements can be made. Contact David Richards by telephone at (512) 465-1423.

I certify that I have reviewed this document and that it conforms to all applicable Texas Register filing requirements.

CERTIFYING OFFICIAL: Tracey Beaver, General Counsel, (512) 465-5665.

To: Texas Department of Motor Vehicles Board
From: Whitney Brewster, Executive Director
Agenda Item: 4.A
Subject: Lifting of Temporary COVID-19 Suspensions of Vehicle Registration and Title Requirements, Including External Communications and Impacts

RECOMMENDATION

Briefing Only.

PURPOSE AND EXECUTIVE SUMMARY

Texas Governor Greg Abbott suspended vehicle registration and title requirements in March 2020 to accommodate public needs during COVID-19. Those suspensions will conclude on April 14, 2021.

FINANCIAL IMPACT

Not applicable.

BACKGROUND AND DISCUSSION

Department staff has been continuously analyzing compliance with registration and titling requirements this past year. This report will discuss the estimated need for motorists who need to come into compliance and impacts to Texas. Additionally, this report will cover the department's efforts to work with county tax assessor-collectors on communications and efforts to increase awareness of the conclusion of these suspensions and the need for motorist compliance by April 14, 2021.

To: Texas Department of Motor Vehicles Board
From: Whitney Brewster, Executive Director
Agenda Item: 4.B
Subject: Operations and Return to 100% Service Capacity under Governor Greg Abbott’s March 2, 2021 Executive Order

RECOMMENDATION

Briefing only

PURPOSE AND EXECUTIVE SUMMARY

In response to Governor Abbott’s Executive Orders on March 2, 2021 and subsequent guidance to state agencies on March 3, 2021, the TxDMV Reopening Plan was revised. The TxDMV is reopening in compliance with the directive to provide all services at or above pre-pandemic levels on a timeline established by TxDMV management and consistent with the expiration of the registration and title waivers on April 14, 2021.

FINANCIAL IMPACT

None

BACKGROUND AND DISCUSSION

Division directors have been working closely with their staff to plan and implement this transition. Implementation varies significantly across divisions based on the business needs of each division and the division’s current telecommuting status. There is a small team helping plan and implement this change, which entails more employees returning to the worksite.

Criteria for determining those employees returning to the worksite includes specific provisions:

- First, the worksite needs to be fully 100% open to respond to customer visits. TxDMV is implementing this by ensuring that there is at least one person on-site in every division during regular business hours.
- Second, employees handling sensitive confidential paper documents must return to the worksite. For example, employees that work with paper documents containing sensitive data must return to work on-site to access those documents.
- Third, employees must return to work on-site in any area in which the work performance is less than 100% of the work performance pre-pandemic. All services must be provided fully and at the same or better level of service pre-COVID-19. Telecommuting remains an option, and will remain an option, as long as work performance is equal or greater than work performance prior to the start of COVID-19. If performance decreases while telecommuting, telecommuting staff will be required to return on-site for additional oversight, direction, training, and coaching.

Board Meeting Date: 4/1/2021
BRIEFING

To: Texas Department of Motor Vehicles Board
From: Whitney Brewster, Executive Director
Agenda Item: 4.E
Subject: Executive Director's Report – Awards, Recognition of Years of Service, and Announcements

RECOMMENDATION

Board Chair and members offer congratulations to employees receiving recognition for an award, reaching a state service milestone, or retirement.

PURPOSE AND EXECUTIVE SUMMARY

Awards

The Pinnacle of Excellence Award is an annual award designed to recognize one regional services employee for outstanding performance. Each of the 16 regional managers nominated staff who they felt were deserving of this prestigious award. The nominees were carefully evaluated on a variety of criteria, including customer service, job performance, and contributions to their respective offices.

This year's Pinnacle of Excellence Award winner is Jessica Kelley. She currently works in the Longview Regional Service Center as customer service representative and serves as the primary trainer, mentor to new employees, and the webDEALER expert. Jessica grew up in Ore City, Texas, was her high school's valedictorian and went on to earn an Associate of Science degree from Northeast Texas Community College before joining the United States Navy where she served as an information services technician. She then worked for the Gregg County Tax Assessor-Collector before joining the Texas Department of Motor Vehicles in 2013.

Recognition of Service

The Executive Director announces the name of individuals who retired from the agency and recognizes employees who have reached a state service milestone of 20 years and every five-year increment thereafter. Recognition at the April 1, 2021 Board Meeting for state service awards and retirements include:

Service Milestones

- Noemi Edington in Motor Carrier Division reached 20 years of state service
- Brenda Shelton in Enforcement reached 20 years of state service
- Seberina Palamarez in Vehicle Titles and Registration Division reached 20 years of state service
- William Grote Jr. in Information Technology Services Division reached 25 years of state service
- Mary Lou Cardenas in Compliance and Investigation Division reached 30 years of state service
- Dewitt Juul in Finance and Administrative Service reached 35 years of state service
- Rene Medrano in Vehicle Titles and Registration Division reached 40 years of state service

Retirements

- Margaret Zapata - Vehicle Titles and Registration Division
- Mimi Shelton – Enforcement Division
- Reuben Patschke – Information Technology Services Division

FINANCIAL IMPACT

No financial impact.

BACKGROUND AND DISCUSSION

No additional background and discussion.

To: Texas Department of Motor Vehicles Board
From: Monique Johnston, Motor Vehicle Division Director
Agenda Item: 5
Subject: Dealership's Protest of an Application for a New Dealership under Tex. Occ. Code § 2301.652. MVD Docket No. 19-0005.LIC; SOAH Docket No. 608-19-2065.LIC. *Continental Imports, Inc. d/b/a Mercedes-Benz of Austin v. Swickard Austin, LLC d/b/a/ Mercedes-Benz of South Austin, Applicant, and Mercedes-Benz USA, LLC, Intervenor.*

RECOMMENDATION

No staff recommendation is being made. This contested matter is between a license holder and a license applicant.

PURPOSE AND EXECUTIVE SUMMARY

The State Office of Administrative Hearings (SOAH) issued a Proposal for Decision (PFD). The Board may now consider the matter and approve a final order.

The contested case involves the existing dealer's protest of an application for a new franchised dealer license. The existing dealer is Continental Imports, Inc. d/b/a Mercedes-Benz of Austin (MB-Austin), and the new dealership applicant is Swickard Austin, LLC d/b/a/ Mercedes-Benz of South Austin (MB-Swickard). The distributor, Mercedes-Benz USA, LLC (MBUSA), intervened in the case in support of the new dealership.

The issue before the Board is whether MB-Swickard established good cause for a new MBUSA dealership in Austin, Texas under Occupations Code Section 2301.652.

FINANCIAL IMPACT

No significant financial impact to TxDMV.

BACKGROUND AND DISCUSSION

On July 27, 2018, MB-Swickard applied for a new dealership license to sell and service Mercedes-Benz motor vehicles in south Austin, and on September 21, 2018, MB-Austin filed a timely protest. The Motor Vehicle Division (MVD) referred this contested case matter to SOAH on January 17, 2019.

A panel of two administrative law judges (ALJs) conducted the hearing on the merits November 12-15 and 19-22, 2019. The parties filed post-hearing briefs, and the ALJs closed the record of the administrative hearing on May 6, 2020.

The ALJs issued the PFD on July 2, 2020, finding that MB-Swickard met its burden of showing good cause for a new dealership and recommended the Board approve MB-Swickard's application.

On July 24, 2020, MB-Austin filed Exceptions to the PFD, and on August 10, 2020, MBUSA filed a Reply which was joined by MB-Swickard. An ALJ considered the Exception and Reply pleadings and issued an Exceptions Letter on August 21, 2020.

The ALJ Exceptions Letter recommended minor changes to Findings of Fact 38 and 122 and related text, and corrected two additional references in the PFD. The original evidentiary analysis, the decision not to delay the case or reopen the record due to the COVID-19 pandemic, and the recommendation to deny the protest and approve the application for a new dealership remained unchanged.

Attachments

1. The following documents from the SOAH record are attached for consideration by the Board:

Date	Document Description
a. July 2, 2020	SOAH ALJs' Proposal for Decision
b. July 24, 2020	Protestant's Exceptions to the PFD
c. August 10, 2020	Intervenor Mercedes-Benz USA, LLC's Reply to Protestant's Exceptions
d. August 10, 2020	Applicant's Notice of Joinder in Intervenor's Reply
e. August 21, 2020	SOAH ALJ Exceptions Letter

2. Each party also submitted materials for consideration by the Board:
 - a. Protestant Continental Imports, Inc. d/b/a Mercedes-Benz of Austin
 - b. Applicant Swickard Austin, LLC d/b/a/ Mercedes-Benz of South Austin
 - c. Intervenor Mercedes-Benz USA, LLC

FILED
608-19-2065
7/2/2020 3:26 PM
STATE OFFICE OF
ADMINISTRATIVE HEARINGS
Jessie Harbin, CLERK

State Office of Administrative Hearings

Kristofer Monson
Chief Administrative Law Judge

July 2, 2020

Daniel Avitia, Director
Motor Vehicle Division
Texas Department of Motor Vehicles
4000 Jackson Avenue
Austin, TX 78731

VIA EFILE TEXAS

RE: **Docket No. 608-19-2065.LIC; MVD Docket No. 19-0005.LIC; Continental Imports, Inc. d/b/a Mercedes-Benz of Austin v. Swickard Austin, LLC d/b/a Mercedes-Benz of South Austin, Applicant, Mercedes-Benz USA, LLC, Intervenor.**

Dear Mr. Avitia:

Please find enclosed a Proposal for Decision in this case. It contains my recommendation and underlying rationale.

Exceptions and replies may be filed by any party in accordance with 1 Tex. Admin. Code § 155.507, a SOAH rule which may be found at www.soah.state.tx.us.

Sincerely,

Handwritten signature of Beth Bierman in black ink.

Beth Bierman
Administrative Law Judge

Sincerely,

Handwritten signature of Stephanie Frazee in black ink.

Stephanie Frazee
Administrative Law Judge

BB/db
Enclosure

cc: All Parties of Record – **VIA EFILE TEXAS**

Marie Medina, Docket Clerk, Texas Department of Motor Vehicle, 4000 Jackson Avenue, Austin, Texas 78731 - **VIA INTERAGENCY MAIL** (with 1 PHC - CD)

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**SOAH DOCKET NO. 608-19-2065.LIC
MVD DOCKET NO. 19-0005.LIC**

CONTINENTAL IMPORTS, INC.	§	BEFORE THE STATE OFFICE
D/B/A MERCEDES-BENZ OF AUSTIN,	§	
Protestant	§	
	§	
v.	§	
	§	
SWICKARD AUSTIN, LLC D/B/A	§	
MERCEDES-BENZ OF SOUTH	§	OF
AUSTIN,	§	
Applicant	§	
	§	
&	§	
	§	
MERCEDES-BENZ USA, LLC,	§	
Intervenor	§	ADMINISTRATIVE HEARINGS

PROPOSAL FOR DECISION

Swickard Austin, LLC, d/b/a Mercedes-Benz of South Austin (Swickard or Applicant) filed a Franchised New Motor Dealer's License Application (Application) with the Motor Vehicle Division (Division) of the Texas Department of Motor Vehicles to establish a new Mercedes-Benz (MB) dealership in Austin, Texas (South Austin dealership). Continental Imports, Inc. d/b/a Mercedes-Benz of Austin (MB Austin or Protestant), which owns an existing MB dealership in Austin, Texas, a few miles away from the proposed South Austin dealership, initiated this proceeding to protest the Application. Mercedes-Benz USA, LLC (MBUSA or Intervenor), the national distributor of MB, intervened in the proceeding on Swickard's behalf.

Having considered the evidence and the arguments of the parties, and having examined the seven statutory factors applicable under Texas Occupations Code § 2301.652, the Administrative Law Judges (ALJs) find that Swickard and MBUSA proved by a preponderance of the evidence that good cause exists for the establishment of a new MB dealership in Austin, Texas. Therefore, the ALJs recommend approval of the Application.

I. PROCEDURAL HISTORY

On July 27, 2018, Swickard submitted its Application to the Division for the new South Austin dealership, to be located at 10900 South IH-35, Austin, Texas.¹ After receiving the required statutory notice from the Division, MB Austin filed a protest with the Division on September 21, 2018. On January 17, 2019, the Division referred the case to the State Office of Administrative Hearings (SOAH) for a contested case hearing, and issued a Notice of Hearing to the parties. MBUSA intervened in the case, aligned with Swickard, and participated in every stage of the proceeding.

The hearing on the merits was held November 12-15 and 19-22, 2019, before ALJs Beth Bierman and Stephanie Frazee. At the hearing, MB Austin was represented by its counsel, Leon Komkov, Bruce Bennett, and William Crocker; Swickard was represented by its counsel, Nicholas Bader and Jason Allen; and MBUSA was represented by its counsel, Lloyd E. Ferguson, Steven Kelso, and Gwen Young.

Thirteen witnesses testified live at the hearing. MBUSA presented testimony from (1) Steven Nivin, Ph.D., an expert witness in economics; (2) Fred Newcomb, MBUSA manager of dealer compliance and standards; (3) Jason Andersen, a facilities project manager for MBUSA; (4) Edward Hoefl, an after-sales operations manager for MBUSA; (5) Frank Gomez, a sales operations manager for MBUSA; (6) Suzanne Heinemann, CPA, a forensic accountant expert; and (7) Sharif Farhat, an expert for MBUSA and Swickard. Swickard also presented testimony from its owner, Jeffery Swickard. MB Austin presented testimony from (1) Edward Stockton, an expert witness; (2) John Hatch, Ph.D., an expert witness; (3) Bryan Hardeman, owner and dealer-principal for MB Austin; (4) Nicholas Opinker, the service director for MB Austin; and (5) James McGuane, the general manager for MB Austin.

¹ Applicant Ex. 3.

The parties filed post-hearings briefs. In Order No 13, issued March 31, 2020, the ALJs denied MBUSA's motion to strike MB Austin's filing of proposed findings of fact and conclusions of law, but granted MBUSA's motion to allow it to file proposed findings and conclusions, which were filed April 17, 2020. By Order No. 13, the record was to have closed April 17, 2020. In the interim, however, starting on April 13, 2020, MB Austin filed several motions requesting official notice of COVID-19 pandemic-related governmental orders, and requesting abatement of this case due to the change in economic conditions. The motions were opposed by MBUSA and Swickard. In Order No. 14, issued May 6, 2020, the ALJs granted the request to take official notice of pandemic-related orders issued by the Texas Governor, City of Austin Mayor, and Travis and Williamson County Judges; denied the request to take official notice of other documents; and denied the motion to abate. The record in this case closed with the issuance of Order No. 14 on May 6, 2020. In Order No. 15, issued July 1, 2020, the ALJs granted the requests to take official notice of additional pandemic-related orders issued by the Texas Governor, but denied MB Austin's motion to reopen the record or to abate this case.

II. APPLICABLE LAW

A person has standing to protest an application to establish a dealership if the person filing the protest is a franchised dealer of the same line-make whose dealership is located either in the county in which the proposed dealership is to be located, or within a 15-mile radius of the proposed dealership.²

When a protest has been filed, the Division may deny the application if good cause is not shown for establishing the new dealership.³ In determining whether there is good cause, the Division must consider the following factors enumerated in section 2301.652 of the Texas Occupations Code:

² Tex. Occ. Code § 2301.652(b). The parties agree that MB Austin meets these standing requirements.

³ Tex. Occ. Code § 2301.652(a).

- (1) whether the manufacturer or distributor of the same line-make of new motor vehicle is being adequately represented as to sales and service;
- (2) whether the protesting franchised dealer representing the same line-make of new motor vehicle is in substantial compliance with the dealer's franchise, to the extent that the franchise is not in conflict with this chapter;
- (3) the desirability of a competitive marketplace;
- (4) any harm to the protesting franchised dealer;
- (5) the public interest;
- (6) any harm to the applicant; and
- (7) current and reasonably foreseeable projections of economic conditions, financial expectations, and the market for the new motor vehicles in the relevant market area.⁴

Under the statute, Swickard has the burden of demonstrating good cause for the establishment of its proposed Austin MB dealership.⁵

III. FACTUAL BACKGROUND

A. Market Study of the Austin Sales Locality

Austin's population has grown significantly over the last decade and is projected to continue to grow.⁶ From 1978 until 2004 or 2005, when Mercedes-Benz of Georgetown (MB Georgetown) relocated from Temple to the north edge of the Austin metro market, MB Austin was the only dealer in the Austin market. During that time, the population of Austin more than doubled from about 585,000 people in 1980 to 1.25 million in 2000.⁷ From

⁴ Tex. Occ. Code § 2301.652(a).

⁵ Tex. Occ. Code § 2301.652(a).

⁶ Tr. 157-89; Exs. I-65, I-71.

⁷ Tr. at 488-89; Ex. I-65.

2000 to 2017, the population grew to approximately 2.1 million people.⁸ Population growth in Austin since 2011 has been very strong both as to total population and population within the ages of 18-65, and has been stronger than other major Texas metro areas from 2011-2018.⁹ Projections by the Texas Demographic Center predict that Austin will continue to have the strongest population growth compared to other major metro areas in Texas through 2034.¹⁰

Between 2001 and 2017, Austin's gross domestic product (GDP)¹¹ more than doubled from \$62 billion to \$135 billion. That time period included the 2008 recession and subsequent recovery.¹² Austin's GDP growth rate has averaged 5 percent since 2002, and averaged 6.4 percent from 2010-2017.¹³ By contrast, the next highest rate in a Texas metro area was San Antonio, which had 3.7 percent GDP growth since 2002. U.S. GDP growth has averaged only 2.5 to 3 percent each year.¹⁴ In Austin, per capita GDP has grown from \$47,169 in 2001 to \$65,839 in 2017.¹⁵

Employment in Austin has grown from 387,000 jobs in 1990 to over one million in 2019, for an average annual growth rate of 3.63 percent. This is a stronger rate of growth than any other Texas metro area.¹⁶ Unemployment rates since 1990 have averaged 4.2 percent annually in Austin, 5.8 percent in Texas, and 5.9 percent in the U.S.¹⁷ Austin's economy has become more diversified over the past 30 years and has increased the number of higher-paying jobs, leading to higher

⁸ Tr. at 1718-19.

⁹ Tr. at 158, 160; Ex. I-71.

¹⁰ Tr. at 158-59; Ex. I-71.

¹¹ Gross domestic product refers to a broad measure of the value of all the goods and services produced within an economy. *See* Tr. at 160.

¹² Tr. at 161-64; Ex. I-71.

¹³ Tr. at 164-65; Ex. I-71.

¹⁴ Tr. at 166-67.

¹⁵ Tr. at 165-66; Ex. I-71.

¹⁶ Tr. at 168-69; Ex. I-71.

¹⁷ Tr. at 171-72; Ex. I-71.

household incomes and declines in the number of lower-income households.¹⁸ The highest growth has been seen in households with annual incomes of \$200,000 and above per year, the highest income strata, which means large growth in the luxury car-buying population.¹⁹

B. MB Austin's Performance in Austin Sales Locality

1. Dealer Background

MBUSA is the exclusive U.S. distributor of MB vehicles in the United States.²⁰ Under the Texas Occupations Code, MBUSA can only market and sell its vehicles to the consuming public and have those vehicles serviced under warranty through its network of dealers.²¹

MB Austin has been an authorized MB dealer since 1978.²² Mr. Hardeman, through his corporation, Continental Imports, Inc., purchased MB Austin with his then-business partner and now owns it with his family.²³ Mr. Hardeman has been the sole dealer-principal of MB Austin since the purchase.²⁴ In about 1987, MB Austin moved to its current location on Airport Boulevard.²⁵ Approximately 13 years ago, Mr. McGuane became MB Austin's General Manager and has handled its day-to-day operations.²⁶ In May 2019, Mr. Hardeman became the owner and dealer-principal of MB San Juan in the Rio Grande Valley.²⁷ Continental Imports, Inc. also owns a Honda dealership and operates, or has operated, other related businesses including

¹⁸ Tr. at 173-76; Ex. I-71.

¹⁹ Tr. at 180-81, 435-36, 489-92; Exs. I-65, I-71.

²⁰ Tr. at 232, 248-50.

²¹ Tr. at 248; *see generally* Tex. Transp. Code ch. 2301.

²² Tr. at 1263.

²³ Tr. at 1261-62, 1265-66.

²⁴ Tr. at 1263, 1273-74.

²⁵ Tr. at 1264-65.

²⁶ Tr. at 1524-25, 1386-87.

²⁷ Tr. at 1272-73, 1375-76.

Wholesale Parts Direct and Continental Collision Center, and has operated in conjunction with Mr. Hardeman's other entities such as Continental Auto Leasing.²⁸ Hardeman Family Joint Venture owns the MB Austin dealership property.²⁹ MB Austin is currently building a parking garage for inventory storage, wholesale parts storage, service customer vehicle parking, employee parking, and additional service bays.³⁰

MB has underperformed in MB Austin's Area of Influence (AOI)³¹ in terms of both sales volume and registration effectiveness compared to its three primary competitors: BMW, Lexus, and Audi.³² As of year-to-date in June 2019, the Austin AOI had only 458 total MB vehicles registered, and 330 of those sales were made by MB Austin, compared to 925 BMWs, 912 Lexuses, and 665 Audis registered in the Austin AOI in the same time period.³³ MB is being outsold by all of its primary competitors' brands, in particular in the lower-priced, entry-level luxury vehicles like the C-Class sedan and GLC SUV segments:³⁴ in the C-Class market segment, 49 MB vehicles were registered, versus 148 for BMW, 209 for Lexus, and 83 for Audi, as of June 2019.³⁵ In the Austin AOI, the MB brand is below its national market share, and BMW, Lexus, and Audi are all above their national market shares.³⁶ By contrast, in MBUSA's Southern Region, year-to-date as of September 2019, MB outsold BMW by 2,700 vehicles and only fell behind BMW nationally in 2019 by 5,000 units (500 of which are in the Austin AOI).³⁷

²⁸ Tr. at 1329-32, 1336-37, 1339-41.

²⁹ Tr. at 1266.

³⁰ Tr. at 1268-69, 1274-76.

³¹ "Area of Influence" or "AOI" is a geographic area defined by a collection of contiguous ZIP codes around the location of a given dealer. ZIP codes are assigned to a given dealer's location by their proximity to the dealer, determined by calculating the closest dealer from the center of a given ZIP code by drive time or drive distance. Tr. at 318-19, 433.

³² Tr. at 108; Ex. P-23.

³³ Tr. at 1087-88.

³⁴ A segment is part of a manufacturer's product line up such as compact cars, mid-size cars, or large SUVs. *See* Tr. at 99.

³⁵ Tr. at 1090, 1092-93; Ex. P-23.

³⁶ Tr. at 1089-90; Ex. P-23.

³⁷ Tr. at 1088-89; Ex. I-65.

The number of new luxury-brand dealerships in the Austin Area of Responsibility (AOR)³⁸ has increased over the past few years – a new Lexus dealership opened in Lakeway in 2015, BMW opened a new dealership in South Austin in 2018, and a new Jaguar/Land Rover dealership is planned northwest of central Austin.³⁹ Based on national registrations, the expectation for MB in 2018 in the Austin AOR was 2,006 vehicles registrations, but there were only 1,581; similarly, MB had a shortfall of 300 vehicle registrations for Texas.⁴⁰ The MB brand has performed below average in the Austin market for at least the last five years.⁴¹ MBUSA determined that a third dealership is needed in the Austin AOR to have the same percent of competitive dealerships as it has in the other markets.⁴²

As general manager, Mr. McGuane oversees the sales, service, and fixed operations of the dealership. Mr. McGuane started as a service technician in the late 1970s. After that, he held positions as a service consultant, service manager, service director, parts and service director, and vice president. Prior to his employment with MB Austin, Mr. McGuane has worked for Toyota, Lexus, Ford, and Lincoln Mercury. Mr. McGuane is responsible for ensuring that every entry on MB Austin's financial statement is made accurately and in compliance with MBUSA's Dealer Accounting Manual.⁴³

Mr. McGuane stated that for about ten months MB Austin went without an after-sales market (ASM) representative before Mr. Hoefl had been tasked with that role. Mr. Hoefl, he said, has been the ASM representative for MB Austin for approximately one year.⁴⁴ The lack of an ASM

³⁸ AORs are collections of AOIs that are connected economically by things like retail shopping and commuting patterns. Tr. at 430-33, 436; Ex. I-65.

³⁹ Tr. at 433-35; Ex. I-65.

⁴⁰ Tr. at 452-53; Ex. I-65.

⁴¹ Tr. at 469-70; 477.

⁴² Tr. at 478-82, 1028-29; Ex. I-65.

⁴³ Tr. at 1524-25, 1527.

⁴⁴ Tr. at 1534.

representative for those ten months had a negative impact on MB Austin's operations, claimed Mr. McGuane, because MB Austin could not resolve service cases, could not discuss with MBUSA its difficulty with obtaining parts, and could not get authorization or direction from MBUSA to repair vehicles. He admitted, however, that MB had assigned an employee to help cover MB Austin during the interim.⁴⁵ Mr. McGuane agreed that his relationship with Mr. Hoefl had been contentious on occasion, but he denied disliking Mr. Hoefl personally and denied that he himself was intimidating or a bully.⁴⁶ In his role as ASM, Mr. Hoefl was the MBUSA contact person for Mr. McGuane when MB Austin could not obtain necessary parts or a software patch to complete repairs.

According to Mr. McGuane, MB Austin rarely saw the MBUSA field technical specialist, so there were delays in MB Austin getting authorizations for repairs that ultimately resulted in MB Austin's inability to timely perform service work for customers.⁴⁷

Mr. McGuane explained that MBUSA assesses a dealer's service performance using various metrics, including the customer experience index (CEI), the fixed first visit (FFV) metric that means "fix it right the first time," and the service opportunity index (SOI). For the CEI in terms of service provided, Mr. McGuane stated that MB Austin was well above the benchmark, which he clarified included the national, regional, and area averages. He pointed out that the dealer was able to perform even though the current construction at MB Austin hampered operations.⁴⁸ MB Austin's SOI was also above the national, regional, and area average, he said.

MB Austin's dealer performance scorecard showed that it was above the objectives set by MBUSA in terms of assessing bonus and incentive eligibility, according to Mr. McGuane.⁴⁹ In February 2019, MB Austin ranked twenty-fourth in overall new-vehicle sales rankings for the

⁴⁵ Tr. at 1535.

⁴⁶ Tr. at 1536-37.

⁴⁷ Tr. at 1541.

⁴⁸ Tr. at 1544-45.

⁴⁹ Tr. at 1546-49; Ex. P-20.

southern region, and fourth in sales of certified pre-owned vehicles.⁵⁰ As of October 2019, MB Austin ranked twentieth and fourth for the southern region in sales of new and certified pre-owned vehicles, respectively.⁵¹ MB Austin's used-to-new ratio was 1.6 to 1, which meant that the dealer sold 1.6 used cars for every new vehicle sold. A large portion of the dealer's sales were in mid- to large-size SUVs, which Mr. McGuane clarified was somewhere between twenty-five to fifty percent of sales. Mr. McGuane asserted that MB Austin's sales were hampered by difficulties obtaining the large size GLE SUV.⁵² Some customers had deposits on hold for the GLEs for up to eleven months. Some customers eventually reclaimed their deposits.⁵³ Mr. McGuane admitted, however, that MB Austin did not have a current deficit for the vehicles and that the MB Austin website listed 71 GLE models for sale.⁵⁴

Mr. McGuane agreed that MB Austin's profits jumped from 2017 to 2018. He attributed the increase to the quality of the employees and the improved processes at the dealership. He denied that MB Austin was selling vehicles at excessive prices or above market rates for those vehicles. He also denied that the dealership was billing labor rates above the market rate or overbilling for warranty work.⁵⁵ In terms of service technicians, Mr. McGuane testified that MB Austin was paying above the Austin market for those technicians.⁵⁶ He did not think that the dealer could hire more technicians by raising compensation.

According to MB Austin's 2019 business plan, MB Austin was \$850,000 ahead in net profit for 2018 compared to 2017, excluding consideration of December 2018.⁵⁷ For new sales, Mr. McGuane agreed that MB Austin planned to increase its "look to book" percentage so that

⁵⁰ Ex. P-22.

⁵¹ Tr. at 1551.

⁵² Tr. at 1554.

⁵³ Tr. at 1555.

⁵⁴ Tr. at 1567.

⁵⁵ Tr. at 1558.

⁵⁶ Tr. at 1563.

⁵⁷ Ex. I-23.

MB Austin would keep at least 50 percent or more of the value of the vehicles taken as trade-ins.⁵⁸ In the pre-owned department, the business plan indicated that the dealer was focused on a 72-hour reconditioning time from start to finish to get a pre-owned vehicle ready for sale. The 2018 net profit for the service department was up \$686,000 through November 2018. The 2019 business plan stated that MB Austin planned to hire three technicians. At the hearing, Mr. McGuane indicated that three technicians had been hired but other technicians had left, so the number of technicians MB Austin employed was approximately the same. According to Mr. McGuane, MB Austin was projecting a slight five percent increase in net profits for its body shop, and hoped to increase sales and gross profits in its parts department.⁵⁹

2. MB Austin's Sales Performance

MB Austin's sales effectiveness has been below 100 percent since at least 2012.⁶⁰ The Austin AOI was at 75.6 percent registration effectiveness in 2018.⁶¹ As of September 2019, it was at 75 percent sales effectiveness.⁶² Of the ten AOIs in Market 12, MB Austin's AOI ranked last in registration effectiveness as of June 2019.⁶³ With the proposed South Austin AOI removed, MB Austin's AOI was the ninth-worst-performing AOI in Texas under MBUSA's national standard and the eighth-worst under the Texas standard. The proposed South Austin AOI was the fourth-worst under the national standard and the third-worst under the Texas standard.⁶⁴

Mr. Hardeman testified that he prefers to sell high-end vehicles rather than entry-level vehicles, such as C-Class vehicles, because of the higher profit margins on the more expensive

⁵⁸ Tr. at 1575.

⁵⁹ Tr. at 1577.

⁶⁰ Tr. at 297-99, 1080. Sales effectiveness is a term representing the ratio of any individual dealership's reported sales of new MB vehicles to an expected number of sales based on the competitive registrations in that dealer's AOI. Sales effectiveness relates to a dealer's performance. Tr. at 296-97.

⁶¹ Tr. at 463-65; Ex. I-66.

⁶² Tr. at 594, 1098-99.

⁶³ Tr. at 1081. Market 12 refers to a region of the United States that includes Austin. Tr. at 1079.

⁶⁴ Tr. at 443-45; Ex. I-65.

vehicles.⁶⁵ However, the GCL and C-Class are first and second on the list of vehicles that other dealers are selling into the Austin AOI.⁶⁶ As of the June 2019 monthly dealer report, 264 vehicles were sold into the Austin AOI, and 98 were sold by MB Austin to a location outside its AOI.⁶⁷ Overall, MB is ranked 10 out of 10 in registration effectiveness compared to other brands in the Austin AOI.⁶⁸ MBUSA witness Mr. Gomez testified that nationwide, MB trails BMW by 5,000 vehicles sold as of the June 2019 report.⁶⁹ According to Mr. Gomez, if the Austin AOI vehicle deficit was removed, the national deficit would be cut by 20 percent.⁷⁰ MB Austin failed to meet its sales objectives in 2017 and 2018, and it was behind its 2019 objective as of the hearing.⁷¹ Mr. Gomez testified that an underperforming dealer will have lower sales objectives than a high-performing dealer; therefore, a dealer that is meeting its sales objectives may still be performing inadequately compared to other dealers.⁷²

MB Austin is compliant with MBUSA's brand standards regarding the design, layout, and finishing's at its dealership facility. However, MBUSA describes MB Austin as only minimally compliant and lists the following deficiencies when comparing MB Austin to MB Georgetown and BMW of South Austin: (1) confusing one-way entry from the street, tight parking lot, and lack of a straight entry into the dealership; (2) dark, recessed, covered entry portal; (3) low ceilings in the showroom, dark due to lack of natural light and extensive gray wall covering; (4) uncovered drive-up service lanes that should be covered to protect customers from heat, cold, and rain; (5) no air conditioning in the service bay areas to provide comfort for service employees; (6) cluttered boutique area with low-end fluorescent lighting and non-compliant fixtures; and (7) generally

⁶⁵ Tr. at 1396. According to Mr. Hardeman, the dealer loses approximately \$700 on every C-Class vehicle sold and something under that amount for every A-Class vehicle sold. Tr. at 1304.

⁶⁶ Tr. at 1078.

⁶⁷ Tr. at 1091-92; Ex. P-23.

⁶⁸ Tr. at 1081.

⁶⁹ Tr. at 1086-89; Ex. P-23.

⁷⁰ Tr. at 1089.

⁷¹ Tr. at 1677.

⁷² Tr. at 1677-78.

messy, untidy customer-facing areas with some cracked, dirty, non-compliant tile.⁷³ MB Austin's location is near train tracks and lower-end businesses rather than a high-end retail area, and its location leaves no room to expand other than building upward.⁷⁴

3. MB Austin's Service Performance

MBUSA's monthly SOI reports show the percentage of serviced vehicles in an AOI and the number of MB vehicles in the AOI that were not serviced by an MB dealer (un-serviced vehicles).⁷⁵ As of December 2018, of the nearly 12,400 MB vehicles registered in MB Austin's AOI, 4,615 were not serviced within the previous 13 months by any MB dealer. MBUSA estimates the dollar value of lost opportunity to MB dealers of almost \$5.4 million.⁷⁶ Of the 7,900 serviced vehicles, MB Austin only serviced 43 percent, leaving 3,900 un-serviced vehicles in the Austin AOI.⁷⁷

MBUSA is concerned not just about the lost profit but the loss of customer loyalty and retention that results when MB vehicles are serviced by other providers.⁷⁸ MBUSA wishes to attract and retain entry-level customers who are typically younger and at the start of their careers because when such customers are retained, they will purchase more expensive vehicles as time passes.⁷⁹ MBUSA views servicing vehicles as a way to maintain customer loyalty and has counseled MB Austin on MBUSA's advertising tools to increase service business.⁸⁰ However, MB Austin has declined to take advantage of MBUSA's advertising and marketing plans, in part because MB Austin is at full service capacity and additional customers would increase customer

⁷³ See MBUSA Proposed Finding of Fact No. 182; Tr. at 623-24, 627, 629-32; 632-65; Exs. I-49, I-50, I-51, I-52.

⁷⁴ Tr. at 623-25.

⁷⁵ Tr. at 851-52, 854-55; Ex. I-26.

⁷⁶ Tr. at 856-57, 870, 882-83; Ex. I-26.

⁷⁷ Tr. at 856-57, 869, 880, 882-83; Ex. I-26.

⁷⁸ Tr. at 260-61.

⁷⁹ Tr. at 858-60; 1372-73, 1517-18; Ex. I-26;

⁸⁰ Tr. at 860-62; 892-93.

wait times.⁸¹ MB Austin's customers have wait times of 7 to 10 days or longer for services other than oil changes.⁸² MB Austin's service director stated that if it had 6 to 8 more service technicians, it could perform better service and take in more service work.⁸³ MB Austin's service shop is not air conditioned and gets to 85 degrees or more in the summer.⁸⁴ MB Austin lost 15 to 20 percent of its service technicians during the summer of 2019.⁸⁵

Mr. Opinker has been the service director for MB Austin for three years. Prior to his current position with MB Austin, Mr. Opinker worked as the service director for other MB dealers in Wisconsin and Plano, Texas. In the beginning of his career, Mr. Opinker was a service technician for BMW, Porsche, Alfa Romero, and DeLorean.

Mr. Opinker testified that MBUSA uses various measures or indices to gauge the performance of the service departments, including the CEI, FFV, and SOI. For CEI and SOI, Mr. Opinker stated that MB Austin was above the benchmarks. He pointed out that the service department's parts and service advisors and technicians at MB Austin had been recognized as the "Best of the Best" by MBUSA.⁸⁶

The dealership currently employs 32 service technicians, but still needs approximately six to eight more. Mr. Opinker said that there was a shortage of qualified service technicians to work on luxury brands. Other dealers and MBUSA, he said, were offering signing bonuses, sometimes up to \$10,000, for service technicians. MB Austin has a listing on Indeed for service technicians, and the shop foreman and service manager were going to high schools and colleges to recruit. Mr. Opinker denied that MB Austin was having a problem retaining its technicians, even though the service shop is not fully air conditioned. Mr. Opinker noted that MBUSA is hiring technicians

⁸¹ Tr. at 861-62.

⁸² Tr. at 862-64, 1234-36, 1454.

⁸³ Tr. at 1501-02.

⁸⁴ Tr. at 866, 897-98; 1515-16.

⁸⁵ Tr. at 864-65.

⁸⁶ Tr. at 1408.

to work on the GLEs that were being assembled improperly at the plant in Alabama. He testified that the GLEs lacked fitment quality and performance, and that the overall quality of the vehicles were poor.⁸⁷

Mr. Opinker thought that the new South Austin MB dealer would have to pay a premium, perhaps \$40 per hour, or about \$100,000 per year, in order to hire approximately 26 service technicians at the new location.⁸⁸ MB Austin currently has 52 service bays at its facility. The new construction at the dealership will add another 14 service bays to bring the total to 66 service bays, which would require MB Austin to hire additional technicians.

According to MB Austin's Dealer Financial Statements, MB Austin had an increase in productivity from 2017 to 2018.⁸⁹ Mr. Opinker explained that this increase was due to the fact that the dealer streamlined processes, realigned the service shop, and readjusted the teams so that they were more balanced.⁹⁰ Efficiency decreased somewhat in 2018 because the focus was on repairs. To his knowledge, Mr. Opinker believed MB Austin's efficiency rating was above MBUSA's standard for technician efficiency. Service hours for technicians increased from 2017 to 2018 because of the improved processes in the shop and an increase in the number of technicians, Mr. Opinker said.

According to Mr. Opinker, if the dealer is at or above benchmark for the CEI, the dealer is awarded a percentage of the manufacturer's suggested retail price (MSRP) off each new vehicle sold in the sales department.⁹¹ In 2016, he said the dealer did "pretty well" with Service Net Promoter Score (NPS), which is an indication that the customer would recommend service at MB Austin. In 2017, MB Austin raised the service CEI to be above the benchmark towards the end of the year. The service NPS also increased through 2017. In 2018, MB Austin was

⁸⁷ Tr. at 1410.

⁸⁸ Tr. at 1411-12; Ex. I-42 at 1.

⁸⁹ Tr. at 1422-23; Exs. I-11 at 12, I-14 at 12.

⁹⁰ Tr. at 1423.

⁹¹ Tr. at 1425.

consistently above the benchmark for service CEI and service NPS.⁹² MB Austin achieved the customer service bonus for every quarter of 2016.⁹³ In 2017, the dealer missed the benchmark for a couple of quarters, but met the benchmark in the final quarter.⁹⁴ In 2018, MB Austin again achieved the bonus in every quarter.⁹⁵

The service capture rate for MB Austin's AOI was below the national and regional benchmark for the service opportunity capture rate during December 2018. The number began to increase, however, and by February 2019, the service capture rate in MB Austin's AOI was above regional and national benchmarks.⁹⁶ From March through June 2019, MB Austin's service capture rate was again above regional and national benchmarks.⁹⁷ This trend continued from August through October 2019.⁹⁸ Mr. Opinker conceded that the SOI score represents the total percentage of service that is performed within MB Austin's AOI based on MB Austin's contribution and all the other dealer's service work in the AOI.⁹⁹

Mr. Opinker stated that MB Austin had an express service department tailored for routine maintenance, where most customers could receive same-day or next-day service. For more advanced service requests, more notice was needed to meet the customer's request. It took approximately seven to nine days to get a customer into a loaner vehicle if more advanced work was needed and a loaner vehicle was requested.¹⁰⁰ Mr. Opinker blamed the delay on the dealer's inability to obtain necessary parts or receive necessary support from MBUSA for software fixes.¹⁰¹

⁹² Tr. at 1426-28; Exs. P-15, P-16, P-17.

⁹³ Tr. at 1429-30; Ex. P-18.

⁹⁴ Ex. P-19.

⁹⁵ Ex. P-20.

⁹⁶ Tr. at 1441; Exs. I-16, P-25.

⁹⁷ Exs. P-26, P-27, P-28, P-29.

⁹⁸ Exs. P-61, P-62.

⁹⁹ Tr. at 1493-94.

¹⁰⁰ Tr. at 1454.

¹⁰¹ Tr. 1455, 1463, 1474-76.

MB Austin offers pick-up and delivery service, and will also send a technician out to a customer's location to perform minor services. MB Austin has one mobile van and one roadside assistance van.¹⁰²

Mr. Opinker agreed that if he could hire more technicians, he could increase the amount of service work performed and money earned by MB Austin.¹⁰³ He denied, however, that MB owners may be taking their vehicles for repair at independent shops because of the labor rates for service an MB Austin. In fact, he said, independent shops bring vehicles to MB Austin to fix. The independent shops then mark up the cost of repair to their customers.¹⁰⁴ MB Austin's posted "door rate" for service labor (also called "customer pay") is \$160 per hour, but the effective rate is actually \$125, he said. MB Austin charges MBUSA \$157.20 per hour for warranty repairs.¹⁰⁵

Mr. Hardeman testified that MB Austin is likely to keep its service business if the South Austin point opens.¹⁰⁶ Mr. Stockton testified that he believes the impact on MB Austin's service business will be less than he would expect from his gravity model (discussed below) because traffic patterns give MB Austin a better location relative to daily commuters, and MB Austin is near employment centers.¹⁰⁷

C. MBUSA's Decision to Establish a New Dealership in Austin

To keep up with increasing competition from other luxury brands, MBUSA continually evaluates the U.S. on a market-by-market basis by looking at the performance of the brand and each dealer, applying analytics to data such as registrations, demographics, and other

¹⁰² Tr. at 1501.

¹⁰³ Tr. at 1501-02.

¹⁰⁴ Tr. at 1502.

¹⁰⁵ Tr. at 1503, 1515.

¹⁰⁶ Tr. at 1393-95.

¹⁰⁷ Tr. at 1019-20.

market-specific data.¹⁰⁸ Since 2001, MBUSA's network has grown from 320 dealers to 384, covering 220-240 of the U.S.'s approximate 800 markets.¹⁰⁹ During that same time period, MBUSA's national sales of MB vehicles has more than doubled, the number of exclusive MB dealerships has doubled, the MB vehicle product line has broadened significantly and become more complex, and customer expectations have increased and become more sophisticated.¹¹⁰ MB dealers are selling twice the volume of vehicles as in 2001, and average dealer throughput (the number of new vehicles sold per dealer) and the average number of vehicles serviced per dealership have grown significantly.¹¹¹

Also since 2001, new luxury brands have been introduced in the market (Lexus, Acura, Infiniti, and Hyundai's Genesis brand, as well Land Rover and Audi), which have increased competition in the market.¹¹² In order to meet competition, MBUSA desires to add a dealership in South Austin as part of a larger planning and assessment process in connection with MBUSA's parent company Daimler's worldwide MB 2020 program.¹¹³ MB 2020 began in anticipation of Daimler's planned large-scale introduction of new vehicle models in segments in which it had never competed and large increases in volumes of most existing models.¹¹⁴ The specific new segments Daimler was developing and has introduced included entry-level luxury sedans and SUVs, like C- and A-Class sedans and GLA and GLB SUVs.¹¹⁵ The intent of these new vehicle segments was to attract younger, less-affluent buyers at a price point they could afford and gain customer loyalty through having their vehicles serviced at MB dealerships.¹¹⁶ Entry-level luxury segments are becoming a more competitive part of the luxury marketplace, and Daimler views it

¹⁰⁸ Tr. at 247-50, 258-60.

¹⁰⁹ Tr. at 248-49.

¹¹⁰ Tr. at 248-49.

¹¹¹ Tr. at 248-50.

¹¹² Tr. at 228, 252-53.

¹¹³ Tr. at 253.

¹¹⁴ Tr. at 253-54.

¹¹⁵ Tr. at 255-56.

¹¹⁶ Tr. at 256-57.

as important to have in place a dealer network that supports the corporate goal of reaching and successfully “conquering” entry-level luxury buyers from other brands.¹¹⁷ Daimler also desires to increase customer satisfaction and convenience by shortening distances to MB dealerships and by increasing the capacity of the dealer network to satisfy the service needs of customers.¹¹⁸

MB’s goal is to achieve an optimal dealer network in the markets where it chooses to have representation.¹¹⁹ An optimal dealer network is one with the proper number of dealerships, dealerships in the right location, and the best dealer partners representing the brand.¹²⁰ MB identified the Austin market as one where MB was lagging behind its competitors in terms of sales and customer convenience and viewed Austin as subpar for years in the context of Austin’s population growth, particularly of higher-income households.¹²¹ In 2014, MBUSA’s executive Network Review Committee (NRC) decided to add a dealer in the Austin metro area.¹²²

The NRC approved Berkshire Hathaway Automotive (Berkshire Hathaway) as its candidate for the dealership.¹²³ In September 2016, MBUSA approved the candidate’s proposed site at 10900 South IH-35 due to the availability of land and appropriate zoning there, close proximity to MBUSA’s competitors (including BMW), proximity to a major highway, and being central to the area of the most lost sales to its competitors.¹²⁴ MBUSA gave notice to the existing dealers of its planned establishment of a new dealer, and MB Austin protested.

¹¹⁷ Tr. at 257, 260-61. The term “conquest” refers to converting a customer from one brand, i.e. BMW, to another, i.e. MB. *See* Tr. at 101.

¹¹⁸ Tr. at 262-63, 308-10.

¹¹⁹ Tr. at 251.

¹²⁰ Tr. at 251.

¹²¹ Tr. at 264-66.

¹²² Tr. at 265-67.

¹²³ Tr. at 269-70.

¹²⁴ Tr. at 270-78; Exs. I-37, I-38.

Berkshire Hathaway ultimately withdrew when it was unable to obtain a dealership license under Texas Occupations Code § 2301.476, which prohibited it from owning dealerships in Texas because it was also a manufacturer of recreational vehicles.¹²⁵ On July 13, 2018, Mr. Hardeman sent a letter to MBUSA requesting to be the candidate for a new dealership located in southwest Austin.¹²⁶ MBUSA did not consider Mr. Hardeman for the new point; MBUSA did not want to replicate MB Austin's historic performance at an additional location.¹²⁷ Mr. Swickard had expressed interest in a dealership in Austin to MBUSA's then-CEO Dietmar Exler in 2017. When Berkshire Hathaway withdrew, Mr. Exler proposed Mr. Swickard as the candidate for the South Austin dealership.¹²⁸ In December 2017, the NRC approved Mr. Swickard as its candidate for the South Austin dealership.¹²⁹ Mr. Swickard entered into a letter of intent with MBUSA in April 2018, and after reviewing various locations, he purchased Berkshire Hathaway's property on South IH-35.¹³⁰

The distribution of luxury vehicle registrations in the AOR has its highest density between MB Austin and the proposed South Austin site.¹³¹ In the South Austin AOI, existing luxury-brand owners must drive an average of 20.7 miles to the nearest MB dealer, compared to 15.1 miles to a BMW dealer, 15.6 miles to an Acura dealer, 15.8 miles to an Audi dealer, and 17.7 miles to a Lexus dealer.¹³² The proposed new dealership has ready access and visibility from the IH-35 thoroughfare, is next to a Volkswagen dealership, and has appropriate land area and zoning to

¹²⁵ Tr. at 279-81.

¹²⁶ Tr. at 293-94; Ex. I-43.

¹²⁷ Tr. at 295.

¹²⁸ Tr. at 282-83

¹²⁹ Tr. at 281-83; Exs. I-39, I-40.

¹³⁰ Tr. at 275-81, 290.

¹³¹ Tr. at 492-93; Ex. I-65.

¹³² Tr. at 498-500; Ex. I-65.

accommodate the dealership.¹³³ According to MBUSA witness Mr. Hoefl, the new location would cover many of the areas where un-serviced vehicles are located.¹³⁴

D. Swickard Dealerships

Swickard is owned by Jeff Swickard. Mr. Swickard, through various other entities, owns and operates nine dealerships, three of which are MB dealerships: Mercedes-Benz of Wilsonville (MB Wilsonville) in a suburb of Portland, Oregon; MB of Seattle, Washington; and MB of Atlanta South, Georgia.¹³⁵ Before becoming involved in car dealerships, Mr. Swickard worked in telecommunications and owned his own telecommunications company.¹³⁶ He lived in Austin from 2006 until 2011 or 2012.¹³⁷ After he sold his company, he purchased MB Wilsonville in 2014.¹³⁸

Mr. Swickard was nominated by other MB dealers to represent them on the MBUSA National Dealer Board in 2017 and has been elected by his national dealer peers to be the Chair of the Board.¹³⁹ Mr. Swickard has invested \$7 million in the South Austin property and estimates that he will spend \$12-15 million building an MB facility if the Application is approved.¹⁴⁰

Mr. Swickard's MB Wilsonville facility is, in MBUSA's view, above and beyond brand requirements in terms of high-end amenities, fixtures, and finishes.¹⁴¹ MBUSA's witness Mr. Andersen, a facilities project manager for MBUSA, testified that such a facility in

¹³³ Tr. at 79-81; 276-78; 501-02; Exs. I-37, I-65.

¹³⁴ Tr. at 873.

¹³⁵ Tr. at 25-26, 56.

¹³⁶ Tr. at 53.

¹³⁷ Tr. at 53.

¹³⁸ Tr. at 54.

¹³⁹ Tr. at 104-05, 286-88.

¹⁴⁰ Tr. at 82-84, 91-92.

¹⁴¹ Tr. at 679-80.

South Austin would improve the brand image of MB in the Austin AOR.¹⁴² Mr. Swickard's Wilsonville dealership turned the Portland metro market around from underperforming to number one in terms of registration effectiveness, exceeding sales performance expectations, and ranking 28th of 384 dealers on key metrics measured by MBUSA in its Dealer Performance Ranking.¹⁴³

Mr. Swickard testified that his MB dealerships focus on attracting entry-level customers in order to grow business and gain new customers.¹⁴⁴ He took efforts to make MB vehicles more affordable by selling cars that had been used as loaner vehicles and other nearly-new vehicles that can be sold for less than brand-new vehicles.¹⁴⁵ He stated that these sales also allowed his dealerships to grow their service departments, and that service is more profitable than sales of new cars.¹⁴⁶ Mr. Swickard hired the Ritz-Carlton Hotel Company to teach his employees about hospitality.¹⁴⁷ He testified that his goal is to take the pretension and judgment out of luxury car buying and to make it comfortable and achievable for everyone.¹⁴⁸

When MB Wilsonville began to get attention due to its good performance, Mr. Swickard began discussing opportunities to expand with MBUSA, and the opportunity to open the South Austin dealership arose.¹⁴⁹ He stated that he intends to be personally involved in the dealership and to spend as much time as he can in Austin.¹⁵⁰ The dealership will have air-conditioned service bays, but the dealership will not have a body shop.¹⁵¹ Mr. Swickard intends

¹⁴² Tr. at 679-80.

¹⁴³ Tr. at 61, 102-03, 284, 286-89; Exs. I-33, I-40.

¹⁴⁴ Tr. at 59.

¹⁴⁵ Tr. at 59-60.

¹⁴⁶ Tr. at 61-62.

¹⁴⁷ Tr. at 69.

¹⁴⁸ Tr. at 69.

¹⁴⁹ Tr. at 73.

¹⁵⁰ Tr. at 78.

¹⁵¹ Tr. at 90-91.

for the South Austin facility to be as well-designed as the competing BMW dealership located nearby.¹⁵²

IV. EXPERT OPINIONS

The parties retained several experts to opine on the performance of MB Austin and the anticipated impact of the new Austin point. Dr. Nivin, Ms. Heinemann, and Mr. Farhat testified for MBUSA and Swickard, and Mr. Stockton and Dr. Hatch testified for MB Austin. Their testimony is summarized below.

A. Opinions of Dr. Nivin

Dr. Nivin has a Ph.D. in economics, is an associate professor of economics and Chair of the Economics Department at St. Mary's University, and is an adjunct professor at the Southwest School of Art in San Antonio. He also has a consulting practice and runs the SABER Institute, a think tank at the university that focuses on regional economic issues.¹⁵³ He previously worked for two corporations as a political economist and was the Chief Economist for the city of San Antonio.¹⁵⁴ For this case, Dr. Nivin performed an assessment of the then-current state of the Austin economy and a projection/forecast of the economy for the next ten years, and he conducted an economic impact analysis of the proposed MB dealership.¹⁵⁵ Dr. Nivin's findings regarding the Austin economy are discussed in Section III.A., above.

Dr. Nivin examined how constructing and operating a new dealership would affect the local economy.¹⁵⁶ His analysis estimated the facility-construction project would generate 141 full-time employees whose wages and benefits would have a combined direct and indirect impact of

¹⁵² Tr. at 92.

¹⁵³ Tr. at 149.

¹⁵⁴ Tr. at 150.

¹⁵⁵ Tr. at 149, 157-58.

¹⁵⁶ Tr. at 152-54.

\$9.4 million in labor income and would add about \$12.9 million to the Austin gross regional product.¹⁵⁷ Construction would generate an additional \$2.4 million in tax and fee revenues to various federal, state, and local agencies.¹⁵⁸ Dr. Nivin also estimated that the dealership's operations (including the dealership and indirect businesses¹⁵⁹) will support 376 full-time equivalent positions, for earned income of \$21.6 million per year with an annual contribution to Austin's gross regional product of about \$66.4 million, and additional annual output to the local economy of about \$150.4 million.¹⁶⁰ Additionally, the dealership is expected to generate about \$30.9 million annual revenues to the government, including city, county, and federal government and local school districts.¹⁶¹

Dr. Nivin also opined on Austin's ability to recover from a recession. He found that during the 2008 recession, Austin's economy did not suffer as much as other major metro areas in Texas, and it demonstrated a strong recovery with sustained growth.¹⁶² In his opinion, the Austin economy has a strong ability to absorb and recover from a recession.¹⁶³ He noted that Austin also recovered quickly from the recession caused by the "dot-com bubble" in the early 2000s.¹⁶⁴ According to Dr. Nivin, the diversification of Austin's economy from 1990 through 2017 has helped to insulate it from recessions.¹⁶⁵ Dr. Nivin testified that Austin has the strongest economy in the state of Texas and one of the strongest economies in the country, and he believes it will continue as such.¹⁶⁶ Dr. Nivin testified that the projections suggest that Austin will continue to experience growth of

¹⁵⁷ Tr. at 192-94; Ex. I-71 at Table 11. The gross regional product refers to the gross domestic product for a regional economy. *See* Tr. at 193.

¹⁵⁸ Tr. at 193-94; Ex. I-71 at Table 12.

¹⁵⁹ Indirect businesses that Dr. Nivin projects will be impacted by the dealerships operations include restaurants, child care, hospitals, and truck transportation, among others. Ex. I-71 at 33, 36.

¹⁶⁰ Tr. at 195; Ex. I-71 at Table 15.

¹⁶¹ Tr. at 195; Ex. I-71 at Table 12.

¹⁶² Tr. at 167; Ex. I-71 at 18.

¹⁶³ Tr. at 168.

¹⁶⁴ Tr. at 170.

¹⁶⁵ Tr. at 175-76; Ex. I-71 at 20.

¹⁶⁶ Tr. at 182.

at least 3 percent per year for the next ten years.¹⁶⁷ His projections suggested that a recession was possible in 2020, and he testified that, based on historical patterns, Austin will experience a dip in growth, but less so than other city economies, and it should “bounce back strongly and continue on its path of leading the growth across the state.”¹⁶⁸ Dr. Nivin cited to the decision of the U.S. Military to bring its Cyber Command center to Austin, the creation of the University of Texas Medical School, and Apple’s expansion of 15,000 more jobs as examples of the growth and diversification of Austin’s economy that will support recovery from a future recession.¹⁶⁹ Dr. Nivin also opined that construction and operation of the dealership following a 2020 recession would be beneficial to the local economy.¹⁷⁰

B. Opinions of Mr. Farhat

Mr. Farhat is the Vice President of Expert Services at Urban Science Applications, Inc. (Urban Science), a large consulting and software company that serves, primarily, the automotive industry.¹⁷¹ He has been with the company since 1986.¹⁷² His company has done consulting work for most of the major automobile manufacturers in the world.¹⁷³ Mr. Farhat has conducted hundreds of dealer network analyses since joining Urban Science.

A dealer network analysis is an assessment of the number, location, and performance of dealerships in a market.¹⁷⁴ To perform a dealer network analysis, Mr. Farhat follows an eight-step methodology: (1) identify the areas to be analyzed; (2) develop a standard upon which dealer network performance and opportunity can be determined; (3) measure actual network

¹⁶⁷ Tr. at 183.

¹⁶⁸ Tr. at 183-84.

¹⁶⁹ Tr. at 184-85.

¹⁷⁰ Tr. at 196-97.

¹⁷¹ Tr. at 410-11.

¹⁷² Tr. at 412-14.

¹⁷³ Tr. at 413-14.

¹⁷⁴ Tr. at 414, 422; Ex. I-65 at 2.

performance; (4) determine the likely cause of any performance shortfalls; (5) identify and analyze proposed solutions to the problem; (6) assess the impact of the proposed solution on the consuming public, existing and proposed dealers, and the manufacturer; (7) confirm the conclusions with comparable market experiences; and (8) finalize conclusions.¹⁷⁵ His analyses are based on data such as actual retail vehicle registrations to specific households in every ZIP code, including the specific vehicle model and type and which dealer sold the vehicle; demographic data from the U.S. Census Bureau; labor statistics from the U.S. Bureau of Labor Statistics; and the dealer's own financial statements submitted to the manufacturer.¹⁷⁶ Mr. Farhat testified that Urban Science's methodology has been tested on historical data and has held up in the real world of automotive dealer networks.¹⁷⁷

Mr. Farhat was asked to assess the Austin metro market and evaluate whether MBUSA is adequately represented as to new vehicle sales in the Austin market. Mr. Farhat concluded, based on his analysis, that:

- MBUSA has not been adequately represented in the Austin AOR since at least 2014.
- The cause of the inadequate representation is the inadequate competition provided by the existing MB dealer network.
- The establishment of the proposed location in South Austin would increase exposure and access to MB products and services, thereby increasing both intra- and inter-brand competition. Making the marketplace more competitive by establishing the South Austin location is desirable because it will materially enhance the availability of stable, adequate, and reliable sales and service to actual and potential purchasers of MB products within the Austin AOR, and therefore be in the public interest.
- There is ample existing new MB sales opportunity available to MB Austin so it is unlikely it will be harmed by the establishment of the South Austin location. In addition to that available sales opportunity, MB Austin could also avoid any

¹⁷⁵ Tr. at 422-23; Ex. I-65 at 2-3.

¹⁷⁶ Tr. at 415-16; 426-28; Ex. I-65 at 19.

¹⁷⁷ Tr. at 424.

negative effect from the establishment of the South Austin location by responding positively to any enhanced competition.¹⁷⁸

Mr. Farhat found that Austin is a highly competitive market for luxury brand manufacturers and that other manufacturers were addressing growth in the market by adding dealer locations.¹⁷⁹ According to his analysis, at national registration levels, the expectation for MB in 2018 in the Austin AOR was 2,006 vehicle registrations. However, there were only 1,581, for a shortfall of 425 vehicles with a similar shortfall against the Texas benchmark of 300 vehicles.¹⁸⁰

Registration effectiveness is the actual number of MB vehicles registered in the AOR divided by the expected number, by segment. Registration effectiveness is a measure of the brand's performance that is an accepted standard throughout the automotive industry.¹⁸¹ Mr. Farhat found that MB's registration effectiveness in the Austin AOR was 78.8 percent against the segment-adjusted national market share and 84.1 percent against the Texas segment-adjusted benchmark.¹⁸² Achieving 100 percent registration effectiveness is considered average, so, according to Mr. Farhat, achieving less than 100 percent reflects inadequate representation of the MB brand. Mr. Farhat also found that MB Austin's sales effectiveness was 61.6 percent of the national benchmark in 2014 and 62.8 percent in 2018.¹⁸³ He also found that MB Austin's poorest performance is in the proposed South Austin AOI.¹⁸⁴

Mr. Farhat completed an "impact" analysis to determine the amount of sales opportunity in the Austin AOR. An impact analysis assesses where the new dealer's new vehicles sales would have come from if it had been in business in 2018.¹⁸⁵ Mr. Farhat looked at two sources of

¹⁷⁸ Ex. I-65 at 3.

¹⁷⁹ Tr. at 434-35.

¹⁸⁰ Tr. at 452-53; Ex. I-65 at 40-41.

¹⁸¹ Tr. at 1586-87.

¹⁸² Tr. at 453; Ex. I-65 at 8.

¹⁸³ Tr. at 472.

¹⁸⁴ Tr. at 469-70, 477.

¹⁸⁵ Tr. at 504; Ex. I-65.

opportunity: (1) losses to MB's competitors measured by gross registration loss (inter-brand competition) and (2) losses to MB dealers outside the AOR selling to residents of the AOR, or in-sell (intra-brand competition). Mr. Farhat calculated what the new dealer might have sold in the area around its location, based on the selling patterns of MB Austin and MB Georgetown in 2018, to compare to the total lost sales opportunity.¹⁸⁶ His analysis did not take into account any projected growth in the market; rather it captured a moment in time as of year-end 2018.¹⁸⁷

Mr. Farhat calculated gross registration loss by comparing the actual MB registrations in each ZIP code of the AOR to the expected registrations specific to that ZIP code at the national benchmark if the brand were achieving 100 percent registration effectiveness in that ZIP code, then adding up those individual deficiencies. These are sales that MB's competitors made to AOR residents that should have been, but were not, made by MB Austin or MB Georgetown; consequently, they are not sales that would be taken away from either existing dealer.¹⁸⁸ Under Mr. Farhat's methodology, in 2018, there were 474 units of gross registration loss.¹⁸⁹ In-sell is the total number of units sold by MB dealers outside the AOR to residents of the AOR; these are sales that neither MB Austin nor MB Georgetown made in 2018. In-sell totaled 281 units for a total lost opportunity of 755 sales in 2018.¹⁹⁰

According to Mr. Farhat, had the new dealer performed like MB Austin in the area around its dealership (its penetration profile),¹⁹¹ the South Austin dealership would have sold 697 new vehicles within 40 miles of its dealership location, a radius that covers almost the entirety of the population core of the Austin AOR.¹⁹² Had the new dealership performed like MB Georgetown, it

¹⁸⁶ Tr. at 504-08; Ex. I-65.

¹⁸⁷ Tr. at 504.

¹⁸⁸ Tr. at 505.

¹⁸⁹ Tr. at 505; Ex. I-65 at 96.

¹⁹⁰ Tr. at 504-06; 578-79; Ex. I-65 at 42, 97-98.

¹⁹¹ Ex. I-65 at 12, 86-90.

¹⁹² Tr. at 506-08; Ex. I-65 at 15, 98.

would have sold 525 new vehicles, and the range of likely sales would be about 500-700.¹⁹³ According to Mr. Farhat, because both of these scenarios are below the lost opportunity in the market of 755 units, there is no reason that Swickard could not have been in business in 2018 and not taken any sales from MB Austin and MB Georgetown.¹⁹⁴

Mr. Farhat tested his model against recent comparable experiences in which MBUSA added two dealers each in the Dallas and Houston AORs in the face of the opening or relocation of several competitive brand dealerships.¹⁹⁵ In both instances, after the additional dealers opened, the MB brand increased in registration effectiveness in the new dealers' AOIs or in the AOR overall, demonstrating that the MB brand was at least keeping up with the addition and relocation of its competitors. Although some of the closest existing dealers lost some sales, in Mr. Farhat's opinion, had MBUSA not added these dealers to Dallas and Houston, the existing dealers would have lost as much if not more sales to their competitors and lost the benefit of the enhanced exposure and brand awareness from the new dealerships throughout the markets.¹⁹⁶

Mr. Farhat also looked at the more recent comparable example in the Austin AOR of BMW's addition of a new dealership in South Austin in mid-2018. BMW's registration effectiveness in South Austin increased from 82 percent in 2017 to 102.1 percent by the end of 2018 and to 116.4 percent through May 2019.¹⁹⁷ In the rest of the Austin AOR (where the pre-existing BMW dealership is located), BMW's registration effectiveness rose from 90 percent in 2017 to 108 percent in 2018 and was still above national average at 102.2 percent through May 2019.¹⁹⁸ According to Mr. Farhat, these results support his conclusion that there is opportunity for the new Swickard dealership to capture new vehicle sales without taking any

¹⁹³ Tr. at 508-09, 576-77; Ex. I-65 at 15, 99.

¹⁹⁴ Tr. at 507.

¹⁹⁵ Tr. at 513-14; Ex. I-65 at 105-10.

¹⁹⁶ Tr. at 514-16; Ex. I-65 at 16, 109, 117.

¹⁹⁷ Tr. at 1610-11; Ex. I-67 at 14.

¹⁹⁸ Ex. I-67 at 15.

measurable sales from MB Austin.¹⁹⁹ Overall, Mr. Farhat concluded that MB Austin is in a good position geographically and financially to compete with the new dealership to its own and consumers' benefit.²⁰⁰

Further, Mr. Farhat evaluated how many dealerships MB would need to have the same share of competitive dealerships, or franchises, as it has in the average of all markets in a larger geographic area, or a "share of franchise" analysis.²⁰¹ According to his analysis, MB should have three dealerships in Austin.²⁰² He further found that as MB's percent share of all competitors' franchises increases in an AOR, its registration effectiveness increases in a highly statistically significant way.²⁰³

Mr. Farhat also evaluated whether the proposed location for the Swickard dealership is reasonable to address the adequate representation of the MB brand in Austin. He used the Urban Science Optimal Location methodology.²⁰⁴ The location his analysis arrived at is in South Austin, to the northwest of the proposed location in a largely residential area.²⁰⁵ However, zoning restrictions in that area preclude a dealership.²⁰⁶

Mr. Farhat was asked about the concerns expressed by MB Austin witnesses that the dealer was unable to receive parts for vehicles or that certain models were not available to sell to customers. He reiterated that registration effectiveness adjusts for product availability, reputation, and the quality of the vehicles sold by a particular brand.²⁰⁷ In other words, the concerns

¹⁹⁹ Tr. at 1082-84.

²⁰⁰ Tr. at 517-20.

²⁰¹ Tr. at 478.

²⁰² Tr. at 478-80; Ex. I-65 at 57.

²⁰³ Tr. at 480-82; Ex. I-65 at 58.

²⁰⁴ Tr. at 500-01.

²⁰⁵ Tr. at 501-02; Ex. I-65 at 14, 93.

²⁰⁶ Tr. at 275-76.

²⁰⁷ Tr. at 1588.

MB Austin expressed as to the quality or availability of the products being produced by MBUSA would be experienced by all MB dealers, not just by MB Austin.

With respect to Dr. Hatch's analysis, Mr. Farhat argued that Dr. Hatch's method of assessing untapped sales opportunity significantly understates the real-world market results. In response to Dr. Hatch's critique of Mr. Farhat's gross registration loss analysis and conclusion that there was additional MB opportunity available in Austin, Mr. Farhat pointed out that his analysis showed the gross registration loss in Austin was 474 units at national average in 2018. Dr. Hatch instead used net registration loss, which resulted in 422 units for 2018. Net loss reduces the gross loss by offsetting the areas of below-average performance with areas of above-average performance. Mr. Farhat contended there was no basis for Dr. Hatch to assume that above-average areas would decline after an increase in brand competition and representation. By netting the areas of gain with the areas of loss, he said, Dr. Hatch made it impossible to determine the level of underperformance in the market.²⁰⁸

Mr. Farhat also opined that Dr. Hatch's methodology significantly underestimated the opportunity available to the brand after introduction of an additional dealer, which consequently overstated any negative impact on the existing, or incumbent, dealers. Mr. Farhat tested Dr. Hatch's methodology by assessing the after-the-fact results of the additional BMW dealer in South Austin.²⁰⁹ Using Dr. Hatch's methodology, BMW's predicted performance was significantly less than the actual results for the BMW addition in South Austin. Mr. Farhat concluded that Dr. Hatch's methodology understated the additional sales opportunity within the Austin AOR by 248 units in 2018, and 259 units through May 2019 annualized.²¹⁰ BMW sales, he said, not only increased in the South Austin area, they increased throughout the Austin AOR.²¹¹ BMW had historically sold fewer vehicles in the Austin AOR until 2018. Beginning in 2018 with

²⁰⁸ Ex. I-67 at 2.

²⁰⁹ Tr. at 1608.

²¹⁰ Ex. I-67 at 3; Tr. at 1610-11.

²¹¹ Tr. at 1612.

the additional South Austin dealer, BMW sold more vehicles in the Austin AOR than MB, and this trend continued into 2019.²¹²

Mr. Farhat also believed that Dr. Hatch's claimed impact on MB Austin was analytically inconsistent and exaggerated. This occurred because Dr. Hatch, while criticizing Mr. Farhat's sales projection as significantly overstated, did not himself provide an alternative reduced-sales projection. Further, Dr. Hatch adopted an "overstated" sales projection while reducing by 60 percent the additional opportunity available. This, said Mr. Farhat, resulted in an exaggerated claim of negative impact on MB Austin.²¹³

Finally, Mr. Farhat said Dr. Hatch's report contained additional incorrect claims. One claim Mr. Farhat took issue with was the implication in Dr. Hatch's report that MB performance declines in higher-income areas due to the presence of other high-end luxury brands like Porsche and Ferrari.²¹⁴ This was contrary to Mr. Stockton's report that stated that demographic variation did not affect MB market share in Texas, and Mr. Farhat surmised that this misstatement by Dr. Hatch was due to Dr. Hatch's lack of experience and knowledge with actual consumer purchase behavior in the automotive industry.²¹⁵ Second, Mr. Farhat noted that Dr. Hatch incorrectly implied that MB losses in the Austin Metro in 2018 were atypically high. According to Mr. Farhat, Dr. Hatch did not acknowledge the effect of the addition of the new BMW dealer in South Austin in 2018. As BMW brand performance increased with the additional dealer, MB brand performance decreased. This, he said, would not be surprising to those familiar with automotive dealer network analysis.²¹⁶ Finally, Mr. Farhat denied that his analysis contained a calculation error, as claimed by Dr. Hatch. The difference in the calculation of the individual AOIs was a result of rounding, and not a calculation error.²¹⁷

²¹² Tr. at 1614.

²¹³ Tr. at 1614-15; Ex. I-67 at 4.

²¹⁴ Tr. at 1615-16.

²¹⁵ Ex. I-67 at 4.

²¹⁶ Tr. at 1596; Ex. I-67 at 5.

²¹⁷ Tr. at 1616; Ex. I-67 at 5.

Mr. Farhat contended that Mr. Stockton's proximity-based impact analysis predetermines negative impact on existing dealers. He believed that Mr. Stockton's analyses do not reflect real-world results because Mr. Stockton incorrectly assumed that MB sales would not increase with the addition of the South Austin dealer.²¹⁸ Mr. Farhat also disagreed with Mr. Stockton's projected sales gain of 242 units over two years for the additional South Austin dealer. Using Texas data, Mr. Farhat posited that an additional Austin MB dealer would get the Austin AOR to the national average, which is more than the 242 units resulting from Mr. Stockton's analysis.²¹⁹

Mr. Farhat also assessed Mr. Stockton's case studies. Based on his analysis, Mr. Farhat contended that with increased representation in the Austin AOR, the overall "pie" would get bigger. Mr. Stockton's analysis, however, was based on what Mr. Farhat termed a "fixed pie" analysis.²²⁰ Mr. Farhat agreed that some markets did not increase in Mr. Stockton's analysis, but he believed that was because those particular markets represented "satellite" locations for the existing, or incumbent, dealer. When satellite locations occur, there is less competition introduced into the market because the locations are owned by the same entity. This produces less aggressive intra-brand and inter-brand competition, he said, while the market may still grow.²²¹

According to Mr. Farhat, Mr. Stockton's proximity analysis confirmed that MB Austin has sufficient opportunity to maintain its sales volume after the addition of the South Austin dealer.²²² Mr. Farhat stated that Mr. Stockton's analysis resulted in 3,602 potential new vehicle sales for the two-year period 2017-18, while in reality MB Austin sold only 1,879 new vehicles in that same time period. After the add-point in South Austin, Mr. Stockton's analysis resulted in 2,026 potential new vehicle sales for MB Austin, which is still greater than the 1,879 actual new vehicle sales. The results for sales of used vehicles was even more dramatic, he said. MB Austin sold 2,716

²¹⁸ Ex. I-67 at 7.

²¹⁹ Tr. at 1621.

²²⁰ Tr. at 1623.

²²¹ Tr. at 1624-25.

²²² Tr. at 1626; Ex. I-67 at 8.

used vehicles in 2017-18, but Mr. Stockton's analysis resulted in 6,686 potential sales of used vehicles before the add-point, and 4,315 potential sales after the add-point.²²³ These results confirmed that Mr. Stockton's impact analysis meant there was still opportunity in the Austin market for MB Austin after the addition of the South Austin dealership.

Mr. Farhat also disagreed with Mr. Stockton's claims that decreases in MB Austin's new-vehicle sales would result in decreases in other departments at MB Austin and a decrease in MB Austin's net profit. The departments within a dealership are run as independent departments that could respond to increased competition. In other words, if new vehicle sales went down, service or used vehicle sales could go up, for example.²²⁴

Finally, Mr. Farhat stated that Mr. Stockton was misguided for focusing on a potential downturn in the market for automotive sales because the addition of a new dealer is a very long-term decision. In fact, Mr. Farhat noted that national vehicle sales have been cyclical, but increasing in the long-term. Because it takes a long time to implement the establishment of a new dealer, Mr. Farhat stated that it would be beneficial if the implementation could be timed during an economic downturn. Certainly, he said, the local economy would benefit from the investment and additional jobs.²²⁵

C. Opinions of Ms. Heinemann

Ms. Heinemann is a certified public accountant specializing in forensic accounting and economic damages in the context of commercial litigation cases, and she is accredited in business valuation. She analyzed MB Austin's financial statements and compared them to composites of specific groups of other MB dealers and those of the National Automobile Dealers Association's luxury dealers to evaluate MB Austin's operations, both generally and by department.²²⁶

²²³ Tr. at 1626-28.

²²⁴ Tr. at 1629-31.

²²⁵ Tr. at 1632-35; Ex. I-67 at 10-11.

²²⁶ Tr. at 691-92, 694, 717-21, 723-27; Ex. I-69 at 48, 51, 58, 64.

Ms. Heinemann also reviewed the financial information of MB Austin's affiliate entities, including a body shop, a wholesale parts business,²²⁷ an automotive financing company, a dealership operation entity, a leasing company,²²⁸ and an entity that owns the land and property where the dealership is located.²²⁹ Ms. Heinemann assessed past lost profits and likely future profitability to determine how a dealership would be impacted after a change in market conditions such as the establishment of a new dealership.²³⁰

Ms. Heinemann found that MB Austin has been very profitable since at least 2014, with net profit ranging from over \$4 million in 2014 to over \$5.6 million in 2018.²³¹ Except in 2014, MB Austin's net profit has increasingly exceeded all three benchmark composite groups.²³² As of its 2018 balance sheet, MB Austin had no long-term debt, which allows it to be more flexible with its cash flow and decision-making in how it will spend the money coming in, unlike if it had to use its cash to pay down debts every month.²³³ MB Austin had a cash position of \$4.6 million, a net cash position of nearly 600 percent, and working capital of 200 percent of what MBUSA requires for a healthy dealership.²³⁴ MB Austin's net profit for the year exceeded its total net fixed assets after depreciation (\$5.6 million versus a little under \$4 million), indicating financial health.²³⁵ MB Austin's return on equity (or the amount that its current year's profit exceeds the owners' equity, or their investment, in the dealership) is very high, and, with the exception of 2014,

²²⁷ Ms. Heinemann testified that the affiliated wholesale parts company, Wholesale Parts Direct, existed through at least 2017, after which a reorganization of the various entities occurred and the Wholesale Parts Direct expenses were moved to the dealer financial statements. She testified that she could not determine how much of the expense from Wholesale Parts Direct is allocated to MB Austin. Tr. at 786-90. However, she also stated that the status of Wholesale Parts Direct did not matter to her analysis because the expenses being allocated to it were included in the dealer financial statements. Tr. at 829.

²²⁸ Ms. Heinemann testified that the leasing company no longer exists. Tr. at 773.

²²⁹ Tr. at 714-15.

²³⁰ Tr. at 700-01.

²³¹ Tr. at 730; Exs. I-14 at 1, I-69 at 51.

²³² Tr. at 739-42, 746-47; Ex. I-69 at 74-75.

²³³ Tr. at 730-33; Ex. I-14 at 1.

²³⁴ Tr. at 734; Ex. I-14 at 1.

²³⁵ Tr. at 734-35; Exs. I-14 at 1, I-69 at 57.

exceeds the average return on equity of the composite groups.²³⁶ MB Austin made \$5.6 million in profit in 2018 compared to \$4.7 million in 2017, even though it sold approximately 16 percent fewer new vehicles in 2018.²³⁷ According to Ms. Heinemann, the dealership's increased profitability is largely due to MB Austin's shifts in operational focus within its separate departments.²³⁸ MB Austin generates a substantially higher amount of total revenues in its fixed operations (service, parts, and body shop departments) relative to the benchmark groups.²³⁹ The gross profit margins dealers typically make, industry-wide, on fixed operations is much higher than in the new or used departments (about \$70 per \$100 in revenues in the service department, \$30 per \$100 in the parts department, and \$40-\$50 per \$100 in the body shop in versus \$6-\$10 per \$100 in the new vehicle department), and MB Austin's gross profit margins are increasingly higher over time.²⁴⁰ Further, MB Austin's net profit in its fixed operations (revenues minus all variable and semi-variable expenses) exceeds all of its fixed expenses (rent, utilities, overhead) by 1.72 times, more than any of the composite groups.²⁴¹ Therefore, MB Austin does not need to generate profits in those departments to cover any of the dealership's fixed expenses.²⁴² Ms. Heinemann also testified that fixed operations are more recession-proof than sales because consumers may delay purchasing new cars but are more likely to continuing servicing their old cars.²⁴³

Ms. Heinemann explained that when a car dealership acquires new vehicles, the vehicles are financed through what are referred to as floorplan financings, which are standard in the

²³⁶ Tr. at 747-50; Ex. I-69 at 77.

²³⁷ Tr. at 750-51; Ex. I-69 at 74.

²³⁸ Tr. at 751-52.

²³⁹ Tr. at 752-56; Ex. I-69 at 88.

²⁴⁰ Tr. at 756-61, 818-19; Ex. I-69 at 90-92, 96.

²⁴¹ Tr. at 761-65; Ex. I-69 at 100.

²⁴² Tr. at 763-65.

²⁴³ Tr. at 761.

industry.²⁴⁴ As of 2018, MBUSA's total inventories, including new cars and parts inventory, was \$30 million.²⁴⁵

MB Austin also has a large used/pre-owned department with higher margins (gross profit per unit sold) than the benchmark groups. It has an increasing, continued growth trend from 2014, when it was selling one used vehicle for every new vehicle sold, to 2018, when it sold 1.7 used vehicles for every new vehicle sold.²⁴⁶ As the number of new units sold by MB Austin has declined, MB Austin has increased both the volume of used vehicle sales and the profitability per unit in that department, and MB Austin's used vehicle department is more profitable than its new vehicle department.²⁴⁷

MB Austin has historically made more money, and charged more for new vehicles, than its peers on an average gross profit per unit basis.²⁴⁸ However, in 2018, MB Austin made a much higher profit on the finance, insurance, and service contract products it sold with its new car sales than in the past, which allowed its overall gross profits in the new vehicle departments to increase substantially.²⁴⁹ Additionally, MB Austin's sales of used cars continued to grow in 2018.²⁵⁰ MB Austin is still charging more than the benchmark groups for the new vehicles it sells, which partly explains how it could sell fewer new vehicles in 2018 but maintain approximately the same profitability in the new vehicle department.²⁵¹ According to Ms. Heinemann's analysis, even assuming that MB Austin loses new vehicle sales to the new dealer, it is well-positioned to leverage its performance in other departments to maintain its higher-than-average overall profitability.²⁵²

²⁴⁴ Tr. at 733.

²⁴⁵ Tr. at 733.

²⁴⁶ Tr. at 753, 765-69, 819-20; Ex. I-69 at 86-87.

²⁴⁷ Tr. at 753, 765-69, 819; Ex. I-69 at 86-87.

²⁴⁸ Tr. at 770-72; Ex. I-69 at 80-81.

²⁴⁹ Tr. at 753-54, 769-70, 772; Ex. I-69 at 80-83.

²⁵⁰ Tr. at 752; Ex. I-69 at 74.

²⁵¹ Tr. at 774-75.

²⁵² Tr. at 776.

According to Ms. Heinemann, MB Austin's financial position and operations put it in a better position to compete on price with a new dealer; it can lower its margins to compete on more flexible pricing and grow the volume of new vehicle sales.²⁵³ She further stated that MB Austin is in a good position to respond to competition by virtue of the flexibility of its balance sheet, the returns on its investments, and the diversification of the types of profits it generates.²⁵⁴

Ms. Heinemann was also asked to respond to Mr. Stockton's calculations of the profits that would potentially be lost by MB Austin.²⁵⁵ In reviewing Mr. Stockton's report, she took the losses that he computed as given and based her calculations on the hypothetical situation in which those losses would occur.²⁵⁶ She stated that Mr. Stockton's opinion of \$2.0 to \$2.5 million in loss was not supported in his report by specific figures and calculations.²⁵⁷ She disagreed with his method for determining which costs are incremental.²⁵⁸ He assumed that 25 percent of the semi-variable expenses were able to be changed if a change in sales occurred; he arrived at 25 percent by rounding up the elasticity of 12.4 percent he calculated through regression analyses.²⁵⁹ Ms. Heinemann did not agree with rounding 12.4 up to 25, and she found that the regression analysis that yielded 12.4 percent elasticity was not statistically significant.²⁶⁰ She found that, in Mr. Stockton's regression analysis, units (vehicles) did not predict expenses in the new vehicle department, and his 25 percent estimate was "completely utter speculation."²⁶¹ According to Ms. Heineman, by using 25 percent of semi-variable expenses as part of his incremental profit calculation, Mr. Stockton over-inflated profits.²⁶² Over-inflating profits, she testified, will in turn

²⁵³ Tr. at 775-76.

²⁵⁴ Tr. at 776.

²⁵⁵ Tr. at 1702; Ex. I-70.

²⁵⁶ Tr. at 1706.

²⁵⁷ Tr. at 1708.

²⁵⁸ Tr. at 1713.

²⁵⁹ Tr. at 1727; Ex. P-1 at 75, 244.

²⁶⁰ Tr. at 1728-29.

²⁶¹ Tr. at 1730.

²⁶² Tr. at 1732.

overestimate losses.²⁶³ She further stated that Mr. Stockton's report included a separate analysis of incremental profit of new vehicle sales that did have a statistically significant outcome; however, the result of that analysis was \$3,406 profit contribution per new vehicle sold versus \$5,661 in his not-statistically-significant calculation.²⁶⁴ In Ms. Heinemann's opinion, Mr. Stockton should have calculated loss using the \$3,406 profit contribution rather than \$5,661; however, his report did not further address the \$3,406 profit contribution result.²⁶⁵ Ms. Heinemann performed regression analyses of incremental profits for each year from 2012-2018 and arrived at figures ranging from \$2,580-\$3,636, which was more closely aligned with Mr. Stockton's unused \$3,406 result.²⁶⁶

Ms. Heinemann testified that Mr. Stockton's analyses for the used vehicle department similarly showed that units are not a strong predictor of profits, although they showed statistical significance.²⁶⁷ Ms. Heinemann's calculations were highly statistically significant (with an R-squared over .90).²⁶⁸ Assuming the new dealership existed in 2018 and assuming all of the unit losses projected by Mr. Stockton actually happened in 2018, MB Austin would have continued to profit by \$3.8 to \$4.1 million, continued to be a very profitable dealership, and continued to perform well compared to the composite groups.²⁶⁹ Ms. Heinemann's estimates based on the percentage of loss projected by Mr. Stockton yielded lost profits from \$1,248,064 to \$1,587,436.²⁷⁰ Ms. Heinemann also testified that, in her opinion, Mr. Stockton's projected losses for the used vehicle department were over-inflated because he assumed a loss of 70 used vehicles would occur from a failure to get trade-ins from customers purchasing new vehicles.²⁷¹ She testified that

²⁶³ Tr. at 1733.

²⁶⁴ Tr. at 1735-36; Ex. P-1 at 75, 267.

²⁶⁵ Tr. at 1736.

²⁶⁶ Tr. at 1743-44, 1751-52; Ex. I-70 at 52, 55.

²⁶⁷ Tr. at 1753.

²⁶⁸ Tr. at 1756; Ex. I-70 at 58,

²⁶⁹ Tr. at 1764-65; Ex. I-70 at 72-76.

²⁷⁰ Tr. at 1768; Ex. I-70 at 50.

²⁷¹ Tr. at 1768-69.

MB Austin gets approximately 60 percent of their supply of used vehicles from other sources such as the wholesale market and auctions.²⁷² Ms. Heinemann did not believe MB Austin would suffer any losses in the pre-owned department and stated that she found no evidence for such losses.²⁷³

Ms. Heinemann testified that she observed excess compensation and expenses in the new and used vehicles department of MB Austin.²⁷⁴ She stated that gross profits in the service department were higher than the benchmark group, but she could not determine whether that was due to charging more for service work or paying service technicians less.²⁷⁵ She further found that in 2018, \$84,021 was paid to owners of MB Austin, with another \$99,000 of supplemental payment to Mr. Hardeman.²⁷⁶ Distributions of \$180,000 were made to each of Mr. Hardeman's three children in 2018 as well.²⁷⁷

D. Opinions of Mr. Stockton

Mr. Stockton is the vice-president of the Fontana Group, a management and economic consulting company located in Tucson, Arizona. He specializes in applied econometrics, which is the use of statistics applied to economic data. Mr. Stockton was asked to assess the adequacy of MB representation in the Austin marketplace, the marketplace for new vehicles in Austin and the surrounding areas, and assess any potential harm to MB Austin if the new South Austin dealership were to be added. Finally, Mr. Stockton was asked to review the expert reports and rebuttal reports of Mr. Farhat and Ms. Heinemann. Mr. Stockton prepared a report, which was admitted into evidence.²⁷⁸

²⁷² Tr. at 1768-69.

²⁷³ Tr. at 1770.

²⁷⁴ Tr. at 1703; Ex. I-70 at 83.

²⁷⁵ Tr. at 1706.

²⁷⁶ Tr. at 1718-19; Ex. I-14 at 2.

²⁷⁷ Tr. at 1719.

²⁷⁸ Ex. P-1.

According to Mr. Stockton, when a dealership point is added, a manufacturer generally benefits because more cars are being bought by dealers from the manufacturer. It is also the case, he said, that the profits of the incumbent dealers are expected to and generally do decline.²⁷⁹ Specifically, Mr. Stockton testified that the add-point in South Austin would negatively impact MB Austin in two ways: the lost sales and the lost benefits to territory to MB Austin will strongly outweigh the offset in gains in brand expansion; and the models that support the higher impact to MB Austin are, in his opinion, much more empirically sound than those models that suggest a net benefit to the market from the add-point.²⁸⁰

Mr. Stockton testified that he assessed whether MB was adequately represented in the Austin AOR by determining whether the MB registrations in the Austin AOR were, in his terms, “normal.”²⁸¹ The registration numbers were “normal,” he said, because the number of MB vehicles registered in the Austin AOR in 2017 and 2018 were almost exactly lined up with other Texas markets. Because there was no shortfall in registrations for these years in the Austin market, he believed the current dealer network in the Austin AOR was not causing any shortfalls in registration to MB.²⁸² Based on his evaluation, Mr. Stockton estimated that had a third Austin dealership existed in 2017 and 2018, approximately 242 incremental MB registrations would have occurred in the Austin AOR. These registrations would be conquests from inter-brand competitors. However, during that same time period, MB Austin would have lost new car registrations.²⁸³

Mr. Stockton stated he was not clear about the principle behind Mr. Farhat’s lost opportunity analysis, even though he had admittedly seen the analysis “dozens of times.”²⁸⁴ According to Mr. Stockton, Mr. Farhat’s analysis entailed using ZIP codes and comparing the registrations in the ZIP codes compared to an average expectation of the market. If the actual

²⁷⁹ Tr. at 925.

²⁸⁰ Tr. at 926.

²⁸¹ Tr. at 928.

²⁸² Tr. at 929-30.

²⁸³ Tr. at 931-33.

²⁸⁴ Tr. at 934.

number of registrations in a ZIP code were less than expected for the market, there is a deficit, which is added to all the other deficits by ZIP code. If the actual number of registrations is equal to or greater than expected, that result is ignored by Mr. Farhat, Mr. Stockton said. Then Mr. Farhat would look at the number of MB registrations in the market that dealers from outside the market sold into the market (the “in-sell”). The shortfalls calculated by ZIP code (also called “gross loss”) would then be added to the sum of the in-sell to equal Mr. Farhat’s lost opportunity.²⁸⁵

In Mr. Stockton’s opinion, the amount of gross loss and in-sell in a market (Mr. Farhat’s lost opportunity) did not correlate with inadequacy of the dealer market, and was also not an achievable opportunity that could be captured by an increased network of intra-brand competitors. Mr. Stockton believed that the benchmark selection process was fundamentally unscientific. As a result, any result that flowed from that process would also be unscientific.²⁸⁶ Mr. Stockton contends that under Mr. Farhat’s analysis, MB, Audi, BMW, and Lexus could all show gross loss in the Austin AOR regardless of who is achieving whatever benchmarks they may have from their respective manufacturers.²⁸⁷

Mr. Stockton also testified that he believed Mr. Farhat was internally inconsistent in his report with respect to in-sell because he uses other brands’ in-sell in his analysis to determine how much dealers in that market should sell into the same market.²⁸⁸ Instead, Mr. Stockton opined that the analysis should determine what in-sell would look like in the ordinary course of business.

Mr. Stockton stated he utilized a standard to assess the Austin market for MB, but that he did not use national registration effectiveness as a benchmark to assess the Austin market because he believed that would involve subjectivity. If he were to pick national registration effectiveness as a benchmark, Mr. Stockton stated he would apply statistical tests to validate his use of that

²⁸⁵ Tr. at 934.

²⁸⁶ Tr. at 940.

²⁸⁷ Tr. at 939.

²⁸⁸ Tr. at 943.

benchmark.²⁸⁹ As an example, Mr. Stockton noted that had he just used the Southern Region states as the benchmark that would have resulted in 4,785 Mercedes registrations in the Austin AOR in 2017-2018.²⁹⁰ In fact, however, in those years there were 4,711 actual Mercedes registrations in the Austin AOR. Using his regression analysis for 2017-18 resulted in 4,669 registrations. This showed, he said, that using his regression analysis resulted in a more reliable analysis because the actual number of registrations was very close to the number he posited from his regression analysis.²⁹¹

Mr. Stockton also used a gravity model to assess the Austin market.²⁹² Mr. Stockton thought the model was highly statistically significant because the R-squared was very high, which meant the gravity model was useful in showing what the sales of MB Austin were. He used the gravity model to calculate a likely percentage of sales loss by MB Austin if a new South Austin dealer was established. According to his calculations, MB Austin's share of the new sales in the market would be 60 percent of what it was in 2017 and 2018 if the South Austin dealer had been in business.²⁹³

Mr. Stockton also testified regarding a profit contribution analysis he calculated for the departments within MB Austin.²⁹⁴ His calculations showed that, exclusive of fixed expenses and inclusive of semi-fixed expenses, the profit contribution per new and used vehicle sold or leased was \$5,661 and \$2,375, respectively. Per \$1,000 dollars of service sales and parts sales, the contribution was \$280 and \$170, respectively.²⁹⁵ The total profit contribution per department was

²⁸⁹ Tr. at 946.

²⁹⁰ This number of registrations of 4785 was an "aspirational number" based on the market share MB captures in the Southern Region in each product segment. The market share was then applied to actual registrations in the Austin AOR and compared on a segment-by-segment basis to determine the number of registrations that would occur in the Austin AOR if MB's performance in the Austin AOR was exactly like its performance in the Southern Region. Tr. at 949.

²⁹¹ Tr. at 948-50.

²⁹² Tr. at 983.

²⁹³ Tr. at 984.

²⁹⁴ Tr. at 986.

²⁹⁵ Ex. P-1 at 75; Tr. at 992.

exposed to the potential new dealership and represented the potential impact on MB Austin, he said.²⁹⁶ In terms of market expansion from the new dealership, if the market expanded five or six percent, and MB Austin was predicted to lose approximately 39 percent, then he concluded that MB Austin would lose about 36 percent of the calculated profit contribution.²⁹⁷ For the new car sales department, Mr. Stockton expected losses of between \$1 and \$1.5 million. For the used vehicle department, he expected losses of approximately \$200,000. The parts and service departments would lose approximately \$750,000.²⁹⁸

On cross-examination, Mr. Stockton agreed that an additional dealership would offer additional choice and increased proximity to consumers, particularly those who live in South Austin. The additional dealership would also introduce the potential for increased price competition. And he agreed that MB Austin was financially stable and has experienced rapidly increasing profitability. MB Austin sells more used cars than new cars, which Mr. Stockton agreed was a successful business strategy for MB Austin.²⁹⁹ In fact, MB Austin was probably doing better in the pre-owned department than other dealers in Texas. He testified that MB Austin was also doing better in its fixed operations—parts and service—than would be implied through his regression-based proximity advantage.³⁰⁰ Given the construction of the new facility, which includes more service bays, Mr. Stockton expected MB Austin’s service department to be even more profitable. Mr. Stockton also conceded that having a new MB dealer in South Austin might alter the competition between MB and BMW, which BMW was currently “winning” by outpacing MB in registrations in South Austin. He further agreed that the third MB dealer would increase MB’s market share in the Austin area.³⁰¹

²⁹⁶ Tr. at 992.

²⁹⁷ Tr. at 994.

²⁹⁸ Tr. at 1004.

²⁹⁹ Tr. at 1018.

³⁰⁰ Tr. at 1019.

³⁰¹ Tr. at 1028.

Mr. Stockton conceded that in his analysis he rounded up elasticity of 0.1237 for the variable portion of the semi-variable expenses for new vehicles to .25 because, by convention, he does not use semi-variable ratios of less than 25 percent.³⁰² He did not explain this rounding in the narrative of his report.³⁰³ He also conceded on cross-examination that the regression analysis from which he drew the elasticity of 0.1237 was not statistically significant.³⁰⁴ The expense elasticity Mr. Stockton calculated for the semi-variable expenses for parts and service was 147 percent, but he used 50 percent in his analysis.³⁰⁵ Although in his report, he had stated that the additional dealer would likely have cannibalized in excess of 20 percent, and possibly as high as 30 percent, of MB Austin's new vehicle profit contribution based on 2017-18 conditions, he conceded that he did not provide a schedule or discussion in his report supporting this conclusion.³⁰⁶ Many of the numbers in his report were not explained or backed up by schedules or tabulations.³⁰⁷

E. Opinions of Dr. Hatch

Dr. Hatch is a director at Applied Economics Consulting Group.³⁰⁸ Dr. Hatch focuses on patent infringement and trade secrets disputes.³⁰⁹ The purpose of Dr. Hatch's testimony was to assess Mr. Farhat's impact analysis and offer his opinions with respect to gross loss and in-sells.³¹⁰ This case was Dr. Hatch's first analysis of the economic impact of adding a car dealership to a manufacturer's dealer network.³¹¹

³⁰² Tr. at 1039; Ex. P-1 at 75, 244.

³⁰³ Tr. at 1040.

³⁰⁴ Tr. at 1041-42.

³⁰⁵ Tr. at 1048; Ex. P-1 at 253.

³⁰⁶ Tr. at 1050; Ex. P-1 at 16.

³⁰⁷ Tr. at 1050-54, 1056.

³⁰⁸ Tr. at 1114; Ex. P-60.

³⁰⁹ Tr. at 1115.

³¹⁰ Tr. at 1116.

³¹¹ Tr. at 1121.

Dr. Hatch concluded that the methodology used by Mr. Farhat was unreliable in terms of his measurement of gross loss and his analysis of the in-sells that represent opportunity in the market for MB dealers within the AOR.³¹² He further opined that Mr. Farhat conducted no analysis on in-sell and merely quoted the number of in-sells in the market for 2018, which was 281, and added that to his impact analysis number.³¹³ According to Dr. Hatch, Mr. Farhat posits that it is feasible for MB to eliminate in-sells entirely.³¹⁴

Dr. Hatch disagreed with Mr. Farhat's method of dividing the Austin AOR by ZIP code, stating that by considering the national vehicle registration benchmark to be the standard for each ZIP code submarket, Mr. Farhat could have artificially created gross loss.³¹⁵ According to Dr. Hatch, variation across ZIP codes should be expected based on where MB dealers are relative to their competitors, and that variation will produce gross loss or increase gross loss each time the market is subdivided.³¹⁶ In Dr. Hatch's opinion, the average of 70 registrations per ZIP code was not a large enough sample "to get an actual result that's even remotely close to the expected result in every single instance where you're measuring it."³¹⁷ For this reason, Dr. Hatch also opined that using a benchmark drawn from a larger market cannot reliably measure performance in submarkets the size of ZIP codes.³¹⁸ He testified that Mr. Farhat should have analyzed whether the range of market shares within the Austin AOR is out of line with the range seen nationally.³¹⁹ Dr. Hatch opined that Mr. Farhat's methodology would inflate gross loss even more at the neighborhood level.³²⁰ Dr. Hatch believes Mr. Farhat's gross loss estimate overstated the available untapped

³¹² Tr. at 1123.

³¹³ Tr. at 1124.

³¹⁴ Tr. at 1124.

³¹⁵ Tr. at 1127-29.

³¹⁶ Tr. at 1133-34.

³¹⁷ Tr. at 1135.

³¹⁸ Tr. at 1135.

³¹⁹ Tr. at 1136.

³²⁰ Tr. at 1148-49.

market potential in the Austin AOR.³²¹ He stated that Mr. Farhat's methodology does not account for factors such as location of existing dealers or personal relationships that lead to sales.³²² He also stated that there is no economic or statistical rationale for using ZIP codes to subdivide the market for purposes of calculating gross loss.³²³ He stated that Mr. Farhat should compare the entire Austin AOR to his chosen benchmark, rather than dividing it into smaller subsections.³²⁴ Further, Dr. Hatch testified that Mr. Farhat's analysis did not account for locational factors such as proximity of other luxury dealers.³²⁵ According to Dr. Hatch, Mr. Farhat's gross loss calculation would not be altered by putting a new dealership right next to an existing one.³²⁶

Dr. Hatch testified that the addition of the new dealership would not capture most of the sales made by competing brands in Austin because it would not be increasing convenience to many of the ZIP codes.³²⁷ He further stated that net loss is more reasonable than gross loss in estimating lost opportunity.³²⁸ In his opinion, gross loss lends itself to inflating underperformance whereas net loss suggests actual underperformance.³²⁹ However, he also stated that using net loss can overstate lost opportunity.³³⁰ Moreover, he stated that the large net loss in 2018 was in the MB Austin AOI; specifically, the Georgetown AOI had 78 in net loss, the proposed South Austin AOI had 141 in net loss, and the MB Austin AOI had 203 in net loss.³³¹

³²¹ Tr. at 1136.

³²² Tr. at 1137-38.

³²³ Tr. at 1148-50.

³²⁴ Tr. at 1151; Ex. P-7 at 6.

³²⁵ Tr. at 1195.

³²⁶ Tr. at 1140.

³²⁷ Tr. at 1144-45.

³²⁸ Tr. at 1182-83; Ex. P-7 at 11.

³²⁹ Tr. at 1183.

³³⁰ Tr. at 1183-84; Ex. P-7 at 11.

³³¹ Tr. at 1185; Ex. P-7 at 12.

Dr. Hatch calculated competition faced by MB Austin by adding up the percentage of market share captured by other luxury dealers such as Audi, Acura, and BMW in the area surrounding MB Austin.³³² He did the same for MB Georgetown and the proposed South Austin dealership. According to Dr. Hatch, MB Austin faces significantly higher competition from other luxury brands than both MB Georgetown and the proposed South Austin dealership.³³³ He further found that MB Austin's 2018 registration effectiveness of 79.1 percent is expected given the degree of competition it faces.³³⁴ According to Dr. Hatch's methodology, the proposed South Austin dealership would have similar registration effectiveness to MB Georgetown (86.5 percent) because the two dealerships would face similar levels of competition from other luxury brands.³³⁵ He stated that sales in the MB Austin AOI would also go up because the south location would be convenient to many of those customers.³³⁶ Specifically, Dr. Hatch predicts that the MB Austin AOI will close about 50 percent of the gap between its current market share and the national benchmark through the addition of the South Austin dealership.³³⁷ He further predicts that MB Georgetown's AOI will experience 15 additional sales, MB Austin's AOI will experience 100 new sales, and South Austin's AOI will experience 100 new sales if the new dealership is added.³³⁸ Accordingly, his opinion is that 195 vehicles is the realistically achievable untapped market opportunity for the South Austin dealership and that 160 vehicles is the realistically achievable lost opportunity for MB in the Austin AOR.³³⁹ Dr. Hatch stated that sales made by the proposed dealership in excess of approximately 250 vehicles would be made at the expense of MB Austin and MB Georgetown, with most of those sales coming from MB Austin due to

³³² Tr. at 1187-90; Ex. P-7 at 36.

³³³ Tr. at 1189-90.

³³⁴ Tr. at 1191.

³³⁵ Tr. at 1192; Ex. P-7 at 14.

³³⁶ Tr. at 1193.

³³⁷ Tr. at 1193.

³³⁸ Tr. at 1194.

³³⁹ Tr. at 1194.

proximity.³⁴⁰ Dr. Hatch testified that Mr. Farhat's projections of sales of 500-700 units by the new dealership is not realistically achievable and exceed the opportunity in the market.³⁴¹

Dr. Hatch also criticized Mr. Farhat's methodology because his impact analysis was not based on geography, but his sales forecast was based on geography.³⁴² Dr. Hatch testified that Mr. Farhat's sales forecast methodology recognizes that geographical proximity has a large effect on which dealership in the Austin AOR will win a sale for the MB brand, and he agrees with Mr. Farhat's methodology in that regard.³⁴³ However, he disagrees with Mr. Farhat's in-sell determination because it inflates the untapped market potential for MB vehicles.³⁴⁴ He stated that Mr. Farhat does not do an analysis; rather, Mr. Farhat says that the in-sells are 281, and he considers that amount to be lost opportunity for MB without analyzing why the addition of one more dealer would lead to zero in-sells.³⁴⁵ According to Dr. Hatch, every market has some number of in-sells.³⁴⁶ Dr. Hatch noted that Mr. Farhat testified that the addition of a new dealership would not end all in-sell in the Austin AOR, but he did not address why in-sell occurs in his expert report.³⁴⁷ Therefore, according to Dr. Hatch, Mr. Farhat's opinion on in-sell is unreliable.³⁴⁸ In Dr. Hatch's opinion, a new dealership will not reduce a significant amount of in-sell that occurs for reasons of loyalty or price-shopping.³⁴⁹ He further opined that availability of specific inventory would be the most significant impact of a new dealership on in-sell; however, he predicted that it

³⁴⁰ Tr. at 1196-97.

³⁴¹ Tr. at 1213-14.

³⁴² Tr. at 1217.

³⁴³ Tr. at 1197.

³⁴⁴ Tr. at 1197-98; Ex. P-7 at 2.

³⁴⁵ Tr. at 1198.

³⁴⁶ Tr. at 1198.

³⁴⁷ Tr. at 1199.

³⁴⁸ Tr. at 1200.

³⁴⁹ Tr. at 1201-03.

would not be a very large impact.³⁵⁰ Dr. Hatch estimated that the new dealership would reduce in-sells by 55 based on his judgment rather than a specific calculation.³⁵¹

V. ARGUMENTS AND ANALYSIS OF STATUTORY FACTORS

A. Adequacy of Representation

To show good cause to add a new dealer point in South Austin, Applicant and MBUSA must address whether MB vehicles are being adequately represented as to sales and service.³⁵²

MB Austin contends that its dealership is adequately representing MB and is well-situated to adequately represent MB in the future. MB Austin asserts that by adding a third point, MBUSA seeks to have more dealerships in Austin than its competitors and that the Austin market will not support three MB dealerships. MB Austin's expert, Dr. Hatch, testified that if the proposed dealership existed in 2018, only about 160-195 additional registrations would have been captured.³⁵³ Mr. Stockton testified that if a third MB dealership had been operating in 2017 and 2018, it would have captured 242 total registrations from competing brands for both years.³⁵⁴ MB Austin asserts that this shortfall is based in part on MB Austin's inability to obtain mid- and large-sized SUVs from MBUSA. MBUSA's expert witness Mr. Farhat found that 474 registrations were not captured by MB in 2018; however, MB Austin asserts that Mr. Farhat's analysis was unreliable and that such a shortfall does not justify a finding of inadequate representation of the MB brand in Austin. MB Austin further asserts that no evidence established *when* the registration shortfall for MB might be sufficient to support another MB dealership without taking sales from existing MB dealers. According to MB Austin, Mr. Farhat's analysis showed that 2.5 MB dealers are needed in the Austin market rather than three.

³⁵⁰ Tr. at 1203-04.

³⁵¹ Tr. at 1204.

³⁵² Tex. Occ. Code § 2301.652(a)(1).

³⁵³ Tr. at 1194.

³⁵⁴ Tr. at 931, 954; Ex. P-1 at 64.

MBUSA asserts that nationwide, MB sales exceed those of its primary competitors (BMW, Lexus, and Audi); however, MB vehicle registrations have lagged behind its competitors' registrations in the Austin AOI.³⁵⁵ Moreover, MB has underperformed compared to its competitors in terms of sales volume and registration effectiveness since 2012.³⁵⁶ MB Austin's AOI ranks tenth out of the ten Market 12 dealers in registration effectiveness.³⁵⁷ MB as a brand has fallen further behind in 2018 and 2019 since BMW opened its South Austin dealership in 2018.³⁵⁸ During that time, MB Austin registered 330 vehicles in its AOI, compared to 925 by BMW, 912 by Lexus, and 665 by Audi.³⁵⁹ As of June 2019, year-to-day, MB was being outsold by its primary competitors, particularly in lower-priced entry-level luxury vehicles, such as the C-Class sedan and GLC SUV segments (MB sold 48 C-Class vehicles, versus 148 for BMW, 209 for Lexus, and 83 for Audi).³⁶⁰ Mr. Hardeman testified that MB Austin would rather sell higher-end vehicles because of the higher profit margins;³⁶¹ MBUSA's position is that such an approach is not effective in meeting MB's competition. In the Southern Region as of September 2019, MB outsold BMW by 2,700 vehicles, but MB trails BMW nationwide by 5,000 units (almost 500 of which are in the Austin AOI).³⁶² Accordingly, MB is underperforming in the Austin AOI compared to its regional and national performance.

MBUSA's expert Mr. Farhat found that MB is not adequately represented in the Austin AOR. Based on the national registration benchmark, the expectation for MB vehicle registrations in 2018 was 2,006, but there were only 1,581 registrations, for a shortfall of 425 in the Austin AOR.³⁶³ MBUSA also asserts that MB Austin's witness Dr. Hatch found that MB had

³⁵⁵ Tr. at 265, 1081-82.

³⁵⁶ Tr. at 1081-82.

³⁵⁷ Tr. at 1081.

³⁵⁸ Tr. at 1082.

³⁵⁹ Tr. at 1087-88.

³⁶⁰ Tr. at 1090, 1092-93; Ex. P-23.

³⁶¹ Tr. at 1396.

³⁶² Tr. at 1088-89.

³⁶³ Tr. at 452-53; Ex. I-65 at 40-41.

a net loss of 422 vehicles.³⁶⁴ MB's registration effectiveness in the Austin AOR was 78.8 percent, with 100 percent representing "average" registration effectiveness.³⁶⁵ Additionally, the proposed South Austin AOI was the fourth-worst in registration effectiveness under the national standard and the third-worst under the Texas standard.³⁶⁶ MB Austin was 61.6 percent sales effective in 2015, 71.1 percent in 2017, and 62.8 percent in 2018.³⁶⁷ According to Mr. Farhat, the Austin market consistently performs below average, whether under the national or Texas average. Mr. Farhat also determined that in order for MB to achieve the same "share of franchises" in Austin as it has nationally, it needs three dealerships in the Austin area.³⁶⁸ MBUSA disputes MB Austin's argument that it is unable to capture more registrations due to lack of supply of certain vehicles because that lack of supply affected dealers nationwide and therefore does not explain why MB Austin would fall below national benchmarks.³⁶⁹

The ALJs find that the evidence established that MB is not adequately represented in terms of vehicle sales in the Austin AOI and AOR. MB is being outsold by its competitors in Austin and lags further behind its competitors in Austin than it does in Texas, the Southern Region, and nationally. MB Austin's assertion that it lags behind in sales due to supply issues is not compelling; such issues impact dealers nationwide, and no evidence suggested that MB Austin is disproportionately affected. Moreover, MB's registration effectiveness is consistently below 100 percent (which represents average performance) in both the Austin AOR and MB Austin's AOI.

MB Austin further asserts that MB is adequately represented in terms of service because MB Austin is capturing all of the realistically achievable service opportunity in its AOI. According

³⁶⁴ Tr. at 1224; Ex. P-7 at 12.

³⁶⁵ Tr. at 453; Ex. I-65 at 40.

³⁶⁶ Tr. at 443-45; Ex. I-65.

³⁶⁷ Tr. at 472-75.

³⁶⁸ Tr. at 478-80; Ex. I-65 at 57. Specifically, Mr. Farhat testified that to meet national franchise share, MB needs 2.8 dealers in the Austin AOR, and to meet its Texas franchise share, it needs 2.7 dealers. Tr. at 479-80.

³⁶⁹ Tr. at 1341-42, 1095-96, 1110.

to MB Austin, it has achieved higher SOI scores than the national, regional, and area benchmarks. MB Austin disputes MBUSA's assertion that MB Georgetown performs most of the service work in MB Austin's AOI because MB Austin's service department is larger, MB Georgetown has low service volume, and MB Austin provides service to customers living near the MB Georgetown dealership.³⁷⁰ MB Austin is currently building a new parking garage that includes additional service bays to expand its service department, and it contends that that addition will help it continue to adequately represent MB in terms of service in the future.

MBUSA argues that MB Austin is not adequately capturing the lost service opportunity in its AOI. According to MBUSA, MB Austin's AOI was below every benchmark (national, regional, area, market, market tier) as of December 2018.³⁷¹ As of December 2018, approximately 12,400 MB vehicles were registered in the AOI, and 4,615 of those vehicles had not been serviced by an MB dealer within the past 13 months. MBUSA asserts that lost service has a value of almost \$5.7 million. Of the 7,900 vehicles that were serviced, MB Austin serviced about 43 percent of them, and 20 percent were serviced by other MB dealers.³⁷² Although MB Austin is currently building additional service bays, it is currently at capacity in its service department, and its customers experience longer-than-average wait times for service other than oil changes.³⁷³ MB Austin asserted that these wait times are the responsibility of MBUSA, because software fixes and parts are not timely available. However, MBUSA contends that such problems would not be unique to MB Austin and do not adequately explain its higher-than-average wait times. Additionally, the new service bays will not solve MB Austin's problem retaining service technicians, which has also led to longer wait times. MBUSA also asserts that MB Austin's location is inconvenient to many of its customers, which also contributes to inadequate service representation.³⁷⁴ MBUSA disputes MB Austin's assertion that younger vehicle owners prefer to take their vehicles to be serviced at independent providers because the testimony does not support

³⁷⁰ Tr. at 1396, 1447, 1449, 1510-11.

³⁷¹ Ex. I-26.

³⁷² Tr. at 856-57, 882-83; Ex. I-26.

³⁷³ Tr. at 862-64, 1454.

³⁷⁴ Tr. at 870-72, 903-04.

such an assertion; rather, the testimony is that those owners must be going to independent providers since they are not being serviced by dealers.³⁷⁵ Additionally, lack of available parts and software updates would equally affect independent providers and dealerships, so those challenges would not explain a lack of service representation by MB Austin.

The ALJs find that, although MB Austin performs better in terms of service than sales, MB is not adequately represented on service in the Austin AOI. A significant number of MB vehicles in the Austin AOI are serviced by independent service providers rather than dealers, which leaves millions of dollars in service lost to MB. MB Austin's claim that it loses service due to lack of parts and software fixes from MB is not persuasive, as such issues would impact service providers nationwide and would not have a disparate impact on MB Austin. The construction of more service bays by MB Austin may help alleviate the service wait times and potentially increase the number of vehicles MB Austin can service, but no evidence was presented to suggest that the impact will be so large that the lost service opportunity will be significantly reduced.

MB Austin contends that its facilities adequately represent the MB brand and that the relevant standard is "adequate" representation, not "optimal" or "superior" representation.³⁷⁶ MB Austin asserts that its dealership facilities are compliant, and compliance is all that is necessary to meet the adequacy standard.

MBUSA acknowledges that MB Austin is at least minimally compliant with the MB brand image requirements but asserts that minimal compliance is not sufficient to compete with, for example, MB Georgetown and the new South Austin BMW dealership.³⁷⁷ Additionally, MB Austin's service bays are not air conditioned, whereas competitor dealerships have air conditioning, which could contribute to MB Austin's difficulty in retaining service technicians.

³⁷⁵ Tr. at 855, 859, 1517-18.

³⁷⁶ MB Austin Response and Closing Brief at 29.

³⁷⁷ Tr. at 625.

MBUSA also argues that MB Austin's location is no longer a desirable part of town for a luxury car dealership.³⁷⁸

The ALJs agree that for purposes of adequately representing the MB brand, minimal compliance with brand standards is not necessarily competitive. Although the fact that MB Austin is minimally compliant neither weighs for or against addition of a new dealership in itself, MB Austin's lack of competitiveness in terms of its facilities may limit MB Austin's ability to adequately represent the brand in Austin's highly competitive luxury vehicle market.

MB Austin concedes that establishing the new dealership in South Austin would increase customer convenience but argues that an increase in customer convenience is not desirable when the market potential is not sufficient to support the new dealership without harming the existing dealers. The ALJs address this argument in the section below on harm to MB Austin.

In its argument, MBUSA puts a great deal of emphasis on Mr. Hardeman's July 2018 letter requesting that MBUSA award MB Austin with the South Austin point in a different location and on his statement that he desired to open an additional location in southwest Austin, asserting that his statements show that MB Austin agrees that a third dealership is necessary.³⁷⁹ MB Austin counters that Mr. Hardeman made the request not because he felt that a third location was necessary but because if MBUSA was intent on adding a third point, he wished to be the dealer rather than face competition. Additionally, MB Austin's witnesses testified that the southwest Austin location could be an additional service/repair shop or showroom, rather than a full dealership. Accordingly, the ALJs do not put as much weight on Mr. Hardeman's statements as MBUSA urges.

Taking into account the evidence on the growth of the Austin market, in terms of population and in terms of high-income households, and the evidence of MB Austin's below-average sales effectiveness, the preponderance of the evidence shows MB Austin is not adequately representing

³⁷⁸ Tr. at 623-24.

³⁷⁹ Tr. at 1012-13; Ex. I-43.

the MB brand in terms of sales. Additionally, registration effectiveness is worse in South Austin, where the new dealership will be located. MB Austin is performing better in terms of service, but the evidence shows the Austin market contains ample service opportunity to support an additional dealership; thus, significant service opportunity is being lost to MB. Moreover, MB Austin's service customers have long wait times due to its service department being at capacity. Additionally, the evidence established that the Austin market has supported at least a dozen new dealerships from competing luxury brands in the past few years; thus, MBUSA's competitors are increasing their market share in the Austin market while MBUSA market share has fallen. Accordingly, this factor weighs in favor of the new dealership.

B. MB Austin's Substantial Compliance with the Dealer's Franchise

The second statutory factor examines whether MB Austin is in substantial compliance with its franchise agreement with MBUSA.³⁸⁰ "Substantial compliance" is a doctrine of contract law that "excuses contractual deviations or deficiencies which do not severely impair the purpose underlying the contractual provision."³⁸¹

MB Austin asserts that it is in substantial compliance with its franchise agreement and states that MBUSA has not sent any franchise noncompliance or cure notices concerning any sales performance contractual obligations.³⁸² MBUSA recently renewed MB Austin's franchise agreement and approved MB Austin's parent company's purchase of the San Juan MB dealership in May 2019.³⁸³ MBUSA asserts that MB Austin has breached its dealer agreement sales obligation to be 100 percent sales effective in its AOI. MB Austin contends that MBUSA did not prove that a failure to achieve 100 percent sales effectiveness is a breach of MB Austin's franchise agreement because MBUSA did not introduce MB Austin's franchise agreement into evidence, and because

³⁸⁰ Tex. Occ. Code § 2301.652(a)(2).

³⁸¹ *Burtch v. Burtch*, 972 S.W.2d 882, 889 (Tex. App.—Austin 1998, no pet.); *RCJD Motors, Inc. v. Huffines Dodge Plano, LP*, SOAH Docket No. 608-10-5694.LIC, Proposal for Decision at 31 (April 2, 2012).

³⁸² Tr. at 1287.

³⁸³ *Citing Hudiberg Chevrolet, Inc. v. Frontier GMC, Inc., et al.*, Proceeding No. 193, Hearing Report at 33-34 (Oct. 30, 1980).

no MBUSA witness testified that 100 percent sales effectiveness was an obligation of the franchise agreement or that MB Austin's failure to achieve 100 percent sales effectiveness was a breach of the agreement. MB Austin asserts that the Final Order in *Westside Motors, Inc. v. Smith-Neilson Dodge* supports its assertion. *Westside* states that a protestant's "failure to achieve [minimum sales requirements] during its first ten months of operations as a Dodge dealer cannot be considered to be a material breach of its franchise agreement, and most certainly not a breach of the type contemplated by Section 4.06(c) of the Code."³⁸⁴ *Westside* is a proposal for decision from 1979, and MB Austin did not brief whether the relevant Code section in effect at that time is the same or similar to the statutory language in effect today. Moreover, MB Austin has been a dealer for decades, not just ten months, as was the case with the protestant in *Westside*. Therefore, the ALJs do not give much weight to that case in analyzing this statutory factor.

MB Austin also argues that it ranked 24th out of 117 MB dealers in the Southern Region and had the highest new vehicle sales volume in Market 12 as of year-to-date September 2019.³⁸⁵ MB Austin asserts that it is achieving acceptable sales levels because it has received dealer bonuses for achieving 80 percent sales effectiveness.³⁸⁶

MBUSA relies on *Burns Motors, Inc. v. Payne Edinburgh LLC* for the proposition that failure to achieve 100 percent sales effectiveness (referred to as minimum sales requirement, or MSR, in that case) is a failure to comply with the franchise agreement and a substantial and material breach that significantly impairs the purpose of the franchise requirement.³⁸⁷ MBUSA asserts that MB Austin has failed to comply with its dealer agreement sales obligation. MB Austin achieved 61.6 percent sales effectiveness in 2014, increasing to 71.1 percent in 2017, and decreasing to 62.8 percent in 2018.³⁸⁸ As of September 2019, MB Austin had about 75 percent

³⁸⁴ *Westside Motors, Inc. v. Smith-Neilson Dodge*, Proceeding No. 140, Hearing Report at 51 (February 20, 1979).

³⁸⁵ Tr. at 1310-11; Ex. P-22.

³⁸⁶ Tr. at 1680.

³⁸⁷ *Burns Motors, Inc. v. Payne Edinburgh LLC*, MVD Docket No. 16-0028, Proposal for Decision at 64 (June 14, 2018).

³⁸⁸ Tr. at 472-76; Ex. I-65 at 54-5.

sales effectiveness.³⁸⁹ MBUSA further argues that although the franchise agreement is not in evidence, the testimony supports its contention that MB Austin is out of compliance with the agreement.³⁹⁰ It also argues that MB Austin did not refute the testimony by introducing the franchise agreement itself and, therefore, the issue is undisputed.

MB Austin disputes MBUSA's reliance on *Burns Motors* because in that case, the franchise agreement was in evidence and it was undisputed that the protesting dealer was required to meet 100 percent of its minimum sales requirement.³⁹¹ Additionally, the manufacturer in that case had frequently raised and corresponded with the protesting dealer about the need to meet that requirement, unlike this case.³⁹²

The ALJs find that MBUSA failed to prove that MB Austin is not in substantial compliance with its franchise agreement. The franchise agreement was not introduced into evidence. The testimony cited by MBUSA to support its assertion that MB Austin is not complying with its franchise agreement discusses sales effectiveness and states that 100 percent sales effectiveness must be achieved in order to be compliant, but neither witness explains where that "requirement" comes from. Therefore, the ALJs have no way of determining whether MB Austin breached its franchise or dealer agreement. Although MB Austin has failed year after year to achieve 100 percent sales effectiveness, it is not clear from the record that such failure constitutes a lack of compliance with its obligations to MBUSA. In *Burns Motors*, which MBUSA relies upon to support its arguments, the parties did not dispute that the protesting dealer had failed to meet its contractual obligations and the contract itself was in evidence. Here, however, the parties dispute whether MB Austin met its contractual obligations in this case, and the contract is not in evidence. MBUSA's argument that the issue is undisputed because MB Austin did not introduce the franchise agreement into evidence to refute MBUSA's witnesses' testimony is misplaced; MBUSA and the Applicant have the burden of proof. The ALJs find that they did not meet their

³⁸⁹ Tr. at 594, 1098-99.

³⁹⁰ Tr. at 296-300, 1076, 1080.

³⁹¹ *Burns Motors*, PFD at 64.

³⁹² *Burns Motors*, PFD at 65-66.

burden of proof on this issue. Accordingly, in this case, this factor does not weigh in favor or against granting the Application.

C. Desirability of a Competitive Marketplace

The third statutory factor requires consideration of “the desirability of a competitive marketplace.”³⁹³ The parties agree that the establishment of a new dealership increases price competition both within and between brands. Having an additional dealer in the market provides choice to consumers, particularly on pricing, allowing consumers to “cross-shop” (shop the price for a given model or type of vehicle between brands at multiple dealerships).³⁹⁴

The parties agree that the Austin luxury-vehicle market is “hypercompetitive.”³⁹⁵ However, MB Austin disputes that the addition of the new dealership will result in lower prices for consumers because MB Austin already faces price competition from other luxury brand dealerships. Additionally, MB Austin argues that MBUSA failed to prove that enough realistically achievable lost opportunity exists in the market to support the new dealership without harming MB Austin; therefore, competition will not increase “in a healthy way.”³⁹⁶ MB Austin asserts that the proposed South Austin location is not near MB brand buyers and that fewer MB sales are made in that area because “the demographics there are less desirable for buying luxury vehicles;”³⁹⁷ rather, those buyers live closer to MB Austin’s location.

MB Austin asserts that MBUSA should have required Applicant to submit a dealer application, including a business plan, a balance sheet, a breakeven analysis, and other financial projections. MB Austin contends that in order to show that the proposed dealership will further healthy competition, reliable proof of the proposed dealership’s estimated revenues and expenses

³⁹³ Tex. Occ. Code § 2301.652(a)(3).

³⁹⁴ Tr. at 1015, 1240, 1598, 1601.

³⁹⁵ MBUSA Opening Brief at 17; MB Austin Response and Closing Brief at 36.

³⁹⁶ MB Austin Response and Closing Brief at 37.

³⁹⁷ MB Austin Response and Closing Brief at 38.

are required.³⁹⁸ MB Austin asserts that, if Applicant sells primarily entry-level A- and C-Class vehicles, it will be selling most of its new vehicles at a loss. According to MB Austin, MBUSA and Applicant are expecting MB Austin to subsidize the new dealership until sometime in the future when the Austin market has grown enough to support all three dealerships.

According to MBUSA, healthy competition means increased intra- and inter-brand competition, resulting in more competitive prices and enhanced customer purchase and service experience and satisfaction. A competitive Austin marketplace would also have an additional, convenient location near the brand's competitors to enhance cross-shopping, and in a high-population area with a large number of qualified households in terms of income and age.³⁹⁹ Additionally, MBUSA asserts that healthy competition is achieved with modern facilities that provide more and better selection of the manufacturer's products, increasing inventory in the market.⁴⁰⁰ MBUSA points to other cases where it contends the Board of the Texas Department of Motor Vehicles looked at a brand's low registration rates in the geographic areas at issue and at the protestant's high gross profits, especially the average profit per new unit sold, in determining whether there was a need for increased intra-brand competition for consumers.⁴⁰¹ Additionally, MBUSA asserts that a new Austin dealership will increase consumer choice and brand advertising. According to MBUSA, the proposed South Austin site will meet the requirements necessary to increase competition because it is an underrepresented area for the brand, it has recent and projected population growth, and it includes a large distribution of higher-income households.⁴⁰² Commercial and residential development is booming, and the location is convenient for customers.⁴⁰³

³⁹⁸ MB Austin cites to the Texas Finance Code and savings and loan association cases for this contention. *See* MB Austin Response and Closing Brief at FN 44.

³⁹⁹ *Citing RCJD*, PFD at 36-37, Final Order at 6; *Rockwall Imports v. The Allee Corp.*, SOAH Docket No. 601-09-1276.LIC, Final Order at 11 (Jan. 23, 2012); *Bayway Auto Sales, Inc v. Sonic Houston V LP*, SOAH Docket No. 608-10-2958.LIC, Final Order at 12-13 (July 14, 2011).

⁴⁰⁰ *Citing GKG Motors, Inc. v. Cantwell Fielder, Ltd, et al.*, SOAH Docket No. 05-0016.LIC, Proposal for Decision at 66 (April 26, 2007).

⁴⁰¹ *Citing Rockwall*, Final Order at 11; *RCJD*, PFD at 36.

⁴⁰² Tr. at 489-92; Ex. I-65 at 80-81.

⁴⁰³ Tr. at 79-81, 1236.

MBUSA argues that Applicant has a history of increasing market competition to consumers' benefit, as he did in turning around the Wilsonville market. Applicant markets to and attracts entry-level luxury customers, while MB Austin does not market to those customers.⁴⁰⁴ However, MB's competitors are marketing to this demographic and outselling MB in entry-level segments.⁴⁰⁵

MB Austin has had higher than average gross profit on sales of new vehicles, charging more for vehicles than its peers on an average per unit basis.⁴⁰⁶ In 2018, MB Austin increased its gross profit on finance, insurance, and service contract products sold with new vehicles.⁴⁰⁷ Accordingly, MBUSA argues, MB Austin can easily adjust its business strategy to meet additional competition and capture untapped opportunity in the market.⁴⁰⁸

MBUSA disputes MB Austin's assertion that Applicant will sell most of its new vehicles at a loss, arguing that assertion is not supported by the evidence. Further, MBUSA points to Applicant's success with MB Wilsonville and other dealerships to support its ability to make a profit and create a successful dealership in South Austin. Further, MBUSA argues that there is sufficient lost opportunity in the market to support a new dealership without the existing dealerships needing to "subsidize" it. As Mr. Newcomb testified, MBUSA would not add a dealer if it would take away sales from existing dealers.⁴⁰⁹

Neither party disputes the desirability for a competitive marketplace. The ALJs find that the evidence demonstrated establishment of the new South Austin dealership will increase

⁴⁰⁴ Tr. at 59-60, 62; 1372, 1396.

⁴⁰⁵ Tr. at 1090; Ex. P-23.

⁴⁰⁶ Tr. at 770-72; Ex. I-69 at 80-81.

⁴⁰⁷ Tr. at 772; Ex. I-69 at 82-83.

⁴⁰⁸ *Citing Austin Chevrolet, Inc. v. Motor Vehicle Board and DMV of Tex. Dept. of Transp.*, 212 S.W.3d 425, 434 (Tex. App.—Austin 2006, pet. denied).

⁴⁰⁹ Tr. at 301.

advertising for the MB brand, expand the availability of inventory in the market, improve customer access to the MB brand, make service more convenient for customers, and result in more choice and competitive pricing for consumers. As discussed in Section V.A. above (addressing adequacy of representation), sufficient lost opportunity exists in the Austin market to support a new dealership without causing harm to the existing dealerships. The proposed site in South Austin is in a growing part of the city where MB is poorly represented, it is convenient to consumers, and it is located near other luxury vehicle dealers, such as the new BMW dealership. Moreover, the new BMW dealership has experienced over 100 percent sales effectiveness, despite MB Austin's claim that the area does not have the demographics to support a luxury dealership. Further, the evidence established that Applicant has a track record of operating successful dealerships and working well with other MB dealers, rather than "cannibalizing" sales from them. MB Austin did not show why it is necessary or required for Applicant to have submitted business plans into evidence in order to establish that adding the new dealership will promote competition in the marketplace. Further, the evidence established that MB Austin is a highly profitable dealership that is in good position for competing in the market. Accordingly, opening the new dealership will promote healthy competition in the marketplace, and this factor weighs in favor of opening the new dealership.

D. Harm to Protested Franchised Dealer

Next, the parties must address whether a new point in South Austin will cause harm to MB Austin.⁴¹⁰

MB Austin asserts that, under *Landmark Chevrolet*, an existing dealer is not required to sacrifice its profits to the proposed dealership if the amount of realistically achievable lost opportunity in the relevant market is less than the number of new units the proposed dealership must sell in order to break even.⁴¹¹ While there was insufficient evidence of untapped opportunity in the market to support an additional dealership in that case, the *Landmark Chevrolet* PFD

⁴¹⁰ Tex. Occ. Code § 2301.652(a)(4).

⁴¹¹ Citing *Landmark Chevrolet Corp. v. General Motors Corp., Chevrolet Motor Division*, Docket No. 02-0002 LIC, Proposal for Decision at 30-31, 35.

nonetheless notes that it is acceptable for an existing dealership to experience some lost profits when a new dealership is established.⁴¹² MB Austin also relies on several other cases in which courts found insufficient evidence of untapped market opportunity, or found that a new dealer would have to take sales from existing dealers in order to make profits, thus harming the existing dealers. MB Austin asserts that its experts' opinions established that there is insufficient, realistically-achievable lost opportunity in the Austin market to support a third dealership. The ALJs do not agree. Ample evidence of the untapped market opportunity was presented by MBUSA. Vehicles registrations lost to competitors and in-sell in the Austin market provide sufficient opportunity to sustain a new dealership, especially considering that Austin will likely experience continued growth in the years between now and when the dealership would be built and operating on a day-to-day basis.

MBUSA contends that the appropriate standard of harm to MB Austin is "whether the establishment will cause so much harm . . . as to cause the failure of the dealership or at least reduce the existing dealer's profitability to such extent that it could not properly serve the public."⁴¹³ Further, an existing dealer is not necessarily harmed because it must share the market with a new dealership, even if it experiences profit loss after expansion of the dealer network.⁴¹⁴ According to MBUSA, where sales and service opportunities exist in the market, as in this case, only profit loss that causes the dealer to shutter its doors or to be unable to serve the public would weigh in favor of the protestant on this factor. MBUSA asserts that there is lost opportunity in the Austin market and that it would be detrimental to MBUSA to add a new dealer that could only profit by capturing sales from existing dealers.⁴¹⁵

MB Austin claims that in every case in the United States in which a new MB dealership was added, the existing dealerships lost sales.⁴¹⁶ Taking that as true, if the standard is that existing

⁴¹² *Landmark Chevrolet*, Proposal for Decision at 30-31.

⁴¹³ *Citing RCJD*, PFD at 41 (internal citations omitted).

⁴¹⁴ *Austin Chevrolet, Inc.*, 212 S.W.3d at 434.

⁴¹⁵ Tr. at 300-01.

⁴¹⁶ Ex. P-1 at 13.

dealers should experience no degree of lost sales for a new dealership, no new MB dealerships could ever be established in the United States. Thus, MB Austin's standard is unreasonable and only proves the point that some degree of loss to existing dealers has been found to be acceptable and to not constitute "harm" for purposes of this statutory factor.

MB Austin asserts again under this factor that Applicant's "breakeven number" is critical to establish that MB Austin will not be harmed by the establishment of the new dealership.⁴¹⁷ According to MB Austin, the market for entry-level luxury vehicles is insufficient to support the new dealership, ranging from 114 entry-level retail registrations lost to competitors in the Austin AOR to only 37 entry-level registrations lost to competing brands in the proposed South Austin AOI as of May 2019.⁴¹⁸ MB Austin argues that MBUSA did not adequately address how the lost opportunity in the market will support the planning volume of 916 vehicles that MBUSA assigned to the proposed dealership.⁴¹⁹

MBUSA asserts that the planning volume estimated for the South Austin dealership of 916 is for the year 2023, thus a projection accounting for growth in the Austin area that is not an unreasonable estimate.⁴²⁰

The ALJs find that MB Austin did not show why Applicant's "breakeven number" is necessary to show that MB Austin will not be harmed when the evidence established that sufficient opportunity exists in the market to sustain the proposed dealership. Moreover, the planning volume for 916 vehicles is merely a projection, and no evidence suggested that the new dealership must sell that many vehicles in order to be profitable or to break even.

Mr. Hardeman testified anecdotally that when MB Georgetown relocated from Temple in 2004, new vehicle sales dropped 35 percent within 90 days, and MB Austin's total profits dropped

⁴¹⁷ MB Austin Response and Closing Brief at 50.

⁴¹⁸ Ex. I-68 at 5-7.

⁴¹⁹ Ex. I-42.

⁴²⁰ Ex. I-42.

45 percent, from \$2 million to \$1.1 million.⁴²¹ According to Mr. Hardeman, it took four or five years for MB Austin's profits to return to 2004 levels.⁴²² Mr. Hardeman believes that eventually MB Austin will lose service business to the new dealership.⁴²³ The ALJs do not find this information to be persuasive on whether MB Austin will be harmed by the addition of a dealership at this point. MB Georgetown relocated 16 years ago; the Austin economy and the luxury vehicle market has changed significantly in that time period.

MB Austin asserts that Mr. Farhat's gross-loss numbers are unreliable based on Dr. Hatch's testimony regarding the "fatal flaw" of applying the gross loss concept at the ZIP code level.⁴²⁴ In its brief, MB Austin reiterates Dr. Hatch's criticisms of Mr. Farhat as set forth above in the summary of his testimony. In sum, MB Austin asserts that it is unrealistic to assume, as Mr. Farhat does, that every ZIP code in the Austin AOR should be at 100 percent registration effectiveness regardless of location or demographics. While MB Austin acknowledges that the Board found Mr. Farhat's gross-loss methodology appropriate in *RCJD Motors*, it argues that the flaws in the gross-loss methodology were not critical in that case because far more registration losses were present in the market than the applicant projected to sell.⁴²⁵ Further, MB Austin asserts that, assuming Mr. Farhat's methodology is valid, his gross-loss number is inflated and unreliable because he made no determination of the normal or expected level of gross loss present in the Austin AOR or the amount of gross loss that would remain if the proposed dealership were established. According to MB Austin, gross loss will always exist, even when MB's registration effectiveness is greater than 100 percent.⁴²⁶

MB Austin also criticizes Mr. Farhat for making no determination of the normal or expected level of in-sell in the Austin AOR or the amount of in-sell that would remain if the

⁴²¹ Tr. at 1289-90, 1294.

⁴²² Tr. at 1289, 1295.

⁴²³ Tr. at 1289.

⁴²⁴ MB Austin Response and Closing Brief at 53.

⁴²⁵ *RCJD*, Final Order at 6-7.

⁴²⁶ Tr. at 1160-61.

proposed dealership were established. MB Austin contrasts his testimony in this case, in which he did not state that the rate of in-sell in Austin was high, with that in *Burns Motors*, where he stated that the in-sell into the protesting dealer's locality was unusually high.⁴²⁷ Additionally, according to MB Austin, Mr. Farhat both assumed that all 281 units of in-sell were available to the new dealership and that in-sell will not be reduced to zero.⁴²⁸ MB Austin asserts that no more than 250 units of lost opportunity are available for capture in the Austin AOR, which is far less than the sales projected by the proposed dealership.⁴²⁹

MBUSA's witnesses testified that they do not expect MB Austin to experience any lost sales due to the lack of registrations in the South Austin AOI and level of in-sell of entry-level vehicles that the new dealership will focus on.⁴³⁰ Mr. Farhat calculated the sales opportunity in the Austin AOR that would have been available to the new dealership had it existed in 2018. He also calculated what the new dealer might have sold in the area based on selling patterns of the existing dealerships. His analysis did not account for projected growth in the Austin area. Mr. Farhat found a total lost opportunity of 755 sales (474 units of gross loss and 281 units of in-sell).⁴³¹ According to MBUSA, it is inappropriate to net out gross loss by the units in the ZIP codes that exceed the national benchmark, as Dr. Hatch suggests, because it is not reasonable to expect ZIP codes that are already above average to decline when sales are made in the deficient ZIP codes, but it is reasonable to expect below-average areas to increase to 100 percent registration effectiveness.⁴³² MBUSA contends that Dr. Hatch's methodology of calculating net loss at the AOI level obscures specific areas that are underperforming. According to MBUSA, most luxury brands examine markets at the ZIP code level.⁴³³ Moreover, MBUSA asserts that although Dr. Hatch criticized Mr. Farhat's use of ZIP codes to calculate gross loss, Dr. Hatch's estimate of 422 units of gross

⁴²⁷ *Burns Motors*, PFD at 62.

⁴²⁸ Tr. at 1198, 1206, 1601.

⁴²⁹ Tr. at 1215; Ex. P-7 at 4.

⁴³⁰ Tr. at 300-01, 1078.

⁴³¹ Tr. at 504-06, 578-79; Ex. I-65 at 42, 96-98.

⁴³² Tr. at 505.

⁴³³ Tr. at 1594.

loss is not far from Mr. Farhat's calculation of 474.⁴³⁴ Additionally, MBUSA asserts that the distribution of loss in an AOR is not random, as Dr. Hatch suggests; rather, calculating loss by ZIP code takes into account the actual registrations in that area as well as demographics and locational issues to show where losses are occurring. Mr. Farhat's analysis revealed that MB is experiencing loss due to the new South Austin BMW dealership.⁴³⁵

MBUSA further criticizes Dr. Hatch's approach for reducing his estimated 425 units of net loss to 195 based on differing degrees of competition in each Austin AOI as "not well developed," "novel," "not utilized in automotive dealer network planning," and something that is not accepted in the industry.⁴³⁶ Moreover, when Mr. Farhat applied Dr. Hatch's approach to the new BMW dealership, it was not predictive and underestimated registration effectiveness by 12.1 to 26.4 percentage points.⁴³⁷

Mr. Farhat determined, based on the sales patterns of MB Austin and MB Georgetown, that the new dealership would sell from 500-700 new vehicles.⁴³⁸ MBUSA asserts that because this range is below the total lost opportunity of 755 units, the new dealership need not take any sales from the existing dealers.⁴³⁹ When Mr. Farhat tested his model against recent additions of MBUSA dealers in Dallas and Houston, he found that MB increased its registration effectiveness in those cities. He also found that although some of the closest existing dealerships lost some sales, they likely would have lost more sales to competitors had the new dealerships not opened.⁴⁴⁰ MBUSA also argues that the addition of the new BMW dealership in South Austin positively

⁴³⁴ Ex. P-7 at 12.

⁴³⁵ Tr. at 1595-97.

⁴³⁶ Tr. at 1608; Ex. I-68 at 3.

⁴³⁷ Tr. at Ex. I-68 at 14.

⁴³⁸ Tr. at 508-09, 576-77; Ex. I-65 at 15.

⁴³⁹ Tr. at 507.

⁴⁴⁰ Tr. at 513-16, Ex. I-65 at 16, 105-10, 117.

impacted the brand by increasing registration effectiveness to over 100 percent without cannibalizing sales from the existing BMW dealer.⁴⁴¹

Mr. Stockton estimated that the new dealership would likely result in MB Austin losing from 20 to 30 percent of its annual new vehicle sales, which would reduce profits by approximately \$1 million to \$1.5 million per year.⁴⁴² Further, Mr. Stockton estimated that MB Austin's preowned department would suffer a loss of \$200,000 in profits and that its parts and service department would suffer a loss of approximately \$750,000 in profits per year.⁴⁴³

According to MBUSA, Mr. Stockton's estimates of 20 to 30 percent loss to MB Austin as a result of the new dealership is faulty. It does not account for economic and population growth in Austin. Additionally, Mr. Farhat demonstrated that Mr. Stockton's gravity model exaggerates predicted impact on existing dealers when applied to real world examples of other markets with recently established new dealerships.⁴⁴⁴ According to Mr. Farhat's application of the model, it overstates impact to existing dealerships by 30 to 40 percent.⁴⁴⁵ Further, Mr. Stockton admitted that his gravity model did not accurately capture MB Austin's performance in its fixed operations.⁴⁴⁶ Moreover, Mr. Stockton's report consists of a 17-page narrative with almost 300 pages of exhibits.⁴⁴⁷ Many of the calculations in the exhibits are presented without explanation or support, either in the report or his testimony. Similarly, many of his estimates are not supported by calculations.⁴⁴⁸ Mr. Stockton's calculation of loss that aligned with Ms. Heinemann's was

⁴⁴¹ Tr. at 1610-11; Ex. I-67 at 14-15.

⁴⁴² Tr. at 997; Ex. P-1 at 234, Ex. I-70 at 48.

⁴⁴³ Tr. at 997-98, 1000.

⁴⁴⁴ Tr. at 1625-26; Ex. I-67 at 26.

⁴⁴⁵ Tr. at 1625-26; Ex. I-67 at 26.

⁴⁴⁶ Tr. at 1019.

⁴⁴⁷ Ex. P-1.

⁴⁴⁸ Tr. at 1051-56.

disregarded in his report, and he instead focused on a statistically non-significant result that he doubled from 12.37 percent to 25 percent.⁴⁴⁹

The ALJs are also not persuaded by Mr. Stockton's and Dr. Hatch's projections and analyses. Mr. Stockton's projections are based on non-statistically significant results that are doubled, though he says he merely rounded up.⁴⁵⁰ Neither Mr. Stockton nor Dr. Hatch used methodologies that have been accepted by the automotive industry or the Board, and their chosen methodologies are not improvements upon the accepted methodologies used by Ms. Heinemann and Mr. Farhat. Rather, the methodologies employed by Mr. Stockton and Dr. Hatch do not hold up when tested in real-world examples of new dealership establishments.

MB Austin contends that there is no lost service opportunity in the Austin AOR, especially given the MB brand's product and supply problems and decline in market share and gross sales. Therefore, it asserts, the new dealership can only be profitable by taking service business from MB Austin.

MBUSA asserts that millions of dollars of lost service opportunity will be available to the new dealership without needing to take any service business from MB Austin.⁴⁵¹ The percentage of MB vehicles serviced by MB dealers in the Austin AOI was below the metro average as well as other benchmarks.⁴⁵² Further, Mr. Hardeman testified that he expects MB Austin to keep its service business if the new dealership opens.⁴⁵³ Additionally, Mr. Hoefl testified that there is more service work than MB Austin can currently handle.⁴⁵⁴

⁴⁴⁹ Tr. at 1039-41.

⁴⁵⁰ Tr. at 1039-42; Ex. P-1 at 244.

⁴⁵¹ Exs. P-25 through P-28.

⁴⁵² Tr. at 867-70, 899-900; Ex. I-25.

⁴⁵³ Tr. at 1393-95.

⁴⁵⁴ Tr. at 899-901, 904.

The ALJs find that sufficient lost service opportunity exists in the market to support a new dealership. The amount of untapped service opportunity is significant, regardless of MB Austin's performance related to service. Moreover, MB Austin simply did not support its assertions that there is no lost service opportunity or that the only way the new dealership could be profitable is to take service work away from MB Austin.

MB Austin claims that it is profitable because of its ability to hit MBUSA's sales and service performance goals and to obtain incentive payments. According to MB Austin, it had an operating profit of \$667,011 in 2018 and collected \$4.7 million in incentives for meeting sales and service performance targets.⁴⁵⁵ MB Austin asserts that although Mr. Stockton and Ms. Heinemann reviewed the impact on MB Austin's cost structure if losses were to occur, they did not look at the impact of lost sales on MB Austin's ability to obtain incentives from MBUSA.

MBUSA disputes MB Austin's contention that it may not qualify for MB incentive payments if the new dealership takes vehicle sales and service business from it. No evidence was presented to show that MB Austin will not qualify for incentive payments if the new dealership opens. MBUSA asserts that MB Austin conflates incentives paid on every new vehicle sale with bonuses tied to achieving a certain volume of new vehicle sales. MBUSA contends that bonuses are generally earned by activities other than new vehicle sales, by meeting other standards; by meeting those standards, MBUSA pays the incentive as a percentage of the price on every new vehicle sold.⁴⁵⁶ According to MBUSA, the only bonus related to new vehicle sales is tied to scores such as sales effectiveness, which represented 14 percent of the 2017 incentives, and MB Austin was already performing poorly on that score.⁴⁵⁷ MBUSA contends that the addition of the new South Austin AOI will allow MB Austin to become more sales-effective by making its AOI smaller, thus increasing the changes that it would do well on this bonus measure.

⁴⁵⁵ Ex. I-69 at 51-52.

⁴⁵⁶ Tr. at 810-11.

⁴⁵⁷ Ex. P-19 at 2.

The ALJs do not find MB Austin's argument regarding incentive payments to be persuasive. As noted by MBUSA, no evidence suggested that MB Austin would not qualify for incentive payments if the new dealership opens or even if MB Austin lost some sales or service to the new dealership.

MB Austin argues that the addition of the South Austin AOI will cause MB Austin to lose its competitive and convenience advantage in approximately six high-income ZIP codes where it currently makes a significant portion of its sales. MB Austin argues that the evidence established that those ZIP codes constitute 799 retail registrations that will be transferred to the proposed dealership.⁴⁵⁸

MBUSA contends that MB Austin is so profitable and financially successful, it can withstand competition from an additional dealer. Every year since 2015, MB Austin's net profit has exceeded the benchmark composite groups analyzed by Ms. Heinemann.⁴⁵⁹ MB Austin has no long-term debt;⁴⁶⁰ it had a cash position of \$4.6 million, a net cash position of nearly 600 percent, and working capital of 200 percent of what MBUSA requires for a healthy dealership;⁴⁶¹ its net profit for 2018 exceeded its total net fixed assets after depreciation (\$5.6 million versus a little under \$4 million);⁴⁶² MB Austin's return on equity is very high and far exceeds the average of the composite groups.⁴⁶³

According to MBUSA, MB Austin's profitability is not dependent on its volume of new vehicle sales. Specifically, in 2018, MB Austin's profit increased from \$4.7 million to \$5.6 million, but it sold 16 percent fewer new vehicles.⁴⁶⁴ MB Austin generates a higher amount of revenues

⁴⁵⁸ Ex. P-47 at 1243.

⁴⁵⁹ Tr. at 739-42; Ex. I-69 at 74-75.

⁴⁶⁰ Tr. at 730-32; Ex. I-14 at 1.

⁴⁶¹ Tr. at 734; Ex. I-14 at 1.

⁴⁶² Tr. at 734-35; Ex. I-14 at 1.

⁴⁶³ Tr. at 747-49; Ex. I-69 at 77.

⁴⁶⁴ Tr. at 750-51; Ex. I-69 at 74.

from its fixed operations (service, parts, and body shop departments) than the benchmark groups, and the profit margins in fixed operations are much higher than those in the new or used vehicle departments.⁴⁶⁵ Additionally, MB Austin's net profit in its fixed operations exceeds all of its fixed expenses by 1.72 times, which is more than the composite groups.⁴⁶⁶ Mr. Stockton agreed that MB Austin performs better in fixed operations than other dealers and better than his proximity models would suggest; he theorized this could be because its location is convenient for customers commuting to Austin from outlying areas to drop off their vehicles for service, or because its fixed operations department is well-run.⁴⁶⁷ MBUSA also asserts that MB Austin is in a better financial position than most dealerships because fixed operations are more recession-proof than vehicles sales: if customers are not buying new cars, then they will need to have their old cars serviced.⁴⁶⁸ Additionally, because its net profit from fixed operations fully covers its fixed expenses, MB Austin has more flexibility in its new and used vehicles departments.⁴⁶⁹

MB Austin also has a large used vehicle department with higher gross profit per unit sold than the benchmark groups.⁴⁷⁰ Mr. Stockton agreed that MB Austin is likely performing better in its used vehicle department than other dealers in Texas.⁴⁷¹ Additionally, in 2018, MB Austin made a higher profit on its finance, insurance, and service contract products with its new car sales while maintaining its higher-than-average gross profits on new vehicles, as compared to the benchmark groups.⁴⁷²

⁴⁶⁵ Tr. at 752-57; I-69 at 88.

⁴⁶⁶ Tr. at 757-61, 818-19; Ex. I-69 at 90-92, 96.

⁴⁶⁷ Tr. at 1019-20.

⁴⁶⁸ Tr. at 761.

⁴⁶⁹ Tr. at 763-65.

⁴⁷⁰ Tr. at 753, 765-68; Ex. I-69 at 86-87.

⁴⁷¹ Tr. at 1016-19; Ex. P-1 at 231.

⁴⁷² Tr. at 753-54, 769-70; Ex. I-69 at 80-81. MBUSA acknowledged that the 2018 increase may have been due to MB Austin's affiliated entity, Continental Auto Leasing, having provided those products to MB Austin's customers in the past. However, Continental Auto Leasing went out of business, so those profits may have moved from that entity to MB Austin in 2018. Tr. at 772-74; Ex. I-69 at 80, 82.

MBUSA asserts that the sales and service opportunity in the Austin AOR will allow for the new dealership to succeed without any measurable losses to MB Austin. However, MBUSA contends that if MB Austin does lose some new vehicle sales or service profit, MB Austin is so diversified in its operations that it will maintain its higher-than-average overall profitability. Additionally, MB Austin is in a good position to compete on price with a new dealer, and price competition benefits consumers. Mr. Hardeman testified that MB Austin is in a good position to compete with new dealerships, that it will likely not go out of business if the new dealership opens, and that it will continue to sell new and used vehicles if the new dealership opens.⁴⁷³ He further acknowledged that MB Austin may capture service business from customers who buy vehicles from the new dealership.⁴⁷⁴ Further, Mr. Swickard testified that he intends to sell to entry-level vehicle customers, which are not the focus of MB Austin's sales.⁴⁷⁵ MBUSA also asserts that carving the South Austin AOI out of the Austin AOR would mean that MB Austin would have higher sales effectiveness in its AOI.⁴⁷⁶

The ALJs find that sufficient opportunity in sales and service exist in the Austin market to support the new dealership without impacting MB Austin. Ms. Heinemann's forensic analysis, taking as true Mr. Stockton's loss estimates, found that MB Austin's diversification and profitability will allow it to compete effectively with a new dealership. MB Austin's arguments regarding potential losses were not supported by the record or relied upon expert testimony and reports that the ALJs find unpersuasive. Therefore, the ALJs conclude that MB Austin will suffer little or no harm from the addition of the new sales point in South Austin and is likely to enjoy some benefits from the addition. Accordingly, this criterion weighs in favor of granting Applicant's application.

⁴⁷³ Tr. at 1383-84.

⁴⁷⁴ Tr. at 1384.

⁴⁷⁵ Tr. at 109.

⁴⁷⁶ Tr. at 475-76; Ex. I-65 at 54.

E. The Public Interest

In demonstrating good cause for approval of an application, an applicant must show that approval of the application is in the public interest.⁴⁷⁷

MB Austin cites to past PFDs to support its assertion that unprofitable dealerships are not in the public interest.⁴⁷⁸ According to MB Austin, reliable proof of the proposed dealership's estimated revenues and expenses as well as reliable proof that the market can support a new dealership are required.⁴⁷⁹ MB Austin also asserts that without an analysis of the number of new vehicles the proposed dealership must sell to break even, harm to the protesting dealer cannot be assessed for purposes of determining the public interest. According to MB Austin, a large volume of entry-level sales is not realistically available to the proposed dealership; therefore, such sales will be taken from MB Austin and MB Georgetown. MB Austin asserts that the only way the new dealership will be profitable is if it takes sales from MB Austin.

MBUSA disputes MB Austin's reliance on the *Lee Trevino* PFD, which was issued in 1984. That PFD discussed the profitability of the existing dealerships rather than the proposed dealership.⁴⁸⁰ MBUSA also disputes MB Austin's claim that the new dealership will not be profitable until some point in the future as there was no evidence to support such a claim. The ALJs agree with MBUSA's reading of *Lee Trevino*. That PFD did not discuss requiring proof of the proposed dealership's estimated revenues and expenses; rather, it discussed the profitability of the existing dealerships. Additionally, MB Austin's assertion that a "large volume" of entry-level sales are not realistically available is vague and not supported by the evidence in the record. Rather, the evidence shows that sufficient lost opportunity, including that of entry-level sales (which MB Austin does not focus on) are available to support the proposed dealership.

⁴⁷⁷ Tex. Occ. Code § 2301.652(a)(5).

⁴⁷⁸ Citing *A.C. Collins Ford*, Proposal for Decision at 22; *Lee Trevino Ford v. Payton Ford Sales, Inc.*, Docket No. 302, Proposal for Decision at 29 (Jan. 30, 1984).

⁴⁷⁹ MB Austin cites to *Lee Trevino Ford*, PFD at 29, 33, for this proposition. However, that PFD does not discuss the need for reliable proof of the proposed dealership's estimated revenues and expenses.

⁴⁸⁰ *Lee Trevino*, PFD at 29.

MBUSA contends that, as discussed above in the factor regarding increasing competition in the marketplace, the addition of the new dealership would benefit the public due to better prices and more convenience. In addition, the public would benefit from job creation from the construction and operation of the dealership, the new tax base created by the sales tax paid on the additional vehicles and parts sales, and the collateral benefits throughout the community. MBUSA also cites to Applicant's track record of good performance with MB and its proven ability to build and manage successful dealerships.

Dr. Nivin projected that construction of the dealership would create 141 full-time jobs with wages and benefits, with a combined direct and indirect impact of \$9.4 million in labor income and a \$12.9 million addition to the Austin gross regional product.⁴⁸¹ Construction would generate an additional \$2.4 million in tax and fee revenues to various federal, state, and local agencies.⁴⁸² When the dealership is operating, it will support 376 full-time equivalent positions for the dealership and indirect businesses, with total earned income of \$21.6 million per year; the dealership is expected to contribute \$66.4 million annually to Austin's gross regional product, with additional annual output to the local economy of about \$150.4 million.⁴⁸³ Dr. Nivin testified that the addition of the dealership will be "an economic positive" that "generates tax dollars, generates employment, generates income, [and] generates economic activity beyond the dealership."⁴⁸⁴ According to MBUSA, these benefits will promote public interest.

MB Austin's assertion that the new dealership can only be profitable by taking sales from MB Austin is unfounded. As discussed above, the Austin market is sufficient to support a new MB dealership without taking sales from the existing dealers. Further, it is in the public interest to have a new dealership stimulating competition in the marketplace, raising brand awareness, promoting price competition, increasing consumer convenience, and enhancing customer service. In addition,

⁴⁸¹ Tr. at 192-94; Ex. I-71 at 34.

⁴⁸² Tr. at 193-4; Ex. I-71 at 34.

⁴⁸³ Tr. at 195; Ex. I-71 at 37-39.

⁴⁸⁴ Tr. at 197.

the Austin community will benefit from the additional jobs and revenue that the new dealership will create. Accordingly, the ALJs find that the addition of the South Austin dealership will be in the public interest, and this factor weighs in favor of MBUSA and Applicant.

F. Harm to Applicant

The next statutory factor to be considered in determining good cause for establishing a dealership is whether denial would result in “harm to the applicant.”⁴⁸⁵

Applicant has invested \$7 million in purchasing the land for the proposed dealership as well as a significant amount of money on consultants and preliminary architectural renderings.⁴⁸⁶ Applicant financed the purchase of the land, so it is paying interest every month on the mortgage.⁴⁸⁷ However, it may be able to recoup the investment if it were to sell the property if the Application is not approved.

MB Austin concedes that Applicant has borrowed funds to acquire the proposed site and paid fees for attorneys and architects. However, MB Austin contends that Applicant will be able to recoup all costs and fees incurred in this matter by selling the proposed location. According to MB Austin, Applicant failed to show that it will suffer any appreciable harm if its application is denied.

As the parties with the ultimate burden of establishing good cause for granting the Application, MBUSA and Applicant bear the burden of showing that Applicant will be harmed if the Application is denied.⁴⁸⁸ Here, they have shown that Applicant might lose some unspecified portion of the total purchase price of the property if the Application is denied; however, Applicant may recoup all of the funds expended in acquiring the land or make even a profit. MBUSA and

⁴⁸⁵ Tex. Occ. Code § 2301.652(a)(6).

⁴⁸⁶ Tr. at 82, 86, 108-10.

⁴⁸⁷ Tr. at 110.

⁴⁸⁸ Tex. Occ. Code § 2301.652(a).

Applicant have also shown that Applicant has incurred some costs and expenses in pursuit of the Application, though they are largely unspecified and entirely unquantified. This evidence is simply too speculative to establish meaningful harm to Applicant.⁴⁸⁹ The ALJs conclude that this factor neither weighs in favor of nor against granting the Application.

G. Projections of Economic Conditions, Financial Expectations, and the Market

The final statutory factor requires the parties to address “reasonably foreseeable projections of economic conditions, financial expectations, and the market for new motor vehicles in the relevant market area.”⁴⁹⁰

The evidence established that Austin has grown significantly over the last decade and its overall population is projected to continue growing in the future. Austin is expected to continue seeing: growth of increases in higher income per household; growth in GDP and, correspondingly, overall income in the economy; growth higher employment and lower unemployment, due in large part to the diversification of the economy and addition of higher-income jobs; and strong growth in income and wages. The evidence further established that Austin will continue to grow despite possible recessions and that Austin’s economy will recover more quickly than other economies if a recession does occur. Austin has experienced gains in luxury vehicle sales since at least 2014, indicating that the market can support an additional MB dealership.

MB Austin concedes that the current and foreseeable projections for economic conditions and market for new vehicles in the Austin market are positive. However, it disputes that the proposed dealership will be profitable. It also contends that sales of the MB brand have been declining nationally and in Texas, at least in part due to MBUSA’s ongoing product and parts supply issues.

⁴⁸⁹ See *Nat. Gas Pipeline Co. of Am. v. Justiss*, 397 S.W.3d 150, 155 (Tex. 2012) (property owner’s testimony on damages must be based on more than intrinsic or speculative value of the property); *McCoy v. Waller Group, LLC*, 05-10-01479-CV, 2012 WL 1470147, at *2 (Tex. App.—Dallas Apr. 26, 2012, no pet.) (party’s conclusory and speculative testimony was legally and factually insufficient to show any damages).

⁴⁹⁰ Tex. Occ. Code § 2301.652(a)(7).

Extensive evidence was presented regarding the current and projected economic growth and diversification and population growth in the Austin market. The evidence established that growth is particularly significant in higher-income households. Therefore, Austin has and will continue to have a large base of luxury vehicles customers. Austin's per capita GDP has grown more strongly, and at a faster rate, than its population.⁴⁹¹ The evidence also established that the Austin economy's diversification and strength positions it to recover quickly from a recession.⁴⁹² Additionally, Austin has low unemployment rates, and the city has been able to absorb its increased population and employ people at higher-than-average incomes.⁴⁹³

Luxury vehicles sales in Austin have risen steadily since at least 2014.⁴⁹⁴ MBUSA asserts that the decision to open a new dealership is a long-term decision.⁴⁹⁵ It is also confident that Applicant can achieve success in Austin similar to what it has achieved in other areas, such as Wilsonville. MBUSA contends that competitive registrations in the South Austin AOI have increased between 2018 and 2019 by 3 percent, further supporting the need for an additional dealership in that area.

Although MB Austin disputes that a new dealership will be profitable, it does not dispute the economic strength of the Austin market. The evidence shows that the Austin economy has historically been strong, has experienced significant growth, and has experienced an increase in the number of potential luxury vehicle buyers for several years. The evidence further established that Austin has historically suffered less and recovered more quickly from nationwide recessions. Therefore, it is likely that the Austin economy will continue growing in the long-term and is well-positioned to recover from a recession. Accordingly, this factor weighs in favor of MBUSA and Applicant.

⁴⁹¹ Tr. at 168-69; Ex. I-71 at 13.

⁴⁹² Tr. at 169-71, 173-76, 183-84; Ex. I-71 at 15-16.

⁴⁹³ Tr. at 172.

⁴⁹⁴ Tr. at 1634-35; Ex. I-67 at 41-42, 43-46.

⁴⁹⁵ Tr. at 250-51.

VI. CONCLUSION

Considering all of the statutory factors discussed above, the ALJs find that Applicant and MBUSA have met the burden of demonstrating good cause for the establishment of the proposed Mercedes dealership in Austin, Texas. Accordingly, the ALJs recommend that the Application be approved.

VII. FINDINGS OF FACT

Procedural Background

1. On July 27, 2018, Swickard Austin, LLC d/b/a Mercedes-Benz of South Austin (Swickard or Applicant) filed a Franchised New Motor Dealer's License Application (Application) with the Texas Department of Motor Vehicles, Motor Vehicle Division (Division) for a license to operate a new Mercedes-Benz (MB) dealership in Austin, Texas.
2. The new dealership would be located at 10900 South IH-35, Austin, Texas.
3. Continental Imports, Inc. d/b/a Mercedes-Benz of Austin (MB Austin), which owns an existing MB dealership in Austin, Texas, filed a protest with the Division on September 21, 2018.
4. On January 17, 2019, the Division referred the case to the State Office of Administrative Hearings (SOAH) for a contested case hearing, and issued a Notice of Hearing to the parties.
5. On March 22, 2019, the Administrative Law Judges (ALJs) issued Order No. 4, setting the prehearing schedule and hearing date.
6. The Notice of Hearing and Order No. 4 contained a statement of the time, place, and nature of the hearing; a statement of the legal authority and jurisdiction under which the hearing was to be held; a reference to the particular sections of the statutes and rules involved; and a short, plain statement of the factual matters asserted or an attachment that incorporated by reference the factual matters asserted in the complaint or petition filed with the state agency.
7. Mercedes-Benz USA, LLC (MBUSA), the exclusive distributor of MB vehicles in the United States, joined the case as an intervenor aligned with Applicant.
8. The hearing on the merits was held November 12-15 and 19-22, 2019, before ALJs Beth Bierman and Stephanie Frazee. At the hearing, MB Austin was represented by its

counsel, William R. Crocker, Leon Komkov, and J. Bruce Bennett; Applicant was represented by its counsel, Jason Allen and Nicholas A. Bader; and MBUSA was represented by its counsel, Lloyd E. Ferguson, Steven M. Kelso, and Gwen J. Young.

9. The parties filed post-hearing briefs. On March 31, 2020, the ALJs denied MBUSA's motion to strike MB Austin's filing of proposed findings of fact and conclusions of law, but granted MBUSA's motion to allow it to file proposed findings and conclusions, which were filed April 17, 2020. By Order No. 13, the record was to have closed April 17, 2020.
10. Starting on April 13, 2020, MB Austin filed several motions requesting official notice of COVID-19 pandemic-related governmental orders and requesting abatement of this case due to the change in economic conditions. The motions were opposed by MBUSA and Swickard. In Order No. 14, issued May 6, 2020, the ALJs granted the request to take official notice of pandemic-related orders issued by Governor Abbott, Mayor Adler, and Travis and Williamson County Judges, denied the request to take official notice of other documents, and denied the motion to abate. The record in this case closed with the issuance of Order No. 14 on May 6, 2020. In Order No. 15, issued July 1, 2020, the ALJs granted the requests to take official notice of additional pandemic-related orders issued by the Texas Governor, but denied MB Austin's motion to reopen the record or to abate this case.

MB Austin

11. MB Austin has been an authorized MB dealer since 1978.
12. Bryan Hardeman, through his corporation, purchased MB Austin with his then-business partner and now owns it with his family. Mr. Hardeman has been the sole dealer-principal of MB Austin since the purchase.
13. In about 1987, MB Austin moved to its current location at 6757 Airport Boulevard in Austin, Texas, which is in central Austin.
14. Approximately 13 years ago, James McGuane became MB Austin's General Manager and has handled its day-to-day operations.
15. Since May 2019, Mr. Hardeman has also been the owner and dealer-principal of MB San Juan in the Rio Grande Valley, Texas.
16. Continental Imports, Inc. also owns a Honda dealership and operates, or has operated, other related businesses including Wholesale Parts Direct and Continental Collision Center, and has operated in conjunction with Mr. Hardeman's other entities such as Continental Auto Leasing.
17. The Hardeman Family Joint Venture owns the MB Austin dealership property.
18. MB Austin is currently building a parking garage for inventory storage, wholesale parts storage, service customer vehicle parking, employee parking, and additional service bays.

19. MB Austin is financially healthy, stable, and profitable, and has been so for many years.
20. Area of responsibility (AOR) is a term used by MBUSA to describe a region that is served by the dealerships in that region. AORs are collections of areas of influence (AOIs) that are connected economically by things like retail shopping and commuting patterns. The Austin AOR extends from Lexington, Texas, to the Highland Lakes area and from south of Temple to approximately Kyle, Texas.
21. AOI is the area surrounding a particular dealership. It is a geographic area defined by a collection of contiguous ZIP codes around the location of a given dealer. ZIP codes are assigned to a given dealer's location by their proximity to the dealer by calculating the closest dealer from the center of a given ZIP code by drive time or drive distance.
22. MBUSA uses a dealership's AOR and AOI to measure the dealer's sales and MB's brand performance.
23. Registration effectiveness is a term that refers to the number of MB registrations in a geographic area. Registration effectiveness relates to the brand's performance.
24. MBUSA measures service performance in its AOIs using the metric Service Opportunity Index (SOI). SOI measures the total non-warranty service performed by any MB dealer for the owners residing in an AOI with one-to-ten-year-old MB vehicles; it therefore measures the service effectiveness of the MB brand, rather than an individual dealer's performance, within an AOI.
25. Sales effectiveness is a term representing the ratio of any individual dealership's reported sales of new MB vehicles to an expected number of sales based on the competitive registrations in that dealer's AOI. Sales effectiveness relates to a dealer's performance.
26. In-sell refers to vehicles sold into an AOI or AOR by dealerships that are outside that AOI or AOR.
27. Market 12 is a term used by MBUSA to refer to the region of the U.S. that includes Austin, Texas.
28. Of the ten AOIs in Market 12, MB Austin's AOI ranked last in registration effectiveness as of June 2019.
29. With the proposed South Austin AOI removed, MB Austin's AOI was the ninth-worst-performing AOI in Texas for registration effectiveness under MBUSA's national standard and the eighth-worst under the Texas standard. The proposed South Austin AOI was the fourth-worst under the national standard and the third-worst under the Texas standard.
30. MB Austin prefers to sell high-end vehicles rather than entry-level vehicles, such as C-Class vehicles, because of the higher profit margins on the more expensive vehicles.

31. Entry-level models, such as the GCL SUV and C-Class sedan are first and second on the list of vehicles that other MB dealers are selling into the Austin AOI. Specifically, 264 vehicles were sold into the Austin AOI, and 98 were sold by MB Austin to a location outside its AOI year-to-date as of the June 2019 monthly dealer report.
32. Nationwide, MB trailed BMW by 5,000 vehicles sold as of June 2019. If the Austin AOI vehicle deficit was removed, the national deficit would be cut by 20 percent.
33. Because sales objectives are lowered for underperforming dealerships, a dealer that is meeting its sales objectives may still be performing inadequately.
34. MB Austin is minimally compliant with MBUSA's brand standards regarding the design, layout, and finishings at its dealership facility but has not upgraded its facilities to a level that would be competitive with MB Georgetown's updated facilities or the new BMW dealership.
35. MB Austin's location is near train tracks and lower-end businesses rather than a high-end retail area, and its location leaves no room to expand other than building upward.
36. MBUSA's monthly SOI reports show the percentage of Serviced VINs in an AOI and the number of MB vehicles in the AOI that were not serviced by an MB dealer (un-serviced vehicles).
37. As of December 2018, of the nearly 12,400 MB vehicles registered in MB Austin's AOI, 4,615 were not serviced within the previous 13 months by any MB dealer. MBUSA estimates the dollar value of lost opportunity to MB dealers of almost \$5.4 million.
38. Of the 7,900 serviced vehicles, MB Austin only serviced 43 percent, leaving 3,900 un-serviced vehicles in the Austin AOI.
39. MBUSA is concerned not just about the lost profit but in the loss of customer loyalty and retention that comes from vehicles being serviced by other providers.
40. MBUSA wishes to attract and retain entry-level customers who are typically younger and at the start of their careers because when such customers are retained, they will purchase more expensive vehicles as time passes.
41. MBUSA views servicing vehicles as a way to maintain customer loyalty and has counseled MB Austin on MBUSA's advertising tools to increase service business. However, MB Austin has declined to take advantage of MBUSA's advertising and marketing plans, in part because MB Austin is at full service capacity and additional customers would increase customer wait times.

42. MB Austin's customers have wait times of 7-10 days or longer for services other than oil changes.
43. MB Austin blames its service wait times on difficulties with software fixes and parts supply from MBUSA. However, such issues affect service providers nationwide and are not specific to MB Austin.
44. MB Austin's service shop is not air conditioned and gets to 85 degrees or more in the summer. MB Austin lost 15-20 percent of its service technicians during the summer of 2019.
45. Traffic patterns give MB Austin a good service location relative to daily commuters, and MB Austin is near employment centers.

Austin Market Study

46. Currently, MB Austin and Mercedes-Benz of Georgetown (MB Georgetown) are the only MB dealerships in the Austin AOR. MB Georgetown is located at the northernmost edge of the Austin AOR.
47. Since at least 2015, MB has underperformed in the Austin AOI in terms of both sales volume and registration effectiveness compared to its three primary competitors: BMW, Lexus, and Audi.
48. As of year-to-date in June 2019, the Austin AOI had only 458 total MB vehicles registered, and 330 of those sales were MB Austin, compared to registrations of 925 BMWs, 912 Lexuses, and 665 Audis in the same time period.
49. MBUSA performs better nationally and regionally than it does in the Austin AOI. In MBUSA's Southern Region, year-to-date as of September 2019, MB outsold BMW by 2,700 vehicles and only fell behind BMW nationally in 2019 by 5,000 units (500 of which are in the Austin AOI).
50. Based on national registration data, the expectation for MB in 2018 in the Austin AOR was 2,006 vehicles registrations, but there were only 1,581. Statewide, MB only had a shortfall of 300 vehicle registrations for Texas in 2018.
51. The MB brand has performed below average in the Austin market for at least the last five years. MBUSA determined that a third dealership is needed in the Austin AOR to have the same percent of competitive dealerships as it has in the other markets.
52. From 1978 until 2004 or 2005, when MB Georgetown relocated from Temple to the north edge of the Austin metro market, MB Austin was the only dealer in the Austin market. During that time, the population of Austin more than doubled from about 585,000 people in 1980 to 1.25 million in 2000.

53. From 2000 to 2017, the Austin population grew to approximately 2.1 million people.
54. Population growth in Austin since 2011 has been very strong both as to total population and population within the ages of 18-65 and has been stronger than other major Texas metro areas from 2011-2018.
55. Projections by the Texas Demographic Center predict that Austin will continue to have the strongest population growth compared to other major metro areas in Texas through 2034.
56. Between 2001 and 2017, Austin's gross domestic product (GDP) more than doubled from \$62 billion to \$135 billion. That time period included the 2008 recession and subsequent recovery.
57. Austin's GDP growth rate has averaged 5 percent since 2002, and averaged 6.4 percent from 2010-2017. By contrast, the next-highest rate in a Texas metro area is San Antonio, which has averaged 3.7 percent GDP growth since 2002. United States GDP growth has averaged 2.5 to 3 percent each year.
58. Austin's per capita GDP has grown from \$47,169 in 2001 to \$65,839 in 2017.
59. Employment in Austin has grown from 387,000 jobs in 1990 to over one million in 2019, for an average annual rate of 3.63 percent, which is a stronger rate of growth than any other Texas metro area.
60. Unemployment rates since 1990 have averaged 4.2 percent annually in Austin, 5.8 percent in Texas, and 5.9 percent in the U.S.
61. Austin's economy has become more diversified over the past 30 years and has increased the number of higher paying jobs, leading to higher household incomes and declines in the number of lower household incomes. The highest growth in household incomes has been in the highest income strata of \$200,000 and above per household, which means greater growth in the luxury car-buying population.

Addition of a New South Austin Point

62. To keep up with increasing competition from other luxury brands, MBUSA continually evaluates the U.S. on a market-by-market basis by looking at the performance of the brand and each dealer, applying analytics to data such as registrations, demographics, and other market-specific data.
63. Since 2001, MBUSA's network has grown from 320 dealers to 384, covering 220-240 of the U.S.'s approximately 800 markets.
64. During that same time period, MBUSA's national sales of MB vehicles has more than doubled, the number of exclusive MB dealerships has doubled, the MB vehicle product

line has broadened significantly and become more complex, and customer expectations have increased and become more sophisticated.

65. MB dealers are selling twice the volume of vehicles as in 2001, and average dealer throughput (the number of new vehicles sold per dealer) and the average number of vehicles serviced per dealership have grown significantly.
66. Also since 2001, new luxury brands have been introduced in the market (Lexus, Acura, Infiniti, and Hyundai's Genesis brand as well as Land Rover and Audi), which have increased competition in the market.
67. In order to meet competition, MBUSA desires to add a dealership in South Austin as part of a larger planning and assessment process in connection with MBUSA's parent company Daimler's worldwide MB 2020 program.
68. MB 2020 began in anticipation of Daimler's planned large-scale introduction of new vehicle models in segments in which it had never competed and large increases in volumes of most existing models.
69. As part of an initiative referred to as MB 2020, MB's parent company, Daimler, began analyzing markets across the United States to determine where the brand needed to expand.
70. Daimler has developed and has introduced included new vehicles in the segments for entry-level luxury sedans (like C- and A-Class sedans) and SUVs (like GLA and GLB SUVs).
71. The intent of entering these new vehicle segments was to attract younger, less affluent buyers at a price point they could afford, and to gain their loyalty through having their vehicles serviced at MB dealerships.
72. Entry-level luxury segments are becoming a more competitive part of the luxury marketplace, and Daimler views it as important to have in place a dealer network that supports the corporate goal of reaching and successfully conquering entry-level luxury buyers from other brands.
73. Daimler also desires to increase customer satisfaction and convenience by shortening distances to MB dealerships and by increasing the capacity of the dealer network to satisfy the service needs of customers.
74. MB's goal is to achieve an optimal dealer network in the markets where it chooses to have representation.
75. An optimal dealer network is one with the proper number of dealerships, dealerships in the right location, and the best dealer partners representing the brand.

76. MB identified the Austin market as one where MB was lagging behind its competitors in terms of sales and customer convenience. MB has viewed Austin as subpar for years in the context of Austin's population growth, particularly of higher-income households.
77. In 2014, MBUSA's executive Network Review Committee (NRC) decided to add a dealer in the Austin metro area. The NRC approved Berkshire Hathaway Automotive (Berkshire Hathaway) as its candidate for the dealership.
78. In September 2016, MBUSA approved the candidate's proposed site at 10900 South IH-35 due to the availability of land and appropriate zoning there, its close proximity to MBUSA's competitors (including BMW), proximity to a major highway, and being central to the area of the most lost sales to its competitors. MBUSA gave notice to the existing dealers of its planned establishment of a new dealer, and MB Austin protested.
79. The distribution of luxury vehicle registrations in the AOR has its highest density between MB Austin and the proposed South Austin site.
80. Berkshire Hathaway ultimately withdrew when it was unable to obtain a dealership license under Texas Occupations Code § 2301.476, which prohibited it from owning dealerships in Texas because it was also a manufacturer of recreational vehicles.
81. On July 13, 2018, Mr. Hardeman sent a letter to MBUSA requesting to be the candidate for a new dealership located in southwest Austin. MBUSA did not consider Mr. Hardeman for the new point.
82. Jeff Swickard had expressed interest in a dealership in Austin to MBUSA's then-CEO Dietmar Exler in 2017. When Berkshire Hathaway withdrew, Mr. Exler proposed Mr. Swickard as the candidate for the South Austin dealership.
83. In December 2017, The NRC approved Mr. Swickard as its candidate for the South Austin dealership. Mr. Swickard entered into a letter of intent with MBUSA in April 2018, and after reviewing various locations, he purchased Berkshire Hathaway's property on South IH-35.
84. In the South Austin AOI, existing luxury-brand owners must drive an average of 20.7 miles to the nearest MB dealer, compared to 15.1 miles to a BMW dealer, 15.6 miles to an Acura dealer, 15.8 miles to an Audi dealer, and 17.7 to a Lexus dealer.
85. The proposed new dealership has ready access and visibility from the I-35 thoroughfare, is next to a Volkswagen dealership, and has appropriate land area and zoning to accommodate the dealership.
86. The new location would cover many of the areas where un-serviced MB vehicles are located.

Swickard Dealerships

87. Applicant is an entity owned and operated by Mr. Swickard.
88. Mr. Swickard, through various other entities, owns and operates nine dealerships, three of which are MB dealerships: Mercedes-Benz of Wilsonville (MB Wilsonville) in a suburb of Portland, Oregon; Mercedes-Benz of Seattle, Washington; and Mercedes-Benz of Atlanta South, Georgia.
89. Before becoming involved in car dealerships, Mr. Swickard worked in telecommunications and owned his own telecommunications company.
90. Mr. Swickard lived in Austin from 2006 until 2011 or 2012.
91. After Mr. Swickard sold his telecommunications company, he purchased MB Wilsonville in 2014.
92. Mr. Swickard was nominated by other MB dealers to represent them on the MBUSA National Dealer Board in 2017 and has been elected by his national dealer peers to be the Chair of the Board.
93. The MB Wilsonville facility exceeds MBUSA's requirements in terms of high-end amenities, fixtures, and finishes.
94. After Mr. Swickard purchased MB Wilsonville, he turned the Portland metro market around from underperforming to number one in terms of registration effectiveness, exceeding sales performance expectations, and ranking 28th of 384 dealers on key metrics.
95. Mr. Swickard hired the Ritz-Carlton Hotel Company to teach his employees about hospitality.
96. A facility in South Austin similar to the Wilsonville dealership would improve the brand image of MB in the Austin AOR.
97. Mr. Swickard's MB dealerships focus on attracting entry-level customers in order to grow business and gain new customers.
98. Mr. Swickard made efforts to make MB vehicles more affordable by selling cars that had been used as loaner vehicles and other nearly-new vehicles that can be sold for less than brand-new vehicles. Such sales have also allowed his dealerships to grow their service departments, and that service is more profitable than sales of new cars.
99. Mr. Swickard intends to be personally involved in the dealership and to spend as much time as he can in Austin.

100. Mr. Swickard plans for the South Austin dealership to have air-conditioned service bays, but the dealership will not have a body shop.
101. Mr. Swickard intends for the South Austin facility to be as well-designed as the new BMW dealership located nearby.

Adequacy of Representation

102. Nationwide, MB sales exceed those of its primary competitors (BMW, Lexus, and Audi); however, MB vehicle registrations have lagged behind its competitors in the Austin AOI.
103. MB has underperformed compared to its competitors in terms of sales volume and registration effectiveness in the Austin AOI since 2012.
104. MB Austin's AOI ranks tenth out of the 10 Market 12 dealers in registration effectiveness.
105. MB as a brand has fallen further behind in 2018 and 2019 since BMW opened its South Austin dealership in 2018.
106. As of year-to-date in June 2019, MB Austin registered 330 vehicles in its AOI, compared to 925 by BMW, 912 by Lexus, and 665 by Audi.
107. MB is being outsold by its primary competitors particularly in lower-priced entry-level luxury vehicles, such as the C-Class sedan and GLC SUV segments (48 MB C-Class versus 148 for BMW, 209 for Lexus, and 83 for Audi).
108. MB Austin prefers to sell higher-end vehicles because of the higher profit margins.
109. Focusing on selling higher-end vehicles is not an effective approach to meet MB's competition in the Austin AOI.
110. In the Southern Region as of September 2019, MB outsold BMW by 2,700 vehicles and trails BMW nationwide by 5,000 units (almost 500 of which are in the Austin AOI).
111. MB is underperforming in the Austin AOI compared to its regional and national performance.
112. Based on national registration levels, the expected number of MB vehicle registrations in the Austin AOI for 2018 was 2,006, but there were only 1,581 registrations, for a shortfall of 425.
113. MB's registration effectiveness in the Austin AOR was 78.8 percent, with 100 percent representing "average" registration effectiveness.
114. MB Austin's sales effectiveness has been below 100 percent since at least 2012.

115. 100 percent sales effectiveness represents achieving average sales effectiveness.
116. MB Austin was at 75.6 percent registration effectiveness in 2018, and as of September 2019, MB Austin was at 75 percent sales effectiveness.
117. MB Austin's AOI ranked tenth out of the ten regional dealers' AOIs in registration effectiveness as of June 2019.
118. The proposed South Austin dealership AOI is the ninth lowest Texas AOI under the national standard and the eighth lowest under the Texas standard, and it has the fourth lowest registration effectiveness under the national standard and the third lowest under the Texas standard.
119. MB Austin had 61.6 percent sales effectiveness in 2015, 71.1 percent in 2017, and 62.8 percent in 2018.
120. The Austin market consistently performs below average in terms of sales effectiveness, whether compared to the national or Texas average.
121. In order for MB to achieve the same "share of franchises" compared to other luxury dealers in Austin as it has nationally, it needs three dealerships in the Austin area.
122. MB Austin is not adequately capturing the lost service opportunity in its AOI.
123. MB Austin's AOI was below every benchmark (national, regional, area, market, market tier) as of December 2018 for service.
124. A lack of supply of certain vehicles experienced by MB Austin affected dealers nationwide and therefore does not explain why MB Austin would fall below national benchmarks.
125. Although MB Austin is in the process of building additional service bays, it is currently at capacity in its service department, and its customers experience longer-than-average wait times for services other than oil changes.
126. MB Austin's new service bays may not solve MB Austin's problem retaining service technicians, which has also led to longer wait times.
127. MB Austin's facility is minimally compliant with the MB brand requirements image, but minimal compliance is not sufficient to compete with other facilities such as MB Georgetown and the new South Austin BMW dealership.
128. MB Austin's service bays are not air conditioned, whereas competitor dealerships have air conditioning, which could contribute to MB Austin's difficulty in retaining service technicians.
129. MB Austin's location is no longer a desirable part of town for a luxury car dealership.

130. MB Austin is not adequately representing the MB brand in terms of sales. Accordingly, this factor weighs in favor of the new dealership.

Substantial Compliance with Dealer Agreement

131. MBUSA has not sent any franchise noncompliance or cure notices concerning any sales performance contractual obligations to MB Austin.
132. MBUSA recently renewed MB Austin's franchise agreement and approved MB Austin's purchase of the San Juan MB dealership in May 2019.
133. MB Austin has failed to achieve 100 percent sales effectiveness.
134. MB Austin has received dealer bonuses for achieving 80 percent sales effectiveness in the past.
135. MB Austin achieved 61.6 percent sales effectiveness in 2014, increasing to 71.1 percent in 2017, and decreasing to 62.8 percent in 2018. As of September 2019, MB Austin had about 75 percent sales effectiveness.
136. The franchise agreement between MB Austin and MBUSA was not introduced into evidence.
137. The evidence failed to establish that achieving 100 percent sales effectiveness is a contractual requirement in the franchise agreement between MB Austin and MBUSA.
138. This factor neither weighs for or against granting the application.

Desirability of Competitive Marketplace

139. The establishment of a new dealership increases price competition both within and between brands.
140. Having an additional dealer in the market provides choice to consumers, particularly on pricing, allowing consumers to cross-shop (shop the price for a given model or type of vehicle between brands at multiple dealerships).
141. The Austin luxury-vehicle market is extremely competitive.
142. MBUSA did not need to obtain a dealer application, business plan, balance sheet, break even analysis, or other financial projections from Applicant in order to determine whether the new dealership will further healthy competition.
143. Based on the untapped sales and service opportunity in the Austin AOR, Applicant can run a successful dealership in Austin without being "subsidized" by the existing dealers.

144. Healthy competition results in increased intra- and inter-brand competition; more competitive prices; enhanced customer purchase and service experience and satisfaction. Health competition also provides additional, convenient location(s) near the brand's competitors to enhance cross-shopping and convenience for consumers.
145. Healthy competition is promoted by facilities that are modern and that increase inventory in the market by providing more and better selection of the manufacturer's products.
146. A new dealership will increase consumer choice and brand advertising in the Austin market.
147. The proposed South Austin site will meet the requirements necessary to increase competition because it is an underrepresented area for the brand, it has recent and projected population growth, and it includes a large distribution of higher-income households. Commercial and residential development is booming in the area, and the location is convenient for customers.
148. Applicant has a history of increasing market competition to consumers' benefit, as he did in turning around the Wilsonville market.
149. Applicant markets to and attracts entry-level luxury customers to whom MB Austin does not market. However, MB's competitors are marketing to this demographic and outselling MB Austin in entry-level segments.
150. Establishment of the new South Austin dealership will increase advertising for the MB brand, increase the availability of inventory in the market, increase access to the MB brand, increase convenience of service, and increase choice and competitive pricing for consumers.
151. The proposed site in South Austin is in a growing part of the city where MB is poorly represented, it is convenient to consumers, and it is located near other luxury vehicle dealers, such as the new BMW dealership.
152. Applicant has a track record of operating successful dealerships and working well with other MB dealers, rather than "cannibalizing" sales from them.
153. MB Austin is a highly profitable dealership that is in good position for competing in the market.
154. Opening the new dealership will promote healthy competition in the marketplace, and this factor weighs in favor of granting the Application.

Harm to Protesting Dealer

155. An existing dealer is not necessarily harmed because it must share the market with a new dealership, even if it experiences some profit loss after expansion of the dealer network.
156. Millions of dollars of lost service opportunity will be available to the new dealership without the need to take any service business from MB Austin.
157. The percentage of MB vehicles serviced by MB dealers in the Austin AOI was below the metro average as well as other benchmarks.
158. MB Austin should keep its service business if the new dealership opens.
159. There is more service work in Austin than MB Austin can handle.
160. MB Austin should not experience any lost sales because the new dealership can capture opportunity existing in the market such as lost registrations in the South Austin AOI and in-sell of entry-level vehicles.
161. As of 2018, a total lost opportunity of 755 sales (474 units of gross loss and 281 units of in-sell) existed in the Austin AOR.
162. Most luxury brands examine markets at the ZIP code level.
163. The distribution of loss in an AOR is not random, rather, calculating loss by ZIP code takes into account the actual registrations in that area as well as demographics and locational issues to show where losses are occurring.
164. MB is experiencing loss due to the new South Austin BMW dealership.
165. Based on the sales patterns of MB Austin and MB Georgetown, the new dealership is projected to sell from 500-700 new vehicles per year.
166. That range is below the total lost opportunity of 755 units in 2018, thus the new dealership need not take any sales from the existing dealers.
167. MB Austin is so profitable and financially successful, it can withstand competition from an additional dealer.
168. Every year since 2015, MB Austin's net profit has exceeded the benchmark composite groups.
169. As of 2018, MB Austin had no long-term debt; it had a cash position of \$4.6 million, a net cash position of nearly 600 percent, and working capital of 200 percent of what MBUSA requires for a healthy dealership; its net profit for 2018 exceeded its total net fixed assets after depreciation (\$5.6 million versus a little under \$4 million); and MB Austin's return on equity is very high and far exceeds the average of the composite groups.

170. MB Austin's profitability is not dependent on its new-vehicle sales volume. Specifically, in 2018, MB Austin's profit increased from \$4.7 million to \$5.6 million, despite selling 16 percent fewer new vehicles.
171. MB Austin generates a higher amount of revenues from its fixed operations (service, parts, and body shop departments) than the benchmark groups, and the profit margins in fixed operations are much higher than those in the new or used vehicle departments.
172. MB Austin's net profit in its fixed operations exceeds all of its fixed expenses by 1.72 times, which is more than the composite groups.
173. MB Austin is in a better financial position than most dealerships because fixed operations are more recession-proof than vehicles sales: if customers are not buying new cars, then they will need to have their old cars serviced.
174. Because its net profit from fixed operations fully covers its fixed expenses, MB Austin has more flexibility in its new and used vehicle departments.
175. MB Austin has a large used vehicle department with higher profit per vehicle than the benchmark groups.
176. In 2018, MB Austin made a higher profit than previous years on its finance, insurance, and service contract products with its new car sales while maintaining its higher-than-average gross profits on new vehicles.
177. MB Austin has had higher than average gross profit on sales of new vehicles, charging more for vehicles than its peers on an average per unit basis.
178. In 2018, MB Austin increased its gross profit on finance, insurance, and service contract products sold with new vehicles.
179. MB Austin can easily adjust its business strategy to meeting additional competition and capture untapped opportunity in the market.
180. Carving the South Austin AOI out of the Austin AOR would mean that MB Austin would have higher sales effectiveness in its new, smaller AOI.
181. Bonuses paid by MB to its dealerships are generally earned by activities other than new vehicle sales by meeting other standards; by meeting those standards, MBUSA pays the incentive as a percentage of the price on every new vehicle sold.
182. The only bonus related to new vehicle sales is tied to scores such as sales effectiveness, which represented 14 percent of the 2017 incentives, and MB Austin was already performing poorly on that score.

183. Because the new South Austin AOI will allow MB Austin to become more sales effective by making its AOI smaller, the chances increase that MB Austin would do well on that bonus measure.
184. Edward Stockton, MB Austin's expert witness, estimated that MB Austin would experience a 20 to 30 percent profit loss as a result of the new dealership. However, his estimate does not account for economic and population growth in Austin and is based on non-statistically significant calculations.
185. Mr. Stockton's gravity model exaggerates predicted impact on existing dealers when applied to real world examples of other markets with recently established new dealerships. The model overstates impact to existing dealerships by 30 to 40 percent.
186. Mr. Stockton admitted that his gravity model did not accurately capture MB Austin's performance in its fixed operations.
187. Mr. Stockton's report consists of a 17-page narrative with almost 300 pages of exhibits. Many of the calculations in the exhibits are presented without explanation or support, either in the report or his testimony. Similarly, many of his estimates are not supported by calculations.
188. Mr. Stockton's calculation of loss that aligned with that of MBUSA's expert, Suzanne Heinemann, was disregarded in his report, and he instead focused on a statistically non-significant result that he doubled from 12.37 percent to 25 percent.
189. Neither Mr. Stockton nor Dr. John Hatch, another of MB Austin's experts, used methodologies that have been accepted by the automotive industry or the Board, and their chosen methodologies are not improvements upon the accepted methodologies used by Ms. Heinemann and Sharif Farhat, MBUSA's expert witnesses. Rather, those methodologies do not hold up when tested in real-world examples of new dealership establishments.
190. Sufficient opportunity in sales and service exist in the Austin market to support the new dealership without impacting MB Austin.
191. MB Austin's diversification and profitability will allow it to compete effectively with a new dealership.
192. MB Austin will suffer little or no harm from the addition of the new sales point in South Austin and is likely to enjoy some benefits from the addition.
193. Accordingly, this criterion weighs in favor of granting Applicant's application.

Public Interest

194. The addition of the new dealership would benefit the public due to better prices and more convenience.

195. The public would be benefited by job creation from the construction and operation of the dealership, the new tax base created by the sales tax paid on the additional vehicles and parts sales, and the collateral benefits throughout the community.
196. Applicant has a history of good performance with MB and an ability to build and manage successful dealerships.
197. Construction of the dealership would create 141 full-time jobs with wages and benefits with a combined direct and indirect impact of \$9.4 million to the local economy. Construction will also add \$12.9 million to the Austin gross regional product.
198. Construction would generate an additional \$2.4 million in tax and fee revenues to various federal, state, and local agencies.
199. When the dealership is operating, it will support 376 full-time equivalent positions for the dealership and indirect businesses, with a projected total earned income of \$21.6 million per year. This would contribute about \$66.4 million annually to Austin's gross regional product, with an additional annual output to the local economy of about \$150.4 million.
200. The new dealership will promote the public interest by stimulating competition in the marketplace, raising brand awareness, promoting price competition, increasing consumer convenience, and enhancing customer service.
201. The Austin community will benefit from the additional jobs and revenue that the new dealership will create.
202. Customers will benefit by the convenience of a shorter drive to reach an MB dealer.
203. The addition of the South Austin dealership will be in the public interest, and this factor weighs in favor of granting the Application.

Harm to Applicant

204. Mr. Swickard has invested \$7 million in purchasing the land for the proposed dealership as well as a significant amount of money on consultants and preliminary architectural renderings.
205. Mr. Swickard financed the purchase of the land, so he is paying interest every month on the mortgage.
206. Mr. Swickard may be able to recoup his investment in the property if he were to sell the property if the application is not approved.
207. The evidence is too speculative to establish any likely harm to Applicant if the Application is denied.

208. This factor of harm to the applicant neither weighs in favor of or against granting the Application.

Economic Projections

209. Austin has grown significantly over the last decade and its overall population is projected to continue growing in the future.

210. Austin's growth is projected to be particularly strong in increases in higher income per household; in GDP and overall income in the economy; trends in employment and unemployment, due in large part to the diversification of the economic, particularly in higher income jobs; and in income and wages.

211. The evidence established that Austin is expected to continue growing despite projected recessions, and the Austin economy is expected to recover more quickly than other economies if a recession occurs.

212. The Austin economy suffered less and rebounded more quickly than other city economies during and after the 2008 recession.

213. The Austin economy has become further diversified and recession-proof since 2008.

214. Austin's economy is expected to grow in the long-term.

215. Austin has experienced gains in luxury vehicle sales since at least 2014, indicating that the market can support an additional MB dealership.

216. Austin's economic growth is particularly significant in higher-income households. Therefore, Austin has and will continue to have a large base of luxury vehicles customers.

217. Austin's per capital GDP has grown more strongly, and at a faster rate, than its population.

218. The Austin economy's diversification and strength positions it to recover quickly from a recession.

219. Austin has low unemployment rates, and the city has been able to absorb its increased population and employ people at higher-than-average incomes.

220. Luxury vehicles sales in Austin have risen steadily since at least 2014.

221. MB's decision to open a new dealership is a long-term decision based on projections of population and economic conditions in the future.

222. Competitive brand registrations in the South Austin AOI have increased between 2018 and 2019 by 3 percent, further supporting the new for an additional dealership in that area.

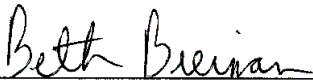
223. The Austin economy has been strong and growing and the number of potential luxury vehicle buyers in the area has increased for many years. Despite projected recessions, the Austin economy is expected to continue growing in the long-term. Accordingly, this factor weighs in favor of MBUSA and Applicant.

VIII. CONCLUSIONS OF LAW

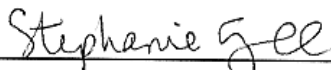
1. The Division has jurisdiction and authority over the subject matter of this case. Tex. Occ. Code ch. 2301, sub ch's. N, O.
2. SOAH has jurisdiction over all matters relating to the conduct of a hearing in this matter, including the preparation of a proposal for decision with findings of fact and conclusions of law. Tex. Occ. Code § 2301.704; Tex. Gov't Code ch. 2003.
3. Notice of the Application was properly provided. 43 Tex. Admin. Code § 215.105.
4. Protestant timely filed its notice of protest. 43 Tex. Admin. Code § 215.106.
5. Notice of Hearing was properly provided. Tex. Occ. Code §§ 2301.705, .707; Tex. Gov't Code §§ 2001.051-.052; 43 Tex. Admin. Code § 215.307.
6. MB Austin has standing to protest Applicant's application. Tex. Occ. Code § 2301.652(b).
7. Applicant has the burden of showing by a preponderance of the evidence that good cause exists for the establishment of a dealership. Tex. Occ. Code § 2301.652(a); 1 Tex. Admin. Code § 155.427.
8. The MB product lines are not being adequately represented as to sales and service in the Austin AOR. Tex. Occ. Code § 2301.652(a)(1).
9. MB Austin is in substantial compliance with its dealer franchise agreements. Tex. Occ. Code § 2301.652(a)(2).
10. A new MB dealership in South Austin will promote healthy inter-brand and intra-brand competition in the relevant markets. Tex. Occ. Code § 2301.652(a)(3).
11. Establishing a new MB dealership in South Austin will not cause MB Austin to suffer significant harm. Tex. Occ. Code § 2301.652(a)(4).
12. Establishing a new MB dealership in South Austin is in the public interest. Tex. Occ. Code § 2301.652(a)(5).
13. The evidence failed to establish that Applicant will be harmed if the Application is denied. Tex. Occ. Code § 2301.652(a)(6).

14. Current and reasonably foreseeable projections of economic conditions, financial expectations, and the market for new motor vehicles in the relevant market area favor the establishment of a new MB dealership in South Austin. Tex. Occ. Code § 2301.652(a)(7).
15. Applicant met its burden of demonstrating good cause for the establishment of the proposed MB dealership in South Austin. Tex. Occ. Code § 2301.652(a).
16. Applicant's application for a new dealership should be granted.

SIGNED July 2, 2020.



BETH BIERMAN
ADMINISTRATIVE LAW JUDGE
STATE OFFICE OF ADMINISTRATIVE HEARINGS



STEPHANIE FRAZEE
ADMINISTRATIVE LAW JUDGE
STATE OFFICE OF ADMINISTRATIVE HEARINGS

FILED
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7/24/2020 11:07 AM
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Jessie Harbin, CLERK

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MVD DOCKET NO. 19-0005 LIC

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Jessie Harbin, CLERK

STATE OFFICE OF ADMINISTRATIVE HEARINGS

SWICKARD AUSTIN, LLC D/B/A MERCEDES-BENZ OF SOUTH AUSTIN,
Applicant,

MERCEDES-BENZ USA, LLC,
Intervenor,

v.

CONTINENTAL IMPORTS, INC. D/B/A MERCEDES-BENZ OF AUSTIN,
Protestant.

PROTESTANT’S EXCEPTIONS
TO THE PROPOSAL FOR DECISION

TO THE HONORABLE ADMINISTRATIVE LAW JUDGES:

Continental Imports, Inc. d/b/a Mercedes-Benz of Austin (“Protestant” or “MB Austin”) respectfully submits the following exceptions to the proposal for decision (“PFD”) issued on July 2, 2020, recommending the granting of the license application of Swickard Austin, LLC d/b/a Mercedes-Benz of South Austin (“Applicant” or “Swickard”) to establish a franchised Mercedes-Benz dealership in the Austin metropolitan market.

1. Your Honors took official notice of the state and local governmental orders issued in response to the COVID-19 pandemic, which began in March 2020, and continues to rage in central Texas and other parts of the U.S. But your Honors refused to take official notice or additional testimony concerning the adverse

economic impact of the pandemic on the economy and the motor vehicle market in Texas and the Austin Area of Responsibility (“AOR”).

Throughout the PFD, your Honors cite and rely on economic and market data from 2017, 2018, and portions of 2019. *See e.g.*, PFD at pp. 24-25, 28, 77-78; Findings of Fact Nos. 209-223. Your Honors also emphasize both MBUSA’s intent to attract younger, less affluent, entry-level buyers to the MB brand and Swickard’s plan to target those potential buyers in the Austin AOR. *See e.g.*, PFD at pp. 13, 18, 19, 22, 73, 97; Findings of Fact Nos. 40, 71, 72, 160).

Protestant excepts to your Honors’ refusal to consider the impact and consequences of the COVID-19 pandemic on market conditions and especially on those younger, less affluent buyers. By refusing to consider the impact of the COVID-19 pandemic, this Court has excused Swickard’s total failure to produce any evidence concerning if or when its proposed dealership can achieve profitability by selling MB vehicles in this altered economy without having to live off the existing MB dealers—primarily Protestant.

The COVID-19 pandemic has rendered , outdated and stale the economic data and the market data and projections on which this case was tried. The unprecedented impact of the pandemic on the economy necessitates the taking of additional evidence concerning current and projected motor vehicle market conditions, economic conditions, and financial expectations of the proposed dealership. The economic consequences of the COVID-19 pandemic are not comparable to an ordinary business

recession but have created a “new normal” with a significantly changed and depressed economy.

Your Honors now do not have the authority to reopen the evidentiary record. However, you are authorized to amend the PFD and recommend that the Board remand this case for the taking of evidence concerning the impact of the COVID-19 pandemic on the good cause factors of adequacy of representation, a competitive marketplace, harm to Protestant, the public interest, and current and reasonably foreseeable projections of economic conditions, financial expectations, and the market for new motor vehicles in the Austin AOR. Your Honors should do so.

2. Board precedent establishes that the ultimate findings on the good cause factors of adequacy of representation, harm to the protesting dealer, a competitive marketplace, and the public interest largely depend on whether the amount of lost opportunity for a brand in a market area is large enough to profitably support both the brand’s proposed new dealership and its existing dealerships.

In *Landmark Chevrolet v. General Motors Corp.*, Docket No. 02-0002 (Dec. 9, 2004) (final order), the Board ruled that the standard for measuring lost opportunity for a brand in a market is the lost opportunity that can be “realistically” or “reasonably” captured by the brand’s existing and proposed dealers.

Protestant excepts to your Honors’ violation of the Board’s *Landmark Chevrolet* decision by measuring lost sales opportunity and lost service opportunity for the MB brand as that which is *theoretically* available for capture rather than that which is *realistically* available for capture.

Regarding sales, your Honors have accepted MBUSA's lost opportunity numbers of 474 units of gross loss and 281 units of insell in the Austin AOR as the measure of the lost opportunity available for capture by the MB dealers in the AOR. Your Honors further accept the false assumption that the proposed Swickard dealership can capture all of the theoretically available lost sales opportunity and thus avoid taking sales away from Protestant.

But not all of these units of lost opportunity are realistically available for capture by the MB dealers. The Board repeatedly recognized this fact in *Landmark Chevrolet* and rejected as "pie-in-the-sky optimism" the assumption that all gross loss and insell in the market area was available for capture by the brand's dealers. See *Landmark Chevrolet*, PFD at pp. 25, 26, 27, 61 [Finding of Fact Nos. 168, 173-178], 63 [Finding of Fact Nos. 191-194], 64 [Finding of Fact No. 207-209].¹ The evidence in this case was undisputed that gross loss and insell will remain in the Austin AOR even if the MB brand were to exceed 100% of its expected share of the Austin AOR. *This is true for every AOR in Texas.* (Ex. I-65 @ 096, Ex. I-66 @ 033, Ex. P-1 @ 241; Tr. 570:22-571:6, 1160:22-1161:7, 1199:1-20). Thus, your Honors' acceptance of a model that provides for capture of all gross loss and insell is erroneous and contrary to Board precedent.

¹ For your Honors' convenience, Protestant attaches highlighted excerpts from the *Landmark Chevrolet* decision in the Appendix to these Exceptions behind Tab 1. A complete copy of the *Landmark Chevrolet* decision is included in Volume 1 of the Appendix to Protestant's Response and Closing Statement behind Tab 6.

Neither Swickard nor MBUSA produced any evidence that gross loss or insell in the Austin AOR is unusually high; nor did they calculate the number of units of gross losses or insell that would be expected to remain in the Austin AOR if the proposed Swickard dealership were established.

The Board's *Landmark* decision emphasized the importance of knowing the level of "normal" insell in the market and the applicant's penetration profile in determining the amount of lost opportunity that is reasonably available for capture, which there was within a 20-mile radius of the proposed dealership. *Landmark Chevrolet*, PFD at pp. 25, 26, 61 [Finding of Fact Nos. 173-178], 63 [Finding of Fact Nos. 191-194]. Neither Swickard nor MBUSA developed a penetration profile for the proposed dealership based on its South Austin location and on its plan to target younger, less affluent, entry-level customers. Swickard and MBUSA simply assumed a penetration profile based on the expected retail registrations of Protestant (located in the central Austin AOR) and MB of Georgetown (in the northern Austin AOR) within 40 miles of the proposed dealership's South Austin location. (Ex. I-65 @ 098). But Swickard and MBUSA did not adjust for the gross loss and insell located outside this 40-mile radius. (Ex. I-65 @ 096, 097). Nor did Swickard and MBUSA make any adjustment to the gross loss and insell numbers to account for units of gross loss and insell that would normally remain in the Austin AOR even if the Swickard dealership were established and the MB brand exceeded 100% of its expected market share.

As a result, the lost opportunity figure of 755 units accepted by your Honors is inflated and makes your Honors' proposed findings on adequacy of representation, harm to Protestant, the desirability of a competitive marketplace, and the public interest unreliable. *See Landmark Chevrolet*, PFD at pp. 25, 26, 61 [Finding of Fact Nos. 175-177], 63 [Finding of Fact Nos. 191-194].

Regarding lost service opportunity, your Honors overlook the undisputed fact that no market area or region in the United States is achieving more than about 70%-71% of the service business theoretically available to MB dealers. (Ex. I-25, Ex. I-26, Ex. P-26, Ex. P-27, Ex. P-28, Ex. P-29, Ex. P-61, Ex. P-62). The Service Opportunity Index ("SOI") reports in evidence—on which MBUSA relies to determine service opportunity—conclusively show that Protestant and MB of Georgetown are capturing all of the MB service business that is realistically available for capture by the existing MB dealers in Protestant's AOI. Your Honors focus and rely on the December 2018 SOI report (Ex. I-26), but disregard the most recent SOI reports (Ex. I-25, Ex. P-26, Ex. P-27, Ex. P-28, Ex. P-29, Ex. P-61, Ex. P-62) showing that Protestant's AOI is capturing service business at a higher rate than MB's national, regional, area, market, or market tier averages. Why your Honors ignore 2019 SOI reports is unexplained and mystifying, particularly given your Honors' emphasis on Protestant's sales performance in September 2019 and October 2019. *See* PFD at pp. 10, 11 51, 52, Finding of Fact Nos. 49, 110, 116.

Your Honors' primary role in this case, as neutral factfinders, is to make recommended basic findings of fact, supported by credible, reliable evidence, on

which the Board can make the ultimate findings of whether or not Swickard proved good cause to establish the proposed dealership. To assist the Board in making its ultimate findings on adequacy of representation, harm to the protesting dealer, the desirability of a competitive marketplace, and the public interest, and in fairness to Protestant and the Board, your Honors should amend the PFD to include the following basic fact findings, which the *undisputed* evidence conclusively establishes:

(Lost Sales Opportunity)

- Every Texas AOR has gross loss for MB as well as for every competitive brand. (Tr. 571:7-19, Tr. 939:4-24; Ex. I-65 @ 096, Ex. I-66 @ 033; Ex. P-1 @ 241).
- Neither Swickard nor MBUSA determined, calculated or offered evidence regarding the normal or expected level of gross loss present in the Austin AOR or the amount of gross loss that would remain in the Austin AOR if the proposed Swickard dealership were established. (Tr. 1163:18-22; Ex. I-65 @ 96, Ex. I-66 @ 033, Ex. P-1 @ 241).
- Neither Swickard nor MBUSA developed a penetration profile for the proposed Swickard dealership based on its location in South Austin and its plan to target younger, less affluent, entry-level buyers.
- Neither Swickard nor MBUSA made a downward adjustment to their gross loss calculation to account for the normal level of gross loss that is present in a market, even in markets in which the MB brand is achieving 100% or greater registration effectiveness. (Tr. 1163:18-22; Ex. I-65 @ 96, Ex. I-66 @ 033, Ex. P-1 @ 241).
- Swickard and MBUSA included in their gross loss calculation gross losses that are located outside the 40-mile penetration profile that, based on Protestant's and MB of Georgetown's expected penetration profiles, they used for the proposed Swickard dealership.
- Swickard and MBUSA's gross loss calculation incorrectly assumes that the proposed Swickard dealership can capture all the gross loss in the Austin AOR no matter where it is located.

- Swickard and MBUSA’s gross loss calculation inflates the amount of lost opportunity that is realistically available for capture by the MB dealers in the Austin AOR.
- Insell occurs in markets for all line-makes or brands. (Tr. 604:2-3).
- Insell remains in a market even when a brand achieves 100% or greater registration effectiveness in that market. (Tr. 570:22-571:6).
- Neither Swickard nor MBUSA determined, calculated, or offered any evidence of, the normal or expected level of insell present in the Austin AOR or the amount of insell that would remain in the Austin AOR if the proposed Swickard dealership were established. (Tr. 578:24-579:5; Tr. 1205:20-1206:5).
- Swickard and MBUSA produced no evidence that the rate of insell into the Austin AOR is abnormally high.
- Swickard and MBUSA included in their insell calculation insells located outside the 40-mile penetration profile, which they developed using Protestant’s and MB of Georgetown’s expected penetration profiles, and which they used for the proposed Swickard dealership.
- Neither Swickard nor MBUSA made any adjustment for the normal or expected level of insell in the Austin AOR expected to remain in the Austin AOR if the proposed Swickard dealership were established or for the insells located outside the 40-mile radius of the proposed Swickard dealership. (Tr. 1602:10-11).
- Swickard and MBUSA incorrectly assumed that all units of insell wherever located in the Austin AOR are available for capture by the proposed Swickard dealership. (Tr. 1198:4-7; Tr. 1206:3-1).
- Swickard and MBUSA insell calculation inflates the amount of lost opportunity that is realistically available for capture by the MB dealers in the Austin AOR.

(Service Opportunity)

- The Service Opportunity Index (“SOI”) reports show that the MB dealer network has not captured 100% of the available service opportunity nationally or in any region or market area of the country. (Ex. P-25, P-26, Ex. P-27, Ex. P-28, Ex. P-29, Ex. P-61, Ex. P-62)
- Since February 2019, the SOI scores for MB Austin’s Area of Influence (“AOI”) have been higher than the national, regional, and

area benchmarks. (Ex. P-26, Ex. P-27, Ex. P-28, Ex. P-29, Ex. P-61, Ex. P-62).

- Since May 2019, the SOI scores for MB of Austin’s AOI have been higher than the market and market tier benchmarks. (Ex. P-28, Ex. P-29, Ex. P-61, P-62).
- Independent providers in the Austin area provide strong competition for the MB service and repair business. (Tr. 855:23-856:16).
- Vehicle owners reduce their tendency to bring their vehicles to dealerships for service as the warranties on their vehicles expire, and as the value of those vehicles diminishes with age. (Tr. 957:13-24).
- Younger owners of entry-level models often prefer to take their vehicles for service and repair to independent service providers rather than to franchised dealers. (Tr. 855:9-22, Tr. 859:1-860:4, Tr. 1517:24-1518:3).
- The inability of the MB dealer networks to achieve more than about 70%–71% of the service opportunity that is (theoretically) available in an AOI has been caused, in part, by MB’s product issues and delays in getting parts from MBUSA and its part suppliers. (Tr. 263:4-12).

3. In *Lee Trevino Ford v. Payton Wright Ford*, Proceeding 302 (March 7, 1984) (final order) and in *A.C. Collins Ford v. Charlie Thomas Ford*, Docket No. 87-206 (Sept. 6, 1989) (final order), the Board declared that unprofitable dealerships are not in the public interest. *Lee Trevino Ford*, PFD at p. 29; *A.C. Collins Ford*, PFD at p. 22. The Board in *Landmark Chevrolet* held that establishing the proposed dealership was not in the public interest because the applicant failed to prove that the lost opportunity realistically available for capture was greater than the number of units the applicant needed to breakeven and be profitable, thus requiring the applicant to cannibalize sales from the existing dealers to “keep the (proposed) dealership viable.” *Landmark Chevrolet*, PFD at 35, 71 [Finding of Fact No. 278].

The Board recognized that the public interest is not served in such a market because unhealthy competition will ensue when, as here, the market potential (or lost opportunity) for a brand is insufficient to enable the proposed and existing dealers to operate profitably. *Landmark Chevrolet*, PFD at p. 35; *Lee Trevino Ford*, PFD at pp. 29, 33.

Protestant's except to your Honors' misinterpretation that the Board in *Lee Trevino Ford* was concerned solely with the profitability of existing dealerships rather than proposed additional dealerships. (PFD at p. 74).² In fact, as in *Landmark Chevrolet*, the Board in *Lee Trevino* was concerned with the profitability of the proposed dealership *and* the existing dealerships:

“[A] critical question exists in this case of whether the market is adequate to support another dealership . . . The question of whether there is sufficient market is of critical importance because if the market is not sufficient to enable *the dealers* to operate profitably, the result of such a circumstance will be detrimental to the public interest, as there can be little doubt but that *dealers* who are not able to operate profitably are also not able to properly take care of the needs of their customers and the public. As in any case of this nature, it is not really possible to predict with absolute certainty just what level of sales or registrations can reasonably be expected to be sold by *the dealers* in the market.

“ . . . it would appear that the risk in this case is greater than what can be considered to be an acceptable risk; that risk being a market not sufficient to support *the existing and additional dealers* on a profitable basis with the resultant detrimental effects upon the public.” (Lee Trevino Ford, PFD at pp. 29, 33).

² For your Honors' convenience, Protestant attaches highlighted excerpts from the *Lee Trevino Ford* decision in the Appendix to these Exceptions behind Tab 2. A complete copy of the *Lee Trevino Ford* decision is included in Volume 2 of the Appendix to Protestant's Response and Closing Statement behind Tab 7.

Excusing Swickard's failure to show if or when its proposed dealership can ever be profitable is contrary to the Board's established precedent in *Lee Trevino Ford* and *Landmark Chevrolet*.

4. Protestant excepts to your Honors' statement that Protestant failed to explain why a "breakeven number" for the proposed dealership is necessary to show that Protestant will not be harmed "when the evidence established that sufficient opportunity exists in the market to sustain the proposed dealership." (PFD at p. 64). Protestant explained the importance of a breakeven number, but your Honors have put the proverbial "cart before the horse."

As shown in Protestant's Closing Statement and as detailed in *Landmark Chevrolet*, a breakeven number for a proposed dealership is of paramount importance in assessing the good cause factors, particularly those of harm to the protesting dealership, healthy or unhealthy competition, and the public interest. See Protestant's Response and Closing Statement at p. 50; *Landmark Chevrolet*, PFD at pp. 27, 32, 35, 47 [Finding of Fact No. 37], 64 [Finding of Fact No. 208], 68 [Finding of Fact No. 68], 71 [Finding of Fact No. 278].³

Without knowing how many new vehicles the proposed Swickard dealership must sell to breakeven and thus become profitable, neither your Honors nor the Board can determine whether the lost opportunity realistically available for capture in the

³ In its Response and Closing Statement, Protestant referenced and/or discussed breakeven more than 20 times and repeatedly discussed or cited the Board's decision in *Landmark Chevrolet* in which the Board discussed the critical role the applicant's breakeven number plays in assessing the merits of a license application.

market will be sufficient to profitably support the proposed and existing MB dealerships in the Austin AOR. The Board repeatedly stressed the importance of establishing the breakeven point and the amount of realistically achievable lost opportunity in *Landmark Chevrolet*:

“... Munday and GM ask the Board to find that Munday’s establishment in the Houston MDA will enhance healthy competition ***absent a showing of quantifiable, reasonably achievable opportunity in the market in excess of the amount needed for Munday to exceed its break-even point without harming Landmark.***

“... In this case, the 1992 shortfall . . . equaled 705 units . . . ***This is well under the number of units Munday needs to break even. In the unlikely event that Munday could capture all of that shortfall, the remainder needed to keep the dealership viable would have to be cannibalized from Landmark and Robbins (the existing dealers).*** Without quantifiable achievable opportunity in the market beyond that, Landmark and Robbins would then be relegated to cannibalizing from other competitors in the market.” (*Landmark Chevrolet*, PFD at pp. 30-31, 32, 35).

“Finding of Fact 247. In this case, the record reflects that Munday and GM are asking the Board to find that Munday’s establishment in the Houston MDA will enhance healthy competition ***absent a showing of quantifiable, reasonably achievable opportunity in the market in excess of the amount needed for Munday to exceed its break-even point without harming Landmark.***” (*Landmark Chevrolet*, PFD at p. 68).

5. Protestant excepts to your Honors’ supposition that Swickard and MBUSA’s (unadjusted and inflated) lost opportunity number of 755 units is sufficient “to sustain the proposed dealership.” (PFD at p. 64). Neither Swickard nor MBUSA produced any such evidence. Because Swickard’s plan is to build a “spectacular,” “state-of-the-art facility” and target young, less affluent, entry-level customers, the breakeven number for the proposed Swickard dealership is likely much higher than 755 new units. This means the proposed dealership will not operate profitably unless

it cannibalizes new vehicle sales, *i.e.*, makes sales that would otherwise be made by Protestant and MB of Georgetown. *See Landmark Chevrolet*, PFD at p. 35, p. 64 [Finding of Fact Nos. 208, 209]).

Your Honors dismiss MBUSA's planning volume for 916 new vehicles for the proposed dealership as "merely a projection" of sales, and then wrongly shift the burden of proof to Protestant by saying that "no evidence suggested that the new dealership must sell that many vehicles (916) in order to be profitable or to break even." (PFD at p. 64). *It was Swickard's burden to show how many new vehicles need to be sold to breakeven — not Protestant's. See Landmark Chevrolet.* Moreover, as noted in prior Board's decisions, the planning volume for a dealership is a *reliable* projection of sales. *See Landmark Chevrolet*, PFD at 47 [Finding of Fact No. 37]). *See also, Don Davis Oldsmobile, Inc. v. Autobahn Imports, Inc. et al*, Docket No. 90-378, PFD at p. 21 (May 30, 1991) (final order granting joint motion for dismissal), ("Planning volume is a measurement consisting of sales potential in the marketplace for a particular product."); *Lee Trevino Ford*, PFD at pp. 22-23 ("[T]he registration deficiency . . . would total 247 units, which is hardly sufficient to support a proposed dealership with a planning volume of 1,350 cars and trucks.").

Swickard had the burden of proving that licensing its proposed dealership is in the public interest. To discharge that burden and avoid triggering cannibalization of MB sales in the Austin AOR, Swickard had to provide a reasonable projection of the number of new vehicles the proposed dealership must sell to breakeven and achieve profitability. Determining breakeven required Swickard to make reasonably

reliable projections of the proposed dealership's operational expenses, which Swickard failed to do. MBUSA's Dealer Accounting Manual defines "breakeven" as the "[e]stimated volume of new vehicle units required to reached zero operating profit." (Ex. P-66 [MBUSA_002080]). The Manual defines "operating profit" as "[t]otal sales less *total cost of sales and total expenses.*" (Emphasis added). (Ex. P-66 [MBUSA_002084]). The incomplete, smattering of operational expenses referenced in "Swickard Austin, LLC's Preliminary Projections" (Ex. A-2) were in Mr. Swickard's words "a kind of best guess." (Tr. 98:1-14, Tr. 119:1-7). Furthermore, the only evidence in the record shows that little or no profit is earned on the sale of the C-class and A-class entry-level MB models – the ones that Swickard plans to focus its sales efforts upon. (Tr. 59:1-6, Tr. 61:5-9, Tr. 109:11-15, Tr. 1302:3-11, 1304:5-12, Tr. 1307:9-20). This fact made it even more incumbent on Swickard to provide a reliable estimate of how many new vehicles the proposed dealership must sell from its planned "spectacular," "state-of-the-art" dealership facility in order to achieve breakeven.

The missing breakeven number would have shown the Board whether the amount of lost opportunity in the Austin AOR reasonably available for capture by the MB brand is sufficient to profitably support the proposed dealership. But Swickard failed to prove both (1) the amount of lost opportunity realistically available for capture *and* (2) the number of new vehicles the dealership must sell to breakeven. The Board should be informed of this failure of proof because it prevents the Board from making legally sustainable findings that the proposed Swickard dealership will

promote healthy competition, will not harm Protestant, and will be in the public interest.

6. Protestant excepts to your Honors' statement that Protestant did not show "why it is necessary or required for Applicant to have submitted business plans into evidence in order to establish that adding the new dealership will promote competition in the marketplace." (PFD at p. 62). The Code places the burden on Swickard to prove that licensing the proposed dealership will be in the public interest, will promote healthy competition, and will not cause harm to the protesting dealer. Because unprofitable dealerships are not in the public interest, the Code also directs the Board to consider the "financial expectations" of the proposed new dealership. Such plans are necessary to show the proposed dealership's financial structure, if and when it will be profitable, and the number of new vehicles needed to be sold to achieve profitability. Without this information, the Board cannot rationally find that licensing the proposed dealership will be in the public interest, that healthy competition will ensue if the proposed dealership is licensed, or that the proposed dealership will not harm Protestant. That is why applicants supply such information to the Board. *See e.g., Landmark Chevrolet*, PFD at p. 47 [Finding of Fact No. 37]; *Weslaco Motors v. Bert Ogden Chevrolet*, MVD Docket No. 08-0011.LIC, SOAH Docket No. 601-08-2071.LIC, PFD at pp. 14-15 (Feb. 6, 2012) (final order); *Atomik Enterprises v. Sport City, Inc.*, Proceeding No. 85, Supp. PFD at p. 8, PFD at p. 7

(April 6, 1978) (final order).⁴ Swickard's failure to do so prevented it from carrying the burden of proving good cause.

To assist the Board in making its ultimate findings on harm to the Protestant, a competitive market place, and the public interest, your Honors should amend the PFD to include the following basic findings of fact, which are conclusively established by the evidence:

- Swickard plans to build a “spectacular” “state-of-the-art” “world class” 80,000 square foot dealership facility. (Tr. 83:9-10, 84:18-20).
- Swickard has not prepared a construction budget, building plans, formal or detailed *pro forma* financial statements, a business plan, or a breakeven analysis. (Tr. 75:14-15, Tr. 97:4-11, Tr. 116:10-18, Tr. 120:21-24, Tr. 121:1-3, Tr. 331:2-22; Ex. A-2). T
- The proposed Swickard dealership will concentrate on selling entry-level C-class and A-class models on which little or no profit is earned by MB Austin. (Tr. 59:1-6, Tr. 61:5-9, Tr. 109:11-15, Tr. 1302:3-11, 1304:5-12, Tr. 1307:9-20).
- Swickard provided no evidence of the number of entry-level MB models the proposed Swickard dealership plans to sell, or the profit margins on such sales.
- In “Swickard Austin, LLC’s Preliminary Projections” (Ex. A-2), Swickard projects selling 775 new vehicles in the first full year of operation, 900 new vehicles in the second full year of operation, and 1050 new vehicles in the third full year of operation. (Ex. A-2).
- Swickard’s “Preliminary Projections” document contains no projection of revenues, no operating statements, no profit projections for any department, and no breakeven analysis for the proposed Swickard dealership. (Ex. A-2).

⁴ For your Honors’ convenience, Protestant attaches copies of the final orders and proposals for decisions in *Weslaco Motors* and *Atomik Enterprises* in the Appendix to these Exceptions behind Tabs 2 and 4.

- The “Preliminary Projections” are not reliable financial data, as Swickard admitted the “Preliminary Projections” are a “guess.” (Tr. 98:1-14, Tr. 119:1-7).
 - MBUSA has made no profit projections or breakeven analysis for the proposed Swickard dealership—which Mr. Newcomb of MBUSA testified is a “high-risk business.” (Tr. 119:11-23, Tr. 120:5-20, Tr. 312:7-8, Tr. 341:12-21).
7. Protestant excepts to Finding of Fact No. 34 concerning Protestant’s compliance with MBUSA’s brand standards. The finding wrongly implies that Protestant’s facility is not “competitive” with other dealership facilities. The finding is based on an incorrect interpretation of the statutory factor of adequate representation. The legal standard is “*adequate*” representation—not “optimal” representation, or representation “superior” to competing brands. MBUSA sets facility standards. Protestant has made all necessary investments to stay in compliance with those standards and has taken all remedial actions requested by MBUSA to do so. (Tr. 674:13-18). Protestant’s compliance with MBUSA’s brand standards is further shown by the fact that Protestant has earned the “Brand Standards Bonus” every year since 2014. (Ex. I-69 @ 052, Ex. P-18 to Ex. P-21). Components of the brand standards bonus include “Facility/Autohaus 2” and “Annual Facility Certification.” (Ex. P-21). If MBUSA wants all its franchised dealers to have facilities that are the same aesthetically, or that are comparable with, or superior to, those of competing brands, then MBUSA has the power to mandate the facility standards necessary to achieve those goals. Until MBUSA does so, dealership facilities, like Protestant’s, that comply with MBUSA’s current facility

standards provide adequate representation. (Tr. 625:19-21). Finding of Fact No. 34 should be modified to state that, “MB Austin is compliant with MBUSA’s brand standards.”

8. Protestant excepts to Finding of Fact No. 37 and to the statements on page 13 of the PFD concerning the lost service opportunity theoretically available for capture in Protestant’s AOI as of December 2018. In the first place, the finding is based on outdated data. The finding ignores the most recent SOI reports showing that the existing MB dealers are capturing all the service opportunity that is reasonably available for capture by the MB brand in Protestant’s AOI. (Ex. P-28, P-29, P-61, P-62). The finding also is based on an incorrect standard of theoretical opportunity instead of the standard of opportunity that is reasonably or realistically available for capture as established by the Board’s decision in *Landmark Chevrolet*. Finding of Fact No. 37 and the statements at page 13 of the PFD should be modified to provide that, “Based on the most recent SOI reports in evidence, the existing MB dealers in the Austin AOR are capturing all the service opportunity that is realistically available for capture in Protestant’s AOI. (Ex. P-28, P-29, P-61, P-62).”

9. Protestant excepts to Finding of Fact No. 38 and the statements on pages 13 and 53 of the PFD concerning the theoretical amount of “un-serviced vehicles in the Austin AOI.” Protestant assumes your Honors’ reference to the “Austin AOI” actually means the “MB Austin AOI.” If that is so, then this finding is based on outdated data from December 2018, and ignores more recent 2019 SOI reports showing that the existing MB dealers are already capturing all the service

opportunity that is realistically available for capture in the AOI. (Ex. P-28, P-29, P-61, P-62). The finding also is based on an incorrect standard of theoretical opportunity instead of the standard of opportunity that is reasonably or realistically available for capture established by the Board's decision in *Landmark Chevrolet*. Your Honors further incorrectly assert at page 13 of the PFD that of the 7,900 serviced vehicles in Protestant's AOI in December 2018, Protestant "only served 43 percent, leaving 3,900 un-serviced vehicles in the Austin AOI." The assertion that Protestant serviced only 43% of the vehicles in the AOI is based on unreliable oral testimony with no documentary evidence to support it. Also, your Honors wrongly state that 3,900 vehicles in the AOI were left "un-serviced." The vehicles not serviced by Protestant were serviced by other MB dealers. Ex. I-26 @ 001 shows that 4,615 vehicles in Protestant's AOI were "un-serviced"—*not* 3,900 vehicles as your Honors wrongly state. At page 53 of the PFD your Honors state that, "Of the 7,900 vehicles that were service[d], MB Austin serviced only about 43 percent of them, and 20 percent were serviced by other MB dealers." If, as your Honors incorrectly suppose, Protestant serviced only 43 percent of the 7,900 serviced vehicles, then 57 percent were serviced by other MB dealers—not 20 percent. All 7,900 were serviced by MB dealers in December 2018. The total vehicles not serviced by MB dealers was 4,615. (Ex. I-26 @ 001).⁵ Finding of Fact No. 38 and

⁵ Mr. Hoelf's improper and unreliable testimony was that of the 63.9% of service opportunity captured in December 2018, Protestant performed 43% of it, meaning that about 20% was performed by other MB dealers. (Tr. 856:23-857:1).

the statements at pages 13 and 53 of the PFD should be modified to provide that, “Based on the most recent SOI reports in evidence, the existing MB dealers in the Austin AOR are already capturing all the service opportunity that is realistically available for capture in Protestant’s AOI. (Ex. P-28, P-29, P-61, P-62). The statements on pages 13 and 53 concerning “3,900 un-serviced vehicles,” “MB Austin only serviced 43 percent,” and “20 percent were serviced by other MB dealers” should be withdrawn.

10. Protestant excepts to Finding of Fact Nos. 41, 125, and 126, and the statements at pages 53 and 56 of the PFD concerning Protestant’s service capacity. The findings and statements are based on outdated data and ignore more recent measures Protestant has taken to expand its service capacity. The findings and statements also ignore the shortage of qualified service technicians that problems with MB vehicles made at its Alabama plant have exacerbated. (Tr. 676:18-677:5, Tr. 1270:10-15, Tr. 1410:13-1411:2, Tr. 1498:8-12). Because of those problems, MBUSA has been recruiting service technicians away from MB dealerships by paying them bonuses. (Tr. 1409:2-13, Tr. 1411:3-8.⁶

Your Honors ignore both the impact of this technician shortage on the proposed Swickard dealership and Swickard’s plan to pay technicians salaries far

⁶ Your Honors’ finding also ignore the Board’s decision in *Hudiberg Chevrolet, Inc. v. Frontier 74GMC, Inc., et. al.*, Docket No. 80–193, PFD at p. 37 (Jan. 8, 1981) (final order) where the Board found that protestant was adequately representing manufacturer as to service even though the protestant had an inadequate number of technicians, had an inadequate parts inventory, and was turning away service work.

below the going rate. Swickard's "Preliminary Projections" call for hiring 19 service technicians at an annual salary of \$60,000. (Ex. A-2). Mr. Swickard testified the proposed dealership would not "raid local car dealerships" to hire them. (Tr. 93:8-12). Mr. Swickard also testified that he had done no study to determine the average service technician wage in Austin. (TR. 126:17-20). The testimony of Mr. Opinker and Mr. Hardeman showed that Swickard's projection of hiring 19 service technicians at an annual wage or salary of \$60,000 is unrealistic. (Tr. 1411:20-1412:4, Tr. 1361:17-1362:19). The shortage of service technicians has driven the salary for qualified service technicians in the Austin market to \$100,000 annually. (Tr. 1412:2-4). MB of Austin's highest paid service technician makes more than \$100,000 per year. (Tr. 1582:3-5). So, how is the proposed Swickard dealership supposed to capture (non-existent) lost service opportunity by paying below market salaries when a shortage of qualified service technicians exists? The PFD does not tell the Board.

Your Honors should inform the Board of the impact of MBUSA's actions on Protestant's retention and recruitment efforts and that Swickard's plan to hire service technicians is unrealistic. Despite the shortage of service technicians, Protestant has managed to hire new service technicians to help lower service wait times and is participating in programs to recruit and train new ones. (Tr. 897:4-20, Tr. 1409:14-1410:1, Tr. 1424:14-21). Finding of Fact No. 126 is speculative. The steps Protestant is taking will help solve retention problems and reduce wait times for major repair service. Finding of Fact Nos. 125 and 126 should be withdrawn,

and Finding of Fact 41 and the statements at pages 53 and 56 of the PFD should be modified to state that, “Despite a shortage of available qualified technicians, caused in part by MBUSA, MB Austin has taken steps to retain service technicians, increase its service capacity, and reduce wait times for major repair service. The proposed Swickard dealership proposes to hire service technicians at salaries below market rates.”

11. Protestant excepts to Finding of Fact No. 44 and the statements made at pages 14 and 54 of the PFD concerning Protestant’s service department and service technicians. The finding and statements are based on the unreliable testimony of MBUSA employee, Fred Hoefl. The space for repairing and servicing of vehicles in Protestant’s service department is not cooled by a central air-conditioning system. But your Honors fail to note that MBUSA standards do *not* require air conditioning. (Tr. 672:23-673:1). The temperature in Protestant’s service and repair space is controlled by large, water-cooled fans. (Tr. 1346:1-18). Mr. Nick Opinker, Protestant’s service director, testified that Protestant did *not* lose any service technicians because of the way in which the service and repair shop is air-conditioned. (Tr. 1410:9-12). Mr. Opinker is in a superior position to know why service technicians under his personal supervision left Protestant’s employ. In fairness to the Protestant and the Board, Finding of Fact No. 44 and the statements at pages 14 and 54 of the PFD should be modified to provide that, “MBUSA standards do not require air conditioning of a MB dealership’s service area. (Tr. 672:23-673:1). The temperature in Protestant’s service and repair space is

controlled by large, water-cooled fans. (Tr. 1346:1-18). There is no credible evidence that MB Austin has lost any of its service technicians because of the lack of a central air conditioning system.”

12. Protestant excepts to Finding of Fact No. 121 and to the statements in the PFD at pages 28, 52 and 78 concerning MB’s “share of franchises” and the alleged need for an additional MB franchised dealership in the Austin market. Your Honors overlook the significant fact that no luxury dealer in the Austin AOR has more than two dealerships, and nowhere in the PFD is this fact mentioned. Mr. Farhat’s analysis did not show when three MB dealers in the Austin AOR will be needed. Your Honors correctly noted at pages 28 and 66 of the PFD that Mr. Farhat’s analysis did not take into account any projected growth in the Austin AOR.⁷ Finding of Fact No. 121 and the statements at pages 28, 52, and 78 of the PFD should be modified to inform the Board that no luxury brand in the Austin AOR has more than two dealers, and to state that, “At present, three MB dealers are not needed in the Austin market for MB to achieve the same ‘share of franchises’ compared to other luxury dealers in the Austin market or to satisfy the sales or service needs of luxury customers in the market.”

13. Protestant excepts to Finding of Fact No. 122 and the statements at pages 54 and 56 of the PFD concerning Protestant’s alleged failure to adequately capture service opportunity in its AOI that is being supposedly lost. In the first

⁷ The economic impact of COVID-19 likely will delay for years any need for a third MB dealership.

place, it is not Protestant's sole responsibility to capture all the service opportunity in its AOI. As your Honors note on page 13 of the PFD and in Finding of Fact No. 36, SOI for an AOI measures the performance of all MB dealers servicing MB vehicles in an AOI—in this case, Protestant and MB of Georgetown. Second, the finding and statements are based on an improper theoretical lost service opportunity standard. The most recent SOI reports in evidence indisputably show that Protestant and MB of Georgetown are capturing all the service opportunity that is realistically available for capture by the MB brand in the AOI. Protestant's construction of additional service bays and its hiring of more service technicians will reduce wait times for major repairs. Finding of Fact No. 122 and the statements at pages 54 and 56 of the PFD should be modified to state that, "The existing MB dealers in the Austin AOR are already capturing all the service opportunity that is realistically available for capture by the MB brand in Protestant's AOI."

14. Protestant excepts to Finding of Fact No. 123 concerning the service performance of Protestant's AOI in December 2018. The finding unjustly ignores the most recent SOI reports (June 2019 through October 2019) showing that the existing Austin AOR MB dealers are exceeding every benchmark on those reports. (Ex. P-28, Ex. P-29, Ex. P-61, Ex. P-62). Protestant is mystified why your Honors choose to make a finding using the most outdated SOI report in evidence. Finding of Fact No. 123 should be modified to state that, "MB Austin's AOI is above every benchmark (national, regional, area, market, market tier) as of October 2019."

15. Protestant excepts to Finding of Fact No. 127 and the statements made at page 55 of the PFD concerning Protestant's compliance with MBUSA's brand standards. As discussed in Exception No. 7, the finding and statements wrongly imply that Protestant's facility is not "competitive" with other dealership facilities and is based on an incorrect interpretation of the statutory factor of adequate representation. The legal standard is "*adequate*" representation—not "optimal" representation, or representation "superior" to competing brands. MBUSA sets facility standards. Protestant makes the necessary investments to maintain compliance with those standards and takes all remedial actions requested by MBUSA to do so. (Tr. 674:13-18). Protestant's compliance with MBUSA's brand standards is further shown by the fact that Protestant has earned the "Brand Standards Bonus" every year since 2014. (Ex. I-69 @ 052, Ex. P-18 to Ex. P-21). Components of the brand standards bonus include "Facility/Autohaus 2" and "Annual Facility Certification." (Ex. P-21). From its facility, Protestant is profitable and is capturing all the MB service business realistically available for capture in its AOI, as shown by the recent SOI reports. If MBUSA wants all its franchised dealers to have facilities that are the same aesthetically, or that are comparable with, or superior to, those of competing brands, then MBUSA has the power to mandate the facility standards necessary to achieve those goals. Until MBUSA does so, dealership facilities, like Protestant's, that comply with MBUSA's current facility standards provide adequate representation. (Tr. 625:19-21). Finding of Fact No.

127 and the statements on page 55 of the PFD should be modified to provide that, “MB Austin is compliant with MBUSA’s brand standards.”

16. Protestant excepts to Finding of Fact No. 128 concerning Protestant’s dealership location. The finding states that the dealership is not in a desirable part of town for a luxury dealership. Protestant’s large volume of service business demonstrate the incorrectness of this finding. The finding is also undermined by your Honors’ Finding of Fact No. 45 (“Traffic patterns give MB Austin a good service location relative to daily commuters, and MB Austin is near employment centers.”). Finding of Fact No. 128 should be modified to state that, “MB Austin’s location is in a good location for a luxury car dealership.”

17. Protestant excepts to Finding of Fact No. 130 and the statements at pages 52, 55, 56, and 63 of the PFD concerning adequacy of representation as to sales in the Austin AOR and in Protestant’s AOI. The finding and statements assert that Protestant is not adequately representing the MB brand in terms of sales. The finding and statements are based on incorrect legal standards and violate Board precedent. The proper legal question is whether “the manufacturer or distributor of the same line-make of new motor vehicle is being adequately represented as to sales and service . . .” Tex. Occ. Code § 2301.652(a)(1). In a metro market like Austin with more than one dealership representing the brand, the inquiry is not whether one dealer is adequately representing the brand in a market area, but whether the existing dealers are doing so. Furthermore, whether the brand is being adequately represented depends on whether the amount of lost opportunity in the market

realistically available for capture by the brand's existing dealers is large enough to profitably support another dealership for the brand. Swickard and MBUSA failed to prove that the existing MB dealers in the Austin AOR are inadequately representing MB as to sales. Using a "net" registration methodology, Mr. Farhat found that from 300 to 425 registrations were "lost" to competing brands in 2018. (Tr. 552:11-21, Tr. 579:11-18; Ex. I-65 @ 040, 041). Using his "gross loss" methodology, Mr. Farhat calculated that 474 registrations were not captured in 2018 for the MB brand by the existing dealer network using MB's national market share penetration as a benchmark and that 281 units of insell were available for capture. (Ex. I-65 @ 96). But Swickard and MBUSA failed to prove that this amount of shortfall (755 units), which as shown above in Exception Nos. 2 and 5 is inflated and unreliable, can profitably support another MB dealership in the Austin AOR. Your Honors suggest on page 63 of the PFD that lost opportunity will grow along with Austin's continued growth. However, Mr. Farhat never calculated such a number, as your Honors noted in the PFD.⁸ Consequently, your Honors' statement constitutes speculation and should be withdrawn. Finding of Fact No. 130 and the statements at pages 52 55, 56, and 63 of the PFD should be modified to provide that, "Swickard and MBUSA failed to prove that the MB brand is not being adequately

⁸ Whether Austin will continue to grow in light of the economic fallout from the COVID-19 pandemic is questionable and is a proper subject for a remanded hearing.

represented in the Austin AOR in terms of vehicle sales. Accordingly, this factor weighs against licensing the proposed dealership.”

18. Protestant excepts to Finding of Fact No. 142 concerning Swickard’s failure to provide MBUSA with a dealer application, business plan, balance sheet, breakeven analysis, or other financial projections. The finding states that MBUSA did not “need” this financial information to determine whether the proposed new dealership “will further healthy competition.” But even if MBUSA did not “need” this information to make its decision to award Swickard a franchise, the Board needs it to decide this case correctly, as shown by the Board’s prior decisions, especially *Landmark Chevrolet*. Without reasonably reliable estimates of the proposed Swickard dealership’s cost structure, operational expenses, revenue projections, and breakeven point, the Board cannot determine whether licensing the dealership will result in healthy or destructive competition. Without knowing how many new vehicles the proposed Swickard dealership must sell to be profitable, the Board has no way of knowing if the amount of lost opportunity realistically available for capture is sufficient to make the proposed dealership profitable without harming the existing MB dealers. Without such evidence, the Board rightly assumes that cannibalization of sales will ensue if the applicant is licensed. *Landmark Chevrolet*, PFD at pp. 27, 35, 64 [Finding of Fact No. 209], 71 [Finding of Fact No. 278]. Unprofitable dealerships and unhealthy competition among dealers of the same brand are not in the public interest. Unhealthy competition occurs when the realistically available opportunity or market potential for a brand in the relevant

market is insufficient to profitably support each of the brand's dealers located in that market. *Landmark Chevrolet*, PFD at p. 32; *Lee Trevino Ford*, PFD at pp. 22-23, 29, 34. Destructive competition between the existing dealerships and the new dealership will result if the realistically achievable lost sales opportunity and service opportunity for the new dealership are insufficient for it to be profitable. *Austin Chevrolet, Inc. v. Motor Veh. Bd.*, 212 S.W.3d 425, 434 (Tex. App. – Austin 2007, pet. denied). Finding of Fact No. 142 should be modified to state that, “Swickard had the burden to prove that the proposed dealership will further healthy competition, which required Swickard to prove that the amount of lost opportunity realistically available for capture in the Austin AOR is sufficient to make the proposed dealership profitable. Swickard failed to provide such proof and thus failed to discharge its burden.”

19. Protestant excepts to Finding of Fact No. 143 concerning whether the proposed Swickard dealership will be subsidized by the existing MB dealers. The finding wrongly assumes that the “untapped sales and service opportunity in the Austin AOR” is sufficient for the proposed dealership to be “successful.” No evidence supports this assumption and the finding based on that assumption. Swickard and MBUSA failed to prove that the amount of lost sales and service opportunity realistically available for capture in the Austin AOR is sufficient to make the proposed dealership “successful,” *i.e.*, profitable. The reliable evidence in the record shows that the existing MB dealers—primarily Protestant—will subsidize the proposed dealership. That is so because not enough untapped sales

and service opportunity is realistically available for capture in the Austin AOR to make the proposed dealership profitable without cannibalizing sales and service business from the existing MB dealers. *Landmark Chevrolet*, PFD at pp. 27, 35, 64 [Finding of Fact No. 209], 71 [Finding of Fact No. 278]. Finding of Fact No. 143 should be modified to state that, “Applicant failed to prove that the untapped sales and service opportunity realistically available for capture in the Austin AOR is sufficient for the proposed dealership to be successful without being subsidized by the existing MB dealers.”

20. Protestant excepts to Finding of Fact No. 144 and the statements at pages 60, 61, and 75 of the PFD concerning “healthy competition.” The finding and statements are misleading. The luxury automobile segment of the Austin AOR is already “hypercompetitive.” (Tr. 299:18-30; Tr. 1315:7-8; MBUSA’s Opening Brief at 17). As of 2018, thirty-eight (38) luxury dealerships serve the Austin market. (Ex. I-65 @ 057, Ex. I-66 @ 022). Protestant faces stiff price competition from the other luxury brand dealerships (Tr. 1185:18-1186:10, Tr. 1189:25-1190:3; Ex. I-65 @ 034, Ex. P-7 @ 013 [¶ 36]). Establishing the proposed Swickard dealership will not increase competition in a healthy way, given Swickard’s and MBUSA’s failure to prove that enough realistically achievable lost opportunity exists in the market to support the new dealership without harming Protestant. Finding of Fact No. 144 and the statements made at pages 60, 61, and 75 of the PFD should be modified to include this sentence: “Because of Swickard and MBUSA’s failure to prove that enough realistically achievable lost opportunity exists in the

Austin AOR to support the new dealership without harming Protestant, unhealthy competition will occur if the proposed Swickard dealership is established.”

21. Protestant excepts to Finding of Fact No. 146 and 150 and the statements at pages 60, 61, and 75 of the PFD concerning customer convenience and competition. The findings and statements are misleading. As shown above, the Austin market is currently “hypercompetitive.” The findings and statements also ignore the fact a brand can always enhance customer convenience by establishing a new dealership that is closer to a part of the market than are the brand’s existing dealers. Adding a new dealership will likely increase inventory and advertising. But such increases are not desirable when, as here, the lost opportunity realistically available for capture by the MB brand has not been shown to be sufficient to profitably support the new dealership without harming the existing MB dealers. *See Lee Trevino Ford*, PFD at p. 28. Finding of Fact Nos. 146 and 150 and the statements at pages 60, 61, and 75 of the PFD should be modified to state that, “Although establishing the proposed Swickard dealership could potentially result in modest increases in advertising for the MB brand, the availability of inventory in the market, access to the MB brand, convenience of service, and choice and competitive pricing for consumers, those potential benefits are outweighed by Swickard and MBUSA’s failure to prove that the lost opportunity realistically available for capture by the MB brand is sufficient to profitably support the new dealership without harming the existing MB dealers.”

22. Protestant excepts to Finding of Fact No. 147 and statements at pages 60, 61, and 75 of the PFD concerning competition and customer convenience. The finding and statements are misleading. As shown above, the Austin market is already “hypercompetitive.” The finding and statements also ignore the fact customer convenience can always be increased simply by establishing a new dealership that is closer to a part of the market than are the brand’s existing dealers. Establishing the proposed Swickard dealership would increase customer convenience in the South Austin area. (Tr. 1012:2-10; Ex. I-65 @ 095). But the cost of such an increase outweighs its benefit. The increase in customer convenience resulting from the establishment of the proposed Swickard dealership would be undesirable and destructive because the lost sales and service opportunity realistically available for capture by the MB brand in the Austin AOR has not been shown to be sufficient to profitably support the proposed dealership without harming MB’s existing dealers. *See Lee Trevino Ford*, PFD at p. 28 (convenience of the facility to the public is not in and of itself controlling “as there may well be other overriding factors which will govern if the consequences of the granting the license are likely to be more detrimental than beneficial.”). Finding of Fact No. 147 and the statements at pages 60, 61, and 75 of the PFD should be modified to state that, “Because of Swickard and MBUSA’s failure to prove that the lost opportunity realistically available for capture by the MB brand is sufficient to profitably support the new dealership without harming the existing MB dealers, licensing the proposed

Swickard dealership would cause unhealthy competition that would outweigh the benefit of increased customer convenience.”

23. Protestant excepts to Finding of Fact No. 149 and the statements at pages 61 and 62 of the PFD concerning entry-level luxury buyers. The finding and statements wrongly assert that Protestant “does not market” to entry-level customers. In fact, entry-level sales constituted almost 20% of Protestant’s new vehicle sales (163 units) in 2018 (Ex. I-14 @ 007 [Lines 4-6, 9, 21-22] and 17% of MB of Austin’s new vehicle sales (177 units) in 2017. (Ex. I-11 @ 007 [Lines 1, 3, 4, 6-7, 18-19]. While these sales are largely unprofitable, they may make it possible for Protestant to meet the objectives needed to qualify for sales-related incentives. Your Honors says that Protestant did not support its assertion “by evidence in the record” that a large volume of entry-level sales are not realistically available to the proposed dealership. Protestant did so by citing to the product popularity report at Ex. I-68@ 006 and 007. That report shows that entry-level registrations constitute a relatively small portion of total retail competitive group registrations. Swickard also produced no evidence of the number of the entry-level sales its dealership would likely make or the projected profit margins on such sales. Nor did Swickard offer evidence of the number of entry-level sales it would have to make to qualify for sales-related incentives. Finding of Fact No. 149 and the statements at page 74 should be modified to provide that, “MB Austin markets to entry-level customers and depends on such sales to qualify for sales-related incentive bonuses. Swickard

produced no evidence of the number of the entry-level sales its dealership would likely make.”

24. Protestant excepts to Finding of Fact No. 153 and to the statements at page 62 of the PFD concerning Protestant’s ability to compete in the market. The finding and statements wrongly imply that healthy competition will occur between Protestant and the proposed Swickard dealership. As shown in Exception Nos. 4, 6, and 18, it will not. As the Board realized in *Landmark Chevrolet*, destructive competition will likely ensue because Swickard and MBUSA failed to show that the realistically achievable lost sales and service opportunity in the Austin AOR is sufficient for the Swickard dealership to breakeven and be profitable. *Landmark Chevrolet*, PFD at pp. 34-35. Finding of Fact No. 153 and the statements at page 62 of the PFD should be modified to state that, “MB of Austin is a highly profitable dealership that is in a good position for competing in the market. However, MB Austin’s competitive response to the proposed Swickard dealership will trigger destructive competition because Swickard and MBUSA failed to prove that the realistically achievable lost sales opportunity and service opportunity available for capture in the Austin AOR are sufficient for MB Austin to maintain its level of sales and profitability and for the new dealership to be profitable.”

25. Protestant excepts to Finding of Fact No. 154 and the statements at page 62 of the PFD concerning competition in the marketplace. The finding and statements provide that the proposed dealership “will promote healthy competition in the marketplace, and this factor weighs in favor of granting the Application.” For

the reasons set forth in Exception Nos. 4, 6, 18, and 21, no evidence supports the finding or these statements. Absent any credible evidence of quantifiable, reasonably achievable opportunity in the Austin AOR in excess of the amount needed for the proposed Swickard dealership to exceed its break-even point without harming Protestant, destructive competition will ensue. *Landmark Chevrolet*, PFD at 32. The finding and statements should be modified to state that “Swickard and MBUSA failed to prove that opening the proposed dealership will promote healthy competition in the marketplace, and this factor weighs against granting the Application.”

26. Protestant excepts to Finding of Fact No. 155 and the statements at pages 63 and 64 of the PFD because they are misleading and based on a misreading of the Board’s *Landmark Chevrolet* decision. Citing to pages 30-31 of the *Landmark Chevrolet* PFD, your Honors state that *Landmark Chevrolet* “notes that it is acceptable for an existing dealership to experience some lost profits when a new dealership is established.” Your Honors have taken this statement out of context and overlooked important qualifications the Board placed on this statement in the PFD and its Findings of Fact:

“Did the Legislature intend to require existing dealers in a market with little to no opportunity above and beyond that which is already being captured to forgo their profitability for the benefit of a new dealer? To answer this question in the affirmative seems exceedingly unfair to Landmark (the protesting dealer) . . . *If the Board adopts Munday’s (the applicant’s) interpretation of harm without some real indication that opportunity exists, Landmark will likely work even harder and sacrifice even more to acquire less . . .*

“The Board has clearly ruled, on a number of occasions, that an existing dealer in a flourishing market *where opportunity looms large* is not necessarily ‘harmed’ simply because it must now share the market with a new dealer, even if it means that the existing dealer will profit less after the dealer network expands. *It is appropriate for the Board to expect a protesting dealer in danger of losing profits to acclimate itself to an addition to the dealer body by adjusting its business strategy to capture as-yet untapped opportunity in the market.*”

“... Munday and GM ask the Board to find that Munday’s establishment in the Houston MDA will enhance healthy competition ***absent a showing of quantifiable, reasonably achievable opportunity in the market in excess of the amount needed for Munday to exceed its break-even point without harming Landmark.***”

“... In this case, the 1992 shortfall . . . equaled 705 units . . . ***This is well under the number of units Munday needs to break even. In the unlikely event that Munday could capture all of that shortfall, the remainder needed to keep the dealership viable would have to be cannibalized from Landmark and Robbins (the existing dealers).*** Without quantifiable achievable opportunity in the market beyond that, Landmark and Robbins would then be relegated to cannibalizing from other competitors in the market.” (Emphasis added). (PFD at pp. 30-31, 32, 35).

The Board in *Landmark Chevrolet* also made the following findings of fact:

“37. Munday’s break-even point for new motor vehicle sales was calculated to be from 1200 to 1500 units per year and its planning potential was determined by GM to be 2296 units.

208. Even if Munday captured all 336 units calculated as part of the hypothetical related to the San Antonio case study touted by GM’s expert, ***this does not represent nearly the amount of sales Munday needs to meet, let alone exceed, its break even point.***”

209. The record in this case reflects a level of opportunity that is so low that ***Munday’s options, upon entry into the Houston MDA market, are truly limited to cannibalization of its closest intrabrand competitors in order to merely survive.***

247. In this case, the record reflects that Munday and GM are asking the Board to find that Munday’s establishment in the Houston MDA will enhance healthy competition ***absent a showing of quantifiable,***

reasonably achievable opportunity in the market in excess of the amount needed for Munday to exceed its break-even point without harming Landmark.

255. Adjustments made to accommodate an addition in a market where ***achievable opportunity does not exist in substantial numbers*** is, in essence, the antithesis of healthy competition and will necessarily impact consumers negatively.

256. Although consumers who purchase vehicles from a dealer who has adjusted its gross profit per vehicle downward to accommodate an addition to its dealer network will likely drive away feeling that they made a good deal, they will not remain satisfied for long if that dealer offsets its accumulating losses in gross profits per vehicle or its increased advertising costs per new vehicle sold by, for example, hiring less qualified service technicians at smaller salaries.”

260. ***Because Munday and GM have failed to identify a quantifiable amount of reasonably achievable opportunity in the Houston MDA, it is impossible to know whether the issues unique to north Houston indicate a real need for an additional to the market as a whole or simply confirm that the existing dealers body is no longer well-placed.***” (Emphasis added). (PFD at pp. 47, 64, 67, 68, 69).

The Board’s *Landmark Chevrolet* decision shows the crucial importance of knowing the amount of reasonably achievable opportunity for MB in the Austin AOR *and* of knowing the proposed Swickard dealership’s breakeven point. Without such knowledge the Board must assume Protestant will be harmed, that destructive competition would ensue upon Swickard’s entry into the market, and that the public interest will not be furthered.

Your Honors also misinterpret Protestant’s reference to case studies in which adding a new MB dealership caused existing dealers to lose sales. The loss in sales by existing dealership resulted because the lost opportunity in those markets, which was reasonably available for capture, was insufficient to profitably support both the

new and the existing dealers. At page 64 of the PFD, your Honors attribute an asserted “standard” to Protestant that Protestant does not espouse. (PFD at p. 64). Protestant’s standards for deciding this case are based on the Board’s *Landmark Chevrolet* and *Lee Trevino Ford* decisions, which your Honors have interpreted incorrectly. Those decisions show that an existing dealer is not harmed within the meaning of the Code because it might lose some sales or profits to a new dealership when the lost opportunity in the market, reasonably available for capture by the brand, is large enough to support both the existing and the proposed dealerships, thus allowing the existing dealer to make up sales or profits lost to the new dealer by capturing untapped opportunity available in the market. *That is not the situation here.*

Finding of Fact No. 155 and the statements at pages 63 and 64 should be modified to state that, “An existing dealer is not necessarily harmed because it must share the market with a new dealership, even though the existing dealer experiences some lost sales or profits after the dealer network is expanded, when opportunity realistically achievable for the brand in the market is sufficient for the new dealer to breakeven and for the existing dealer to adjust its business strategy to capture untapped opportunity reasonably available for capture.”

27. Protestant excepts to Finding of Fact No. 156 and the statements at page 70 of the PFD concerning lost service opportunity because they are based on the incorrect standard of theoretical loss as opposed to the proper standard of loss that is reasonably available for capture. *See* Exception Nos. 8, 9, 13, 19, 21. Your

Honors state that Protestant failed to support its assertion that no lost service opportunity exists or that the only way the new dealership could be profitable is to take service work away from Protestant. (PFD at 70). Your Honors improperly shift the burden of proof to Protestant and also disregard the most recent SOI reports in evidence. Those SOI reports indisputably establish that all the service opportunity reasonably available for capture is being captured by the existing MB dealers. (Ex. I-25, Ex. P-26, Ex. P-27, Ex. P-28, Ex. P-29, Ex. P-61, Ex. P-62). Because that is so, the proposed dealership will necessarily take service business from Protestant. The Board recognized in *Landmark Chevrolet* that this kind of cannibalization occurs when there is insufficient reasonably achievable lost *sales* opportunity in the market. Such cannibalization also will occur when there is insufficient lost *service* opportunity reasonably available for capture in the market. Finding of Fact No. 156 and the statements on page 70 of the PFD should be modified to provide that, “The existing MB dealers are already capturing all the service opportunity that is realistically available for capture in the Austin AOR and Protestant’s AOI. The proposed dealership would, therefore, take service business away from Protestant.”

28. Protestant excepts to Finding of Fact No. 157 concerning the percentage of MB vehicles serviced by the existing dealers in “the Austin AOI” because the finding is misleading and based on older, outdated SOI reports. By referring in the PFD to “the Austin AOI,” Protestant assumes your Honors mean “MB Austin’s AOI.” The most recent SOI reports in evidence show that since May

2019, the SOI scores for Protestant's AOI have been equal to, or higher than, national, regional, area, market, and market tier benchmarks. (Ex. P. 28, P-29, Ex. P-61, P-63). Your Honors give no explanation why these recent reports are ignored in favor of older reports. The Board should know about these recent reports that are in the evidentiary record and what they show. Finding of Fact No. 157 should be modified to state that, "Since May 2019, the SOI scores for Protestant's AOI have been equal to, or higher than, national, regional, area, market, and market tier benchmarks."

29. Protestant excepts to Finding of Fact No. 158 concerning service work in Austin because it is based on the incorrect standard of theoretical service loss as opposed to the proper standard of service loss that is realistically available for capture. As shown in Exception Nos. 8, 9, 13, 19, 21, and 24, and by the most recent SOI reports in evidence, the existing MB dealers already are capturing all the service opportunity that is realistically available for capture. Consequently, the proposed dealership will necessarily take service business from Protestant. Finding of Fact No. 158 should be modified to state that, "MB Austin will lose service business to the proposed dealership because MB Austin and MB of Georgetown are capturing all the service opportunity that is realistically available for capture in MB Austin AOI."

30. Protestant excepts to Finding of Fact No. 159 concerning service work in Austin because it is based on the incorrect standard of theoretical service loss as opposed to the proper standard of service loss that is realistically available for

capture. As shown in Exception Nos. 8, 9, 13, 19, 21, 24, and 26, and by the most recent SOI reports in evidence, the existing MB dealers are already capturing all the service opportunity that is realistically available for capture. Consequently, the proposed dealership will necessarily take service business from Protestant. Finding of Fact No. 159 should be modified to state that “MB Austin and MB of Georgetown presently are capturing all the service opportunity that is realistically available for capture in MB Austin AOI.”

31. Protestant excepts to Finding of Fact No. 160 and the statements at pages 62 and 75 of the PFD concerning harm to the existing MB dealerships from sales lost to the proposed Swickard dealership. The findings and statements are based on the incorrect standard of theoretical lost sales opportunity rather than on the correct standard of lost sales opportunity that is reasonably available for capture by the MB brand from its competitors. The finding and statements also improperly assume that the new dealership would capture all the claimed lost sales opportunity “in the market”—which Protestant assumes is the Austin AOR. The Board’s decision in *Landmark Chevrolet*—as well as the expert testimony in this case — shows that such an assumption is unrealistic and unwarranted. Finding of Fact No. 160 and the statements at pages 62 and 75 of the PFD should be modified to provide that, “MB Austin will experience a loss of sales to the proposed dealership because neither Swickard nor MBUSA proved that the amount of lost sales opportunity realistically available for capture in the Austin AOR is sufficient to profitably

support the proposed dealership. Consequently, the proposed dealership will cannibalize sales from the existing MB dealers, primarily MB Austin.”

32. Protestant excepts to Finding of Fact No. 161 concerning the total amount of lost sales opportunity in the Austin AOR. The finding is misleading because, as shown in Protestant’s previous Exceptions, it is based on the incorrect standard of unachievable, theoretical lost sales opportunity. The lost opportunity numbers recited in the finding are not realistically achievable or available for capture because all the experts admitted that gross loss and insell will remain in the Austin AOR even if the MB brand exceeds 100% of its expected share of the Austin AOR. The expert for Swickard and MBUSA, Mr. Farhat, made no reduction to the the lost sales opportunity number to account for the gross loss and insell that would remain in the Austin AOR if the proposed Swickard dealership were established. Mr. Farhat also included gross loss and insell located outside the 40-mile radius of the proposed Swickard dealership, which is the purported penetration profile for that dealership. The numbers in the finding are, therefore, inflated and unreliable. Finding No. 161 should be modified to state that, “Swickard and MBUSA failed to prove the amount of lost sales opportunity that is realistically available for capture by the MB brand from its competitors in the Austin AOR.”

33. Protestant excepts to Finding of Fact No. 163 concerning zip codes because it is misleading. The finding incorrectly suggests that the concept of gross loss takes into account “locational issues.” The testimony was undisputed that gross loss, measured at the zip code level, does not account for dealership locations. Dr.

Hatch and Mr. Farhat both testified that the gross loss concept, as applied at the zip code level, does not consider the influence of the dealership locations of the competing brands. In other words, measuring gross loss at the zip code level omits any consideration of dealership locations. (Tr. 1195:23-25, Tr. 1197:15-19). To avoid misleading the Board about the gross loss analysis, Finding of Fact No. 163 should be modified to state that, “Calculating gross loss by Zip Code takes into account the actual registrations in that area as well as demographics, but does not take into account or consider the influence of the dealership locations of the competing brands.”

34. Protestant excepts to Finding of Fact No. 164 and the statement at page 62 of the PFD concerning the performance of the South Austin BMW dealership. No reliable evidence supports this finding or your Honors’ statement that, “the new BMW dealership has experienced over 100 percent sales effectiveness . . .” MBUSA’s Mr. Farhat testified that he did not determine the number of sales made by each of the Austin BMW dealers. (Tr. 1642:6-10). Mr. Gomez, MBUSA’s sales operation manager for Market 12 until 2018, testified, over MB of Austin’s “best evidence” objection, that the South Austin BMW store had sold “760-something through October . . .” (Tr. 1084:11-16). He also testified, over Protestant’s hearsay objection, that BMW’s North Austin store was selling fewer new units in 2019 than in prior years. (Tr. 1688:16-23). Mr. Gomez’s testimony was improper and your Honors erred in not excluding it. In any event, MBUSA produced no documentary evidence to support Mr. Gomez’s statement or that MB

was losing sales to BMW because of the establishment of the South Austin store. Nor was any such data produced to Protestant by MBUSA in response to MB of Austin's discovery requests, which also supported the exclusion of Mr. Gomez's hearsay testimony. The finding should be modified to state that, "Neither Swickard nor MBUSA proved that MB is experiencing loss due to the new South Austin BMW dealership." The statement at page 62 of the PFD should be withdrawn.

35. Protestant excepts to Finding of Fact No. 165 concerning the proposed Swickard dealership's projected new vehicle sales. The finding is both improper and misleading. The finding is improper because it is a mere summary of Mr. Farhat's testimony. "Mere recitals of testimony or references to or summations of the evidence are improper." *Texas Health Facilities Comm'n v. Charter Medical-Dallas*, 665 S.W.2d 446, 452 (Tex. 1984). The finding is misleading because it ignores projected sales of new vehicles of 916 made by MBUSA and 775 made by Swickard—the folks actually in the business of selling motor vehicle business—both which exceed the inflated lost sales opportunity of 755 units. To avoid misleading the Board and to make a proper finding, Finding of Fact No. 165 should be modified to state that, "The only reliable projections in evidence show that the proposed dealership will sell more new vehicles per year than the lost sales opportunity that is realistically available for capture by the MB brand from its competitors in the Austin AOR."

36. Protestant excepts to Finding of Fact No. 166 because it is based on the incorrect standard of theoretical lost sales opportunity and an unreliable sales

projection as shown in Protestant's previous Exceptions. The 755 units of lost sales opportunity referenced in the finding is an unreliable, inflated number based on a calculation of theoretical loss as opposed to a loss figure that is realistically available for capture by the MB brand from its competitors. It is undisputed that gross loss and insell would remain in the Austin AOR even if the proposed Swickard dealership were established. But Mr. Farhat made no adjustment to his 755 figure to account for this remaining gross loss and insell or to account for the gross loss and insell located outside the 40-mile radius that Mr. Farhat developed for the proposed dealership based on the penetration profiles of Protestant and MB of Georgetown. Finding of Fact No. 166 should be modified to state that, "Swickard and MBUSA failed to prove that the proposed dealership will not take sales from the existing MB dealers."

37. Protestant excepts to Finding of Fact No. 167 concerning Protestant's ability to withstand competition from the proposed dealership. The finding is based on an incorrect standard. As shown in Protestant's previous Exceptions, an existing dealer is not required to sacrifice its profits to a new dealership when the lost opportunity in the market that is reasonably available for capture by the brand is less than the amount necessary to profitably support the new dealership. The Board does not require the existing dealers to subsidize or support the new dealer. *Landmark Chevrolet*, PFD at pp. 30-31, 32, 35. Finding of Fact No. 167 should be modified to state that, "Swickard and MBUSA failed to prove that the amount of lost

opportunity realistically available for capture is sufficient enough to profitably support the Swickard dealership without taking profits from MB Austin.”

38. Protestant excepts to Finding of Fact No. 170 and the statements at pages 70 and 71 of the PFD concerning Protestant’s profitability in relation to sales volume and incentive payments. The finding is misleading. Protestant’s profitability is largely dependent on its ability to hit MBUSA’s sales and service performance goals and thus obtain incentive payments from MBUSA. (Ex. I-69 @ 051, 052). In 2018, Protestant had an operating profit of only \$667,011. (*Id.*). During that year, Protestant collected approximately \$4.7 million in incentives for meeting MBUSA’s sales and service performance-related targets. (*Id.*). Swickard and MBUSA did not analyze the impact of the loss of sales to the proposed dealership on Protestant’s ability to achieve the sales and service-related incentives and performance bonuses it needs to be more than marginally profitable. Your Honors excuse their failure to do so by wrongly shifting the burden of proof to Protestant, stating at pages 70 and 71 of the PFD, that no evidence was presented to show that MB Austin will not qualify for incentive payments if the new dealership opens or lost some service business to it. It was Swickard’s and MBUSA’s obligation to present such evidence. Finding of Fact No. 170 and the statements at page 70 and 71 of the PFD should be modified to provide that, “The low amount of realistically achievable sales and service opportunity available for capture in the Austin AOR indicates that the establishment of the proposed Swickard dealership likely would keep MB Austin from meeting the thresholds necessary to achieve

incentive and bonus payments. Swickard and MBUSA produced no evidence to the contrary.”

39. Protestant excepts to Finding of Fact No. 179 concerning Protestant’s ability to adjust its business strategy once the proposed Swickard dealership is established. The finding wrongly assumes that enough “untapped opportunity in the market” exists to profitably support the existing MB dealers and the proposed dealership. As shown in Protestant’s previous Exceptions, Swickard and MBUSA failed to prove that the untapped sales and service opportunity realistically available for capture in the Austin AOR is sufficient for the proposed dealership to be successful without being subsidized by the existing MB dealers. As shown in Exception No. 23, the Board in *Landmark Chevrolet* held that an existing dealer must “adjust its business strategy to capture untapped opportunity in the market,” but the existing dealer is not required to sacrifice business to a new dealer when the untapped opportunity in the market is insufficient to profitability support the new dealer. Finding of Fact No. 179 should be modified to state that, “MB Austin should not be required to adjust its business to meet competition from the proposed Swickard dealership because Swickard and MBUSA failed to prove that the amount of lost opportunity in the Austin AOR realistically available for capture by the MB brand is sufficient to profitably support the existing dealers and the proposed dealership.”

40. Protestant excepts to Finding of Fact No. 184 and the statement made on page 68 of the PFD concerning Mr. Stockton’s testimony. The finding and

statement assert that Mr. Stockton's estimate of Protestant's profit loss did not account for economic and population growth in Austin and is based on non-statistically significant calculations. Your Honors provide no evidentiary support for the statement and finding. The second sentence of Finding of Fact No. 184 and the statement made at page 68 of the PFD should be withdrawn.

41. Protestant excepts to Finding of Fact No. 185 and the statements at page 68 of the PFD concerning Mr. Stockton's use of the gravity model. The finding and statement mischaracterize Mr. Stockton's testimony. Mr. Stockton never claimed that the sales losses of existing dealerships would follow on a one-to-one basis with lost territory under the gravity model. Mr. Stockton testified that market share increases would offset some of the territory loss, and that Protestant's sales losses would be somewhat less than the territorial losses to the proposed Swickard dealership. (Ex. P-1 @ 016 [¶ 47]). He also pointed out that in other examples in which MBUSA added dealerships, market share increases offset some, but not all territorial losses. (Ex. P-1 @ 013 [¶ 41]). He noted that sales losses were approximately two-thirds of the territorial losses. (Tr. 994:7-10). Finding of Fact No. 185 and the statements at page 68 of the PFD should be withdrawn.

42. Protestant excepts to Finding of Fact No. 186 and the statement made on page 68 of the PFD concerning Mr. Stockton's testimony concerning the gravity model. The finding and statement wrongly assert that Mr. Stockton "admitted that his gravity model did not accurately capture MB Austin's performance in its fixed operations." Mr. Stockton made no such admission. Mr. Stockton's testimony was

that the proposed dealership's impact on Protestant's service business "probably" would be less than expected by the gravity model. (Tr. 1019:14-18). The gravity model is a useful predictive model – *not* a precise measurement. Finding of Fact No. 186 and the statement at page 68 of the PFD should be withdrawn, or at the very least modified to state that, "Mr. Stockton acknowledged that the impact on MB Austin's service business by the proposed Swickard dealership would probably be less than expected."

43. Protestant excepts to Finding of Fact No. 189 and the statements made on page 69 of the PFD concerning the methodologies used by Mr. Stockton and Dr. Hatch. The finding and statements wrongly accuse them of using methodologies that have not accepted by the automotive industry or by the Board. In fact, the Board and automotive manufacturers and distributors for decades have used "net loss" to measure lost opportunity in market areas. MBUSA's market expert, Mr. Farhat, used it, as your Honors recognize in the PFD. (PFD at pp. 27, 51-52). The finding and statements also wrongly assert that the methodologies used by Mr. Stockton and Dr. Hatch are "not improvements" upon the methodologies used by MBUSA's experts and "do not hold up when tested in real-world examples of new dealership establishments." The downward adjustment that Dr. Hatch and Mr. Stockton recommended concerning gross loss and insell are supported by "real-world" data and necessary to measure the lost sales opportunity that is realistically available for capture by a brand from its competitors, which is the standard the Board set forth and applied in *Landmark Chevrolet*. The expert testimony and reports of Mr. Farhat

and Mr. Stockton together show that every Texas AOR has gross loss for every competitive brand. (Tr. 571:7-19, Tr. 939:4-24). At the hearing, Mr. Farhat admitted that “[t]here’s no claim . . . that there will no longer be gross loss . . .” if the proposed dealership is established in the Austin AOR. (Tr. 1602:10-11). During 2018, gross loss remained in all Texas AORs even where MB’s registration effectiveness was far greater than 100%. (Ex. I-65 @ 096, Ex. I-66 @ 033, Ex. P-1 @ 241). Dr. Hatch testified that gross loss would likely remain in the Austin AOR if MB of Austin were achieving 150% of benchmark in the AOR. (Tr. 1160:22-1161:7). As to insell, Mr. Farhat testified that insell “occurs in markets for all brands.” (Tr. 604:2-3). Mr. Farhat also admitted that insell remains in a market even when a brand achieves 100% or greater registration effectiveness in that market. (Tr. 570:22-571:6). Dr. Hatch agreed, testifying that insell would remain in the Austin AOR if the MB brand were 150% of the benchmark. (Tr. 1199:1-20). Mr. Farhat’s analysis also showed that gross loss and insell were located outside the penetration profile he developed for the proposed dealership. (Ex. I-65 @ 096, 097, 098, 099). Finding of Fact No. 189 and the statements made on page 69 of the PFD should be modified to provide that, “Mr. Stockton and Dr. Hatch used methodologies previously accepted by the Board. Those methodologies demonstrate that the gross loss and insell numbers for the Austin AOR must be adjusted downward to account for the gross loss and insell that would remain in the Austin AOR even if the proposed dealership were established and the MB brand

achieved more than 100% of market share and to account for the gross loss and insell located outside of the proposed dealership's penetration profile.”

44. Protestant excepts to Finding of Fact No. 190 and the statements on page 73 of the PFD concerning lost sales and service opportunity because they are unsupported by reliable evidence. As shown in Protestant's previous Exceptions, Swickard and MBUSA failed to prove that sufficient realistically achievable lost sales and service opportunity exist in the Austin AOR to support the proposed dealership without adversely impacting Protestant. Finding of Fact No. 190 and the statements on page 73 of the PFD should be modified to state that, “Swickard and MBUSA failed to prove that sufficient realistically achievable lost sales opportunity and lost service opportunity exist in the Austin AOR to support the proposed dealership without harming Protestant.”

45. Protestant excepts to Finding of Fact No. 191 concerning Protestant's ability to compete with the proposed dealership. The finding is misleading because it wrongly assumes that enough sufficient realistically achievable lost sales and service opportunity exists in the Austin AOR to support the proposed dealership profitably and from which Protestant can recoup sales and service business lost to the new dealership. The Board's *Landmark Chevrolet* decision shows that an existing dealer is not required to sacrifice its profits to the proposed new dealership if the amount of realistically achievable lost opportunity in the relevant market is less than the number of new units the proposed dealership must sell to breakeven. *See Landmark Chevrolet*, PFD at pp. 30-31. In *Landmark*, the Board recognized

that the protesting dealer could “adjust its business strategy to capture “*untapped opportunity in the market*” if such untapped opportunity is more than enough to support the new dealership and allow the protesting dealer to recoup sales and service that might be lost to the new dealer. *Id.* Finding of Fact No. 191 should be modified to state that, “MB Austin’s diversification and profitability would allow it to compete effectively with the proposed dealership only if the lost sales and service opportunity realistically available for capture by the MB brand in the Austin AOR was more than sufficient to profitably support the proposed dealership and allow MB Austin to recoup sales and service business lost to the new dealership.”

46. Protestant excepts to Finding of Fact No. 192 and the statements on page 73 of the PFD concerning harm to Protestant. The finding and statement are not supported by substantial evidence. As shown in Protestant’s previous Exceptions, Swickard and MBUSA failed to prove that sufficient realistically achievable lost sales and service opportunity exist in the Austin AOR to support the proposed dealership without harming Protestant. Finding of Fact No. 192 and the statements at page 73 should be modified to provide that, “Swickard and MBUSA failed to prove that MB Austin will suffer little or no harm from the addition of the proposed dealership because they failed to prove that enough realistically achievable lost sales and service opportunity exists in the Austin AOR to support the proposed dealership profitably without harming Protestant.”

47. Protestant excepts to Finding of Fact No. 193 because it is a mere conclusion and not reasonably supported by substantial evidence considering the

reliable and probative evidence in the record as a whole. Mere conclusions are not proper findings of fact. *Charter Medical-Dallas*, 665 S.W.2d at 451. The finding also overlooks Swickard and MBUSA's failure to prove that enough realistically achievable lost sales and service opportunity exists in the Austin AOR to support the proposed dealership profitably without harming Protestant. Finding of Fact No. 193 should either be withdrawn or modified to state that "The criterion of harm to the protesting franchised dealer weighs in favor of denying the Application."

48. Protestant excepts to Finding of Fact Nos. 194 and 202 and the statements at pages 60, 61, and 75 of the PFD concerning customer convenience. The finding and statements are misleading. As shown in previous Exceptions, an increase in customer convenience is not desirable and contrary to the public interest when, as here, the lost opportunity realistically available for capture by the MB brand has not been shown to be sufficient to profitably support the new dealership without harming the existing MB dealers. *See Lee Trevino Ford*, PFD at p. 28 (convenience of the facility to the public is not in and of itself controlling "as there may well be other overriding factors which will govern if the consequences of the granting the license are likely to be more detrimental than beneficial."). Finding of Fact Nos. 194 and 202 and the statements at pages 60, 61, and 75 of the PFD should be modified to state that, "Although establishing the proposed Swickard dealership could potentially result in modest increase in customer convenience, the potential benefit is outweighed by Swickard and MBUSA's failure to prove that the lost

opportunity realistically available for capture by the MB brand is sufficient to profitably support the new dealership without harming the existing MB dealers.”

49. Protestant excepts to Finding of Fact Nos. 194 and 200 and the statements at pages 60, 61, and 75 of the PFD concerning price competition, customer convenience, and the public interest. The finding and statements are misleading. As shown in previous Exceptions, the Austin market is currently “hypercompetitive.” The findings and statements also ignore the fact a brand can always enhance customer convenience by establishing a new dealership that is closer to a part of the market than are the brand’s existing dealers. Moreover, an increase in price competition and customer convenience is not desirable and contrary to the public interest when, as here, the lost opportunity realistically available for capture by the MB brand has not been shown to be sufficient to profitably support the new dealership without harming the existing MB dealers. *See Lee Trevino Ford*, PFD at p. 28. Cannibalization of sales and service is not in the public interest. An unprofitable dealership is not in the public interest. Finding of Fact Nos. 194 and 200 and the statements at pages 60, 61, and 75 of the PFD should be modified to state that, “Although establishing the proposed Swickard dealership could potentially result in modest increases in advertising for the MB brand, the availability of inventory in the market, access to the MB brand, convenience of service, and choice and competitive pricing for consumers, those potential benefits are outweighed by Swickard and MBUSA’s failure to prove that the lost opportunity

realistically available for capture by the MB brand is sufficient to profitably support the new dealership without harming the existing MB dealers.”

50. Protestant excepts to Finding of Fact Nos. 195, 199, and 201, and the statements at pages 24 and 75 of the PFD regarding employment and economic contributions to the local economy expected to be generated by the proposed Swickard dealership. The findings are speculative because Swickard failed to prove when, if ever, the proposed dealership can be profitable and thus viable. As shown in previous Exceptions, Swickard provided only a few guesswork expenses and failed to provide a breakeven analysis for the dealership. (Tr. 75:14-15, Tr. 98:1-14, Tr. 119:1-7, Tr. 331:2-22; Ex. A-2). An unprofitable dealership will not “support” 376 full-time positions for the dealership and other businesses, nor will it generate millions of dollars for the local economy. The findings also are misleading because they lump together the number of dealership employees with the number of employees of “indirect businesses.” The Board should know how many employees the proposed dealership is reasonably projected to have. The notion expressed in footnote 159 at page 24 of the PFD that the proposed dealership would increase full-time employment at restaurants, child care facilities, hospitals, and truck transportation is sheer speculation. Finding of Fact Nos. 195, 199, and 201 and the statements at pages 24 and 75 of the PFD should be withdrawn, or at the very least modified to state that, “Swickard did not provide a reliable estimate of the number of full-time employees the proposed dealership would have if established and profitable, or a reliable estimate of indirect employment or other contributions to

the local economy that would result from the establishment of the proposed dealership.”

51. Protestant excepts to Finding of Fact No. 203 that the addition of the proposed dealership will be in the public interest because it is a mere conclusion and not reasonably supported by substantial evidence considering the reliable and probative evidence in the record as a whole. Mere conclusions are not proper findings of fact. *Charter Medical-Dallas*, 665 S.W.2d at 451. Moreover, the finding does not take into account Swickard’s failure to prove (1) if or when the proposed dealership will be profitable, and (2) that any profits will not be made at the expense of Protestant because of the lack of realistically achievable lost opportunity for the MB brand in the Austin AOR. Unprofitable dealerships are not in the public interest. *A.C. Collins Ford*, PFD at p. 22; *Lee Trevino Ford*, PFD at p. 29. The public interest is not served when the market potential for a brand is not sufficient to enable its franchised dealers to operate profitably. *Landmark Chevrolet*, PFD at p. 35; *Lee Trevino Ford*, PFD at pp. 29, 33. As the Board pointed out in *Landmark Chevrolet*, when the number of units needed for the proposed dealership to breakeven is less than the reasonably achievable lost opportunity, the public interest is not served because cannibalization of sales will occur. Such destructive competition is not in the public interest. Finding of Fact No. 203 should be withdrawn or modified to state that, “Swickard and MBUSA failed to prove that establishing the proposed dealership would be in the public interest because they failed to prove if or when the proposed dealership will be

profitable or that any profits the proposed dealership makes will not come at the expense of Protestant because of the lack of realistically achievable lost opportunity for the MB brand in the Austin AOR.”

52. Protestant excepts to Finding of Fact Nos. 209-223 and to the statements at pages 77 and 78 of the PFD concerning economic projections because they are based on outdated, stale economic data and market data, and fail to account for the impact of COVID-19 on Austin’s current and future economy and motor vehicle market. These findings should be withdrawn and a recommendation made to the Board to remand this case for the taking of further evidence on current and reasonably foreseeable projections of economic conditions, financial expectations, and the market for new motor vehicles in the Austin AOR as a consequence of the COVID-19 pandemic.

53. Protestant excepts to Finding of Fact No. 213 that the Austin economy has been “recession-proof since 2008.” No evidence supports this statement. Current events show its unreliability. Finding of Fact No. 213 should be withdrawn.

54. Protestant excepts to Conclusion of Law No. 8 and the statements at pages 52, 54 and 55 of the PFD concerning the adequacy of MB sales and service representation in the Austin AOR. The conclusion is unsupported by proper basic findings of fact, based on an erroneous standard of theoretical lost sales and service opportunity in violation of the Board’s *Landmark Chevrolet* decision, is unsupported by substantial evidence and contrary to the credible evidence in the record. The statements at pages 52, 54, and 55 and Conclusion of Law No. 8 should

be modified to state that, “Swickard and MBUSA failed to prove that MB’s product lines are not being inadequately represented as to sales and service in the Austin AOR. Tex. Occ. Code § 2301.652(a)(1).”

55. Protestant excepts to Conclusion of Law No. 10 and the statements at page 62 of the PFD concerning the promotion of healthy inter-brand and intra-brand competition in the relevant markets because the conclusion is unsupported by proper basic findings of fact, is unsupported by substantial evidence and contrary to the credible evidence in the record. As shown in Protestant’s previous Exceptions, unhealthy competition occurs when, as here, the realistically available opportunity or market potential for a brand in the relevant market is insufficient to profitably support each of the brand’s existing and proposed dealers located in that market. Conclusion of Law No. 10 and the statements at page 62 of the PFD should be modified to provide that, “Swickard and MBUSA failed to prove that establishing the new dealership will promote healthy inter-brand and intra-brand competition in the relevant markets. Tex. Occ. Code § 2301.652(a)(3).”

56. Protestant excepts to Conclusion of Law No. 11 concerning harm to Protestant because the conclusion is unsupported by proper basic findings of fact, is unsupported by substantial evidence, and contrary to the credible evidence in the record. Swickard and MBUSA failed to prove that the realistically achievable “lost opportunity” for the MB brand in the Austin AOR is more than the number of new vehicles the proposed dealership must sell to breakeven, making the sales needed by the proposed dealership to likely be taken or “cannibalized” from Protestant. As

shown in Protestant's previous Exceptions, a brand's existing dealers are not required to sacrifice their profits to subsidize a proposed new dealership for the brand when the amount of realistically achievable lost opportunity for the brand cannot profitably support the new dealership. Conclusion of Law No. 11 should be modified to state that, "Swickard and MBUSA failed to prove that establishing the new dealership will not cause MB Austin to suffer significant harm. Tex. Occ. Code § 2301.652(a)(4)."

57. Protestant excepts to Conclusion of Law No. 12 concerning the public interest because the conclusion is unsupported by proper basic findings of fact, is unsupported by substantial evidence, and contrary to the credible evidence in the record. Licensing an unprofitable dealership is not in the public interest. Swickard and MBUSA failed to prove if or when the proposed dealership will be profitable or that any profits the proposed dealership makes will not come at the expense of Protestant because of the lack of realistically achievable lost opportunity for the MB brand in the Austin AOR. Conclusion of Law No. 11 should be modified to state that, "Swickard and MBUSA failed to prove that establishing the new dealership is in the public interest. Tex. Occ. Code § 2301.652(a)(5)."

58. Protestant excepts to Conclusion of Law No. 14 concerning current and reasonably foreseeable financial, economic, and market projections for the Austin AOR because the conclusion is based on stale, outdated evidence, unsupported by substantial evidence, and contrary to the credible evidence in the record. Despite past growth of the Austin AOR and its expected growth before the

intervention of the COVID-19 pandemic, Swickard and MBUSA failed to prove that enough realistically achievable lost sales and service opportunity exists in the Austin AOR to support the proposed dealership profitably without taking MB sales and service business from the existing dealers. As shown in Protestant's previous Exceptions, MBUSA's own expert analysis showed that the Austin market did not yet need three MB dealerships. Conclusion of Law No. 14 should be modified to state that, "Swickard and MBUSA failed to prove that current and reasonably foreseeable projections of economic conditions, financial expectations, and the market for new motor vehicles favor the establishment of a new MB dealership in South Austin. Tex. Occ. Code § 2301.652(a)(7)."

59. Protestant excepts to Conclusion of Law 15 concerning the burden of establishing good cause for establishing the proposed dealership because, for all the reasons set forth in the foregoing exceptions, the conclusion is unsupported by proper basic findings of fact, is unsupported by substantial evidence, and contrary to the credible evidence in the record. Swickard and MBUSA failed to carry their burden to prove good cause. Conclusion of Law No. 15 should be modified to state that, "Applicant failed to meet its burden of demonstrating good cause for the establishment of the proposed MB dealership in South Austin. Tex. Occ. Code § 2301.652(a)."

60. Protestant excepts to Conclusion of Law No. 16 because, for all the reasons set forth in the foregoing exceptions, Swickard's application should not be

granted. Conclusion of Law No. 16 should be modified to state that, “Applicant’s application for a new dealership should not be granted.”

CONCLUSION AND PRAYER

For the foregoing reasons, Protestant prays that its exceptions be in all things sustained; that your Honors amend the PFD to recommend to the Board that this case be remanded to SOAH for the taking of additional evidence concerning adequacy of representation, harm to Protestant, the public interest, and current and reasonably foreseeable projections of economic conditions, financial expectations, and the market for new motor vehicles in the Austin AOR in light of the COVID-19 pandemic. Alternatively, Protestant prays that your Honors amend the PFD to make the modifications and other relief requested in the foregoing Exceptions and to recommend to the Board that Swickard’s application to establish the proposed MB of South Austin dealership be rejected, and that Protestant’s protest be sustained. Protestant also prays for such other relief to which it has shown itself to be entitled.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that a true copy of the foregoing document has been delivered by via e-mail on July 24, 2020, to the following counsel of record in this proceeding:

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APPENDIX

TAB 1

Excerpts from *Landmark Chevrolet* PFD

comparison to expected sales after the addition of the Gunn dealership. (Tr. at 2404-2412) With respect to the Instant case, it is Landmark's position that, at the time this protest was initiated, the Houston MDA already had all the earmarkings of a highly competitive market that had reached its saturation point with respect to Chevrolet representation. Not only was there, with respect to the Chevrolet brand, no shortfall in the market based on a reasonable standard, the Chevrolet dealers in the market enjoyed less gross profit per new vehicle sold and paid more in advertising per new vehicle sold than the average Chevrolet dealer in the nation. Since Landmark went one step further in that it made less gross profit per new vehicle sold and paid more in advertising per new vehicle sold than the average Houston dealer, Protestant argues that it is ludicrous to suggest that Landmark will be able to overcome setbacks resultant from Munday's unjustified addition to the Houston MDA Chevrolet dealer body. Landmark also disputes the contention that Chevrolet is outdealed by Ford, asserting, among other things, that because Landmark consistently outperforms its intrabrand competitors in the Houston MDA, it should be counted not as one dealer, but four.

The upshot of Respondents' argument is that healthy marketplace competition will be enhanced through an addition to a dealer network where opportunity exists in the market to support such an addition. The ALJ agrees and is more than willing to accept, as a real life example of this, Respondents' interpretation of San Antonio MDA dealer network performance in response to the addition of the Gunn dealership in 1989. The ALJ is not, however, persuaded that the Instant case mirrors or in any way resembles the San Antonio case with respect to the amount of opportunity available in the market. In this case, Munday and GM ask the Board to find that Munday's establishment in the Houston MDA will enhance healthy competition absent a showing of quantifiable, reasonably achievable opportunity in the market in excess of the amount needed for Munday to exceed its break-even point without harming Landmark. On the other hand, there is no evidence in the record that Gunn was added to the San Antonio MDA absent this level of opportunity. Without evidence revealing that the two markets were similarly situated with respect to opportunity, a comparison of them is virtually meaningless.

At the same time, the ALJ is not persuaded by Landmark's insistence that it can do nothing more to acclimate to additional competition in the market. The ALJ is confident that additional adjustments can and will continue to be made by Landmark in many different areas of its operations in order to try to regain and/or maintain its profit margin. While its gross profit per new vehicle sold is indeed low compared to other dealers, it is not so low that it is incapable of being further lowered.³² Likewise, advertising expenses per new vehicle sold are not so high that they cannot be further increased.³³ The ALJ's primary concern, however, is that adjustments made to accommodate an addition in a market where achievable opportunity does not exist in substantial numbers is, in essence, the antithesis of healthy competition and will

³² Landmark's gross profit per new vehicle sold in 1992 was \$1,366. In 1993, it increased to \$1,726. (Ex. C-52 and Ex. GM-139)

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recoup or maintain their bottom lines and those dealers, in turn, must continue the process until no dealer is left unaffected. In this way, an addition to the dealer body where sufficient opportunity has not been verified is likely to have ramifications in all corners of the market. In the end, dealership operational strategies are altered to the public's detriment in an effort to regain or retain profit. In this case, the 1992 shortfall in the Northern Houston Area according to Mr. Anderson's calculations, which includes areas outside of Munday's penetration profile, equaled 705 units. (Ex. GM-98, p. A7) This is well under the number of units Munday needs to break even. In the unlikely event that Munday could capture all of that shortfall, the remainder needed to keep the dealership viable would have to be cannibalized from Landmark and Robbins. Without quantifiable achievable opportunity in the market beyond that, Landmark and Robbins would then be relegated to cannibalizing from other competitors within the market. For one or more of the Houston MDA dealers who may be struggling to attain a fraction of Landmark's level of success, an unneeded addition may signal the death knell. Thus, the likelihood that the aforementioned scenario would be played out in the Houston MDA is great and, in the ALJ's opinion, outweighs the comparatively small benefit offered by Munday in relation to decrease in distance between a Chevrolet dealer and its interbrand competitors or the average consumer in the Spring AGSSA. That being said, language from the Board decision in the *Trevino* case, ironically quoted in Respondents' closing arguments, eloquently sums up the predicament Munday and GM are faced with in this case:

"However, a critical question exists in this case of whether the market is adequate to support another dealership . . . The question of whether there is sufficient market is of critical importance because if the market is not sufficient to enable dealers to operate *profitably*, the result of such circumstance will be detrimental to the public interest as there can be little doubt but that dealers who are not able to operate profitably are also not able to properly take care of the needs of their customers and the public."³⁴

(Emphasis added)

Given that Munday and GM have failed to answer the most critical questions related to whether the Houston MDA was, during the relevant time period, a market with enough opportunity to support another dealership, the ALJ is unable to recommend a finding that Munday's addition would be beneficial to consumers in the Houston MDA.

Thus, the ALJ is of the opinion that Munday and GM have failed to establish good cause for the establishment of the Munday dealership by a preponderance of the credible evidence. Based on this conclusion, the ALJ recommends that the Board find that Landmark would have prevailed in its protest of Munday's application had it not withdrawn its protest.

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246. There is insufficient evidence in the record to show that this case mirrors or in any way resembles the San Antonio case with respect to the amount of opportunity available in the market.
247. In this case, the record reflects that Munday and GM are asking the Board to find that Munday's establishment in the Houston MDA will enhance healthy competition absent a showing of quantifiable, reasonably achievable opportunity in the market in excess of the amount needed for Munday to exceed its break-even point without harming Landmark.
248. There is insufficient evidence in the record to show that Gunn was added to the San Antonio MDA absent quantifiable, reasonably achievable opportunity in the market in excess of the amount needed for Gunn to thrive without harming existing dealers.
249. Without evidence revealing that the Houston MDA and the San Antonio MDA were similarly situated with respect to opportunity, a comparison of them is virtually meaningless.
250. Additional adjustments can and will continue to be made by Landmark in many different areas of its operations in order to try to regain and/or maintain its profit margin in response to Munday's entry into the Houston MDA.
251. Landmark's gross profit per new vehicle sold in 1992 was \$1,386. In 1993, it increased to \$1,726. (Ex. C-52 and Ex. GM-139)
252. While Landmark's gross profit per new vehicle sold is indeed low compared to other dealers, it is not so low that it is incapable of being further lowered.
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would, in the first full year that Munday is in operation, likely do worse in terms of absolute numbers of sales and profit than it had in the previous year.

Munday and GM assert that, irrespective of any findings in Landmark's favor on the issue of profits, they are entitled to finding in their favor on the issue of harm as long as Landmark's very existence is not called into question by Munday's establishment in the Spring AGSSA. The crux of Landmark's argument, on the other hand, is that harm has been established, in accordance with the statute, if the Board finds that Landmark will profit less than it would have had Munday not been added to the Houston MDA dealer network. Landmark argues that its viability is not relevant to a finding of harm nor need it be shown that it would lose business from year to year in terms of absolute numbers in order to prevail on the issue of harm.

Thus, the issue to be determined is whether Landmark's lost profitability contentions are applicable to the statute. Stated another way, when all is said and done, Landmark's success or failure on the issue of harm rests in the answer to the following question: Did the Legislature intend to require existing dealers in a market with little to no opportunity above and beyond that which is already being captured to forgo their profitability for the benefit of a new dealer? To answer this question in the affirmative seems exceedingly unfair to Landmark. At a low point in Houston's economic history but with an eye toward the future, Landmark built, at great expense and with GM's full blessing, a facility that not only met but well exceeded GM's requirements. Much has been done in order that Landmark might solidify its place within the dealer network. If the Board adopts Munday's interpretation of harm without some real indication that opportunity exists, Landmark will likely work even harder and sacrifice even more to acquire less. The ALJ is hard-pressed to see the equitable nature of that arrangement.

Munday and GM point out that prior Board decisions on the issue of harm support the proposition that much more is required to prove harm than that an existing dealer would be less profitable once a new dealer has entered its market. This is true indeed. The Board has clearly ruled, on a number of occasions, that an existing dealer in a flourishing market where opportunity looms large is not necessarily "harmed" simply because it must now share the market with a new dealer, even if it means that the existing dealer will profit less after the dealer network expands.³⁰ It is appropriate for the Board to expect a protesting dealer in danger of losing profits to acclimate itself to an addition to the dealer body by adjusting its business strategy to capture as-yet untapped opportunity in the market. This case is distinguishable from prior cases before the Board because of Respondents' failure to provide a sufficient amount of evidence in the record to support a finding that such opportunity exists in any significant

³⁰ *Bill Munday Pontiac, Inc. v. Hendrix GMC Trucks & Rex Hawes Pontiac GMC*, Proceeding No. 213, Final Order denying Protest-March 13, 1981; *Moritz Cadillac v. Holiday Lincoln-Mercury*, Proceeding No. 266, Final Order denying Protest-September 30, 1982.

recoup or maintain their bottom lines and those dealers, in turn, must continue the process until no dealer is left unaffected. In this way, an addition to the dealer body where sufficient opportunity has not been verified is likely to have ramifications in all corners of the market. In the end, dealership operational strategies are altered to the public's detriment in an effort to regain or retain profit. In this case, the 1992 shortfall in the Northern Houston Area according to Mr. Anderson's calculations, which includes areas outside of Munday's penetration profile, equaled 705 units. (Ex. GM-98, p. A7) This is well under the number of units Munday needs to break even. In the unlikely event that Munday could capture all of that shortfall, the remainder needed to keep the dealership viable would have to be cannibalized from Landmark and Robbins. Without quantifiable achievable opportunity in the market beyond that, Landmark and Robbins would then be relegated to cannibalizing from other competitors within the market. For one or more of the Houston MDA dealers who may be struggling to attain a fraction of Landmark's level of success, an unneeded addition may signal the death knell. Thus, the likelihood that the aforementioned scenario would be played out in the Houston MDA is great and, in the ALJ's opinion, outweighs the comparatively small benefit offered by Munday in relation to decrease in distance between a Chevrolet dealer and its interbrand competitors or the average consumer in the Spring AGSSA. That being said, language from the Board decision in the *Trevino* case, ironically quoted in Respondents' closing arguments, eloquently sums up the predicament Munday and GM are faced with in this case:

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Thus, the ALJ is of the opinion that Munday and GM have failed to establish good cause for the establishment of the Munday dealership by a preponderance of the credible evidence. Based on this conclusion, the ALJ recommends that the Board find that Landmark would have prevailed in its protest of Munday's application had it not withdrawn its protest.

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23. Neither the AGSSA nor the MDA are exclusive territories assigned to a particular dealer, as dealers are free to sell vehicles anywhere within the United States. (Tr. at 323-324)
24. At the time it initiated its protest of Munday's February 1, 1993 application for a new franchised motor vehicle dealer's license, Landmark was located directly on Interstate 45, with almost 3,000 feet of interstate frontage, in AGSSA 12. (Ex. C-54 and Tr. at 1101)
25. William "Bill" Heard purchased Landmark in 1984, then consisting of almost 12 acres, for approximately \$12 million. (Tr. at 1096)
26. Between 1984 and 1992, the Landmark property was expanded with the addition of six adjoining, undeveloped acres, at a price of \$2 million, and the lease of an additional five acres, formerly a Volkswagen dealership, with a lease price of roughly \$3 to \$4 million. (Tr. at 1097, 1100-1101)
27. Landmark paved the undeveloped acreage acquired between 1984 and 1992 and constructed a truck center, a commercial vehicles center, and a body shop at a total cost of more than \$5 million. (Tr. at 1098-1099)
28. The former Volkswagen dealership property leased by Landmark was transformed into Landmark's used vehicle outlet. (Tr. at 1100)
29. When Mr. Heard first purchased Landmark, the dealership had only been selling 100 new Chevrolets per month. (Tr. at 1176)
30. Due in no small part to its aggressive operating strategy, Landmark sold 3,944 new Chevrolets in 1991, 5,166 new Chevrolets in 1992, and 6,403 new Chevrolets in 1993. (Ex. MCG-28 and Tr. at 1101, 1195-1196)
31. In 1992 and 1993 Landmark was the number one Chevrolet dealer in the nation in terms of new vehicle sales. (Tr. at 1101)
32. The Munday dealership was proposed to be located in AGSSA 18, in the northern portion of the Houston MDA, in an area also referred to as Spring, Texas, or the Spring AGSSA. (Tr. at 20-22, 25 and Ex. MCG-6)
33. The straight-line distance between Landmark and the proposed Munday location is 10 miles. (Tr. at 31, 93-94)
34. The Munday dealership was to encompass nine acres of land, with 550 feet of frontage on FM 1960. (Tr. at 24-25, 66-67)
35. Munday's facility, which was to comprise approximately 34,000 square feet, including 22 service stalls, and a 14 stall body shop, intended to stock 260 units

202. Given that, in 1992, Lawrence Marshall failed the 30-30 test used by GM's expert to evaluate whether a dealership is rightfully classified as a non-MDA dealer by only a handful of units, it would not have been unreasonable to consider it an MDA dealer.
203. If Lawrence Marshall had been considered part of the MDA in 1992, the census tracts in its AGSSA that fell below expected penetration, if any, would have effectively increased the total gross loss available to Munday. (Tr. at 2137-2138)
204. Respondents' failure to quantify gross loss according to a reasonable standard precludes accurate calculation of the amount of gross loss available to Munday irrespective of whether Lawrence Marshall should have been included in the MDA or not.
205. In the San Antonio case study offered by GM's expert as an experience comparable to the instant case, insell of 27.4% was reduced by 5.8% to 21.6% after an addition was made to the San Antonio MDA Chevrolet dealer network. (Ex. GM-98, p. 70)
206. Assuming the Houston MDA reacts to Munday's addition in essentially the same way as the San Antonio case study offered by GM's expert as an experience comparable to the instant case, the Board can expect Chevrolet dealers within the Houston MDA to reduce the insell number of 5796 units by 336 units. (Ex. GM-98, p. 70)
207. There is insufficient evidence in the record to support a finding that any one dealership would likely capture all units of insell available to dealers in an MDA.
208. Even if Munday captured all 336 units calculated as part of the hypothetical related to the San Antonio case study touted by GM's expert, this does not represent nearly the amount of sales Munday needs to meet, let alone exceed, its break even point.
209. The record in this case reflects a level of opportunity that is so low that Munday's options, upon entry into the Houston MDA market, are truly limited to cannibalization of its closest intrabrand competitors in order to merely survive.
210. Landmark works hard to bring consumers in the door and, once they get there, to put them in a Chevy product.
211. In 1991 and 1992, Landmark's gross profit per vehicle was lower than the average gross profit per vehicle of the average Houston Chevrolet dealer and lower than the average gross profit per vehicle of dealerships of any make in the nation. (Ex. C-51, Tab 13; Tr. at 1675)

245. The San Antonio MDA dealer network performance in response to the addition of the Gunn dealership in 1989 is a real life example of healthy marketplace competition enhanced through an addition to a dealer network where opportunity exists in the market to support such an addition.
246. There is insufficient evidence in the record to show that this case mirrors or in any way resembles the San Antonio case with respect to the amount of opportunity available in the market.
247. In this case, the record reflects that Munday and GM are asking the Board to find that Munday's establishment in the Houston MDA will enhance healthy competition absent a showing of quantifiable, reasonably achievable opportunity in the market in excess of the amount needed for Munday to exceed its break-even point without harming Landmark.
248. There is insufficient evidence in the record to show that Gunn was added to the San Antonio MDA absent quantifiable, reasonably achievable opportunity in the market in excess of the amount needed for Gunn to thrive without harming existing dealers.
249. Without evidence revealing that the Houston MDA and the San Antonio MDA were similarly situated with respect to opportunity, a comparison of them is virtually meaningless.
250. Additional adjustments can and will continue to be made by Landmark in many different areas of its operations in order to try to regain and/or maintain its profit margin in response to Munday's entry into the Houston MDA.
251. Landmark's gross profit per new vehicle sold in 1992 was \$1,386. In 1993, it increased to \$1,726. (Ex. C-52 and Ex. GM-139)
252. While Landmark's gross profit per new vehicle sold is indeed low compared to other dealers, it is not so low that it is incapable of being further lowered.
253. Landmark spends almost \$700 per unit sold on advertising. (Tr. at 1775)
254. Landmark's advertising expenses per new vehicle sold are not so high that they cannot be further increased.
255. Adjustments made to accommodate an addition in a market where achievable opportunity does not exist in substantial numbers is, in essence, the antithesis of healthy competition and will necessarily impact consumers negatively.
256. Although consumers who purchase vehicles from a dealer who has adjusted its gross profit per vehicle downward to accommodate an addition to its dealer

network will likely drive away feeling that they made a good deal, they will not remain satisfied for long if that dealer offsets its accumulating losses in gross profits per vehicle or its increased advertising costs per new vehicle sold by, for example, hiring less qualified service technicians at smaller salaries.

257. No matter how successful one high-volume dealer is at a single location, it is but one dealer. The obvious competitive advantages associated with multiple outlets or franchises are well documented both inside and outside the automobile industry.
258. While the Board has never provided that a brand is entitled to the same number of outlets as its marketplace competitors, being able to meet one's competitors head to head is understandably desirable as a means of ensuring that all share the market fairly while, at the same time, providing numerous alternatives to the public.
259. Out of all the areas within the Houston MDA, the growth patterns for north Houston and in the Spring AGSSA do appear to make it an attractive location for Ford and Chevrolet to be equally matched.
260. Because Munday and GM have failed to identify a quantifiable amount of reasonably achievable opportunity in the Houston MDA, it is impossible to know whether the issues unique to north Houston indicate a real need for an addition to the market as a whole or simply confirm that the existing dealer body is no longer well-placed.
261. A dealer for dealer comparison to Ford is only relevant insofar as the record reflects adequate opportunity to support Chevrolet's desire to increase its Houston MDA network irrespective of the number of outlets held by its closest brand competitor.
262. Given that Munday and GM have failed to prove that shortfall and/or the requisite level of achievable opportunity exists in the Houston MDA, there is insufficient reason to find that Munday's addition will do anything more than force a redistribution of the same number of registrations among a now larger dealer body.
263. The issues surrounding healthy competition in the marketplace do not weigh in favor of Munday and GM.

5. The Public Interest

264. For customers in the Spring AGSSA, the establishment of the Munday Chevrolet dealership shortens the average distance to a Chevrolet dealership from 7.81 miles to 4.26 miles. (Ex. GM-98 p. 59)

- In new vehicle inventory, 100 used vehicles, \$60,000 in parts inventory, and employ 79 people. (Ex. MCG-7)
36. The real estate upon which the Munday dealership was to be placed cost over \$2 million and the building was estimated to cost another \$2.5 million. (Tr. at 28)
 37. Munday's break-even point for new motor vehicle sales was calculated to be from 1200 to 1500 units per year and its planning potential was determined by GM to be 2296 units. (Ex. C-51, Tr. at 114, 1616, Robenalt Depo. at 121)
 38. The FM 1960 property purchased by Mr. Munday was originally acquired by GM as a part of its land-bank program. (Robenalt Depo. at 46-47)
 39. The function of GM's land-bank program was to purchase real estate in areas where GM thought it might want representation in the future while land was available and priced reasonably. (Tr. at 855 and Roggenkamp Depo. at 16)
 40. Chevrolet conducted a study of the Houston market in 1987 and determined that a dealership would be desirable at some point in the future in the FM 1960/Interstate 45 area. (Wong Depo. at 20-21; Dujmovich Depo. at 40-41; Glenn Depo. at 56)
 41. Despite GM's preference for locating dealerships in metropolitan areas on freeways, as opposed to secondary roads, because of the favorable traffic counts and visibility, the property ultimately acquired by Mr. Munday from GM was approximately half a mile from the Interstate on FM 1960. (Feeley Depo. 24; Glenn Depo. at 30-31, 56; Wong Depo. at 14; Kibler Depo. at 41; Heckert Depo. at 38-39; Roggenkamp Depo. at 87-88)
 42. Another study of the Houston market, performed by Chevrolet in 1989-1990, concluded that the then existing dealer network was adequately serving the Spring AGSSA and that Landmark was the dominant dealer in this AGSSA, with 16.59% of its total retail passenger car registrations and 11.93% of its total truck registrations within this AGSSA in 1989. (Dujmovich Depo. at 7)
 43. The 1989-1990 Chevrolet Houston market study also showed a decline in retail industry registrations between 1985 and 1989 of 16,000 units and recommended the addition of Chevrolet dealerships in the areas of Spring, to the north of the Landmark dealership, and Jersey Village, an area to the west of the Landmark dealership. (Dujmovich Depo. at 37, 76)
 44. In 1991, Chevrolet attempted to establish dealerships in the Spring and Jersey Village AGSSAs. (Tr. at 1103-1105)

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APPENDIX

TAB 2

Excerpts from *Lee Trevino Ford PFD*

However, a critical question exists in this case of whether the market is adequate to support another dealership, particularly in the general Arlington and south Arlington areas. The question of whether there is sufficient market is of critical importance because if the market is not sufficient to enable the dealers to operate profitably, the result of such a circumstance will be detrimental to the public interest, as there can be little doubt but that dealers who are not able to operate profitably are also not able to properly take care of the needs of their customers and the public. As in any case of this nature, it is really not possible to predict with absolute certainty just what level of sales or registrations can reasonably be expected to be sold by the dealers in the market.

What is known, however, is that consistent with nationwide trends, total new car industry registrations and Ford car registrations have declined significantly in the past five years in the Fort Worth Multiple Point, and this fact is of particular significance in light of all of the evidence relating to the population and economic growth in the market area; that is, in spite of population growth, total car registrations, as well as Ford and Chevrolet registrations, have declined.

As Dr. Westbrook pointed out, he saw little point in trying to relate population growth to what has happened in the auto industry in the last four or five years. "Clearly it has been an unusual period in which not only has there been a national recession, but also a drastic cut in the auto industry." (1:219). With respect to the south Arlington PMA, in terms of car

number of additional registrations, it would appear that the risk in this case is greater than what can be considered to be an acceptable risk; that risk being a market not sufficient to support the existing and additional dealers on a profitable basis with the resultant detrimental effects upon the service provided to the public. Under the existing circumstances, it is not reasonable to conclude that the granting of the application will not be harmful to Arendale Ford and therefore the approval of the application would not be in the public interest.

Concerning the matter of the financial strength and profitability of the existing dealers, it appears that all of the multiple point Ford dealers except Arendale, have been consistently profitable. However, the mere fact that the existing dealers have reported profits of certain amounts during the past several years does not establish just how strong or profitable the dealers may be. No analysis of return on sales or return on investment is contained in the record and it is not possible from the evidence in the record to assess the financial strength of the existing dealers.

Moreover, as the evidence on vehicle registrations and penetration show, the motor vehicle industry is extremely volatile as the decline in the number of Ford dealers in 1982 indicates. With respect to Arendale Ford, the evidence shows that this dealership has not been profitable in three of the four past years (App. Ex. 2), and the dealership does not have a strong capital structure (3:82). While it is true that Arendale Ford's existing financial circumstances may be attributable to

APPENDIX

TAB 3

Weslaco Motors Decision

**TEXAS DEPARTMENT OF MOTOR VEHICLES
MOTOR VEHICLE DIVISION**

**WESLACO MOTORS, LP,
Applicant**

v.

**BERT OGDEN CHEVROLET, INC.
d/b/a BERT OGDEN CADILLAC,
Protestant**

§
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§

**SOAH DOCKET NO. 601-08-2071.LIC
MVD DOCKET NO. 08-0011-LIC**

FINAL ORDER DISMISSING PROTEST

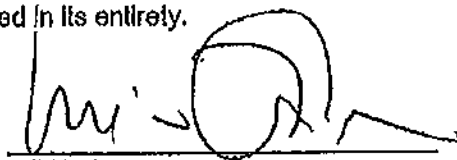
The above referenced matter came before the Director of the Motor Vehicle Division in the form of a Proposal for Decision from the State Office of Administrative Hearings. The Director, having considered the evidence, arguments, findings of fact and conclusions of law presented in the Proposal for Decision, the Protestant's exceptions, and the Applicant's replies, enters this Final Order:

IT IS ORDERED:

1. That the Findings of Fact and Conclusions of Law as set out in the Proposal for Decision, including the September 16, 2009 amendments made by the State Office of Administrative Hearings, are hereby adopted;
2. That the protest of Bert Ogden Chevrolet, Inc. d/b/a Bert Ogden Cadillac is hereby dismissed in its entirety; and
3. That the Motor Vehicle Division shall continue administrative processing of the application which is the subject matter of this docket.

All other relief not expressly granted is hereby denied in its entirety.

Date: 02/04/2012



**Bill Harbeson
Interim Division Director
Motor Vehicle Division
Texas Department of Motor Vehicles**

SOAH DOCKET NO. 601-08-2071.LIC

WESLACO MOTORS, L.P.,	§	BEFORE THE STATE OFFICE
Applicant	§	
	§	
v.	§	OF
	§	
BERT OGDEN CHEVROLET, INC.	§	
Protestant	§	ADMINISTRATIVE HEARINGS

PROPOSAL FOR DECISION

Weslaco Motors, L.P., (Applicant or Weslaco Motors) seeks approval of its application filed with the Motor Vehicle Division (MVD) of the Texas Department of Transportation (TxDot) to amend its dealership license to add the Cadillac passenger auto and light truck lines by General Motors to its current dealership located in Weslaco, Hidalgo County, Texas. Bert Ogden Chevrolet, Inc. d/b/a Bert Ogden Cadillac (Protestant or Bert Ogden Cadillac), an existing Cadillac dealer in Hidalgo County, protested the application. Having considered the evidence submitted in this matter and arguments of the parties, the Administrative Law Judge (ALJ) finds that Weslaco Motors established good cause for approving its application. Consequently, the ALJ recommends approval of the application by the MVD.

I. JURISDICTION, NOTICE, AND PROCEDURAL HISTORY

The MVD of TxDot has jurisdiction over this matter, pursuant to TEX. OCC. CODE (CODE) §§ 2301.652; 2301.701-713; and 43 TEX. ADMIN. CODE (TAC) §§ 8.105-8.107. The State Office of Administrative Hearings has jurisdiction over all matters related to convening the contested case hearing, including the authority to issue a proposal for decision containing findings of fact and conclusions of law, pursuant to Code § 2301.704.

The issue of notice was not disputed by the parties; consequently, that issue will be set out in the findings of fact and conclusions of law without further discussion here.

The hearing convened on December 2, 2008, before ALJ Suzanne Formby Marshall in the William P. Clements Building, 300 West 15th Street, Fourth Floor, Austin, Texas. William David Coffey, III, of David Coffey, III, & Associates in Austin, Texas, appeared and represented Weslaco Motors. Dudley McCalla, attorney, appeared and represented Bert Ogden. The hearing concluded on December 4, 2008, and the record was held open in order to receive a transcript of the hearing and written closing arguments by the parties.¹ The record closed on February 24, 2009.

II. DISCUSSION

A. Background

Weslaco Motors seeks approval to amend its franchise license in order to establish and operate a Cadillac dealership to be located at 2401 E. Expressway 83, in Weslaco, Texas.² Bert Ogden operates a Cadillac dealership located at 1400 E. Expressway 83, in Weslaco, and it filed a protest to Weslaco Motors' application.³ Weslaco Motors is located approximately twenty miles from Bert Ogden Cadillac.⁴ General Motors (GM) did not appear, intervene, or otherwise participate in this case.⁵

Weslaco Motors has entered into an agreement with Cardenas Autoplex (Cardenas),⁶ a Cadillac dealership in Harlingen, Texas, to buy the assets of the Cardenas Cadillac franchise, which

¹ During this period of time, it was also necessary to clarify which portions of the record were subject to confidentiality protection due to the disclosures made during the hearing of Mr. Payne's financial worth and to receive supplemental pages to exhibits that were admitted into evidence at the hearing, under the optional completeness doctrine.

² Currently, Weslaco Motors also operates a GM dealership (comprised of Pontiac, Buick, Chevrolet, and GMC) at this location. Applicant's Ex. A-3. (Reference to Applicant's Exhibits will be A-1, 2, etc., indicating exhibits that are tabbed and numbered, with a notebook (Exhibit A). For example, Ex. A-3 refers to TAB 3 in Applicants exhibit notebook.)

³ The protest was filed on February 28, 2008.

⁴ Mr. Ogden has standing to bring this protest because the proposed Weslaco Motors Cadillac dealership will be located within the same county as his dealership. Code § 2301.652(b)(1).

⁵ GM's participation would have assisted the ALJ by providing evidence related to its rationale for approving the Weslaco Motors application, market representation, areas of primary responsibility (APRs), and acceptable levels of competition.

⁶ Cardenas Autoplex also operates a Mercedes-Benz dealership at the same location.

will be used in operating the proposed Weslaco Motors Cadillac dealership.⁷ GM has given approval to the transaction as well as the relocation.⁸ The TxDot MVD has approved the transaction, subject to the protest.

B. Applicable Law

As the applicant, Weslaco has the burden of proving "good cause" for establishing and operating the proposed dealership. Code § 2301.652(a). The following factors are to be considered by the MVD in assessing whether good cause has been shown:

- (1) whether the manufacturer or distributor of the same line-make of new motor vehicle is being adequately represented as to sales and service;
- (2) whether the protesting franchised dealer representing the same line-make of new motor vehicle is in substantial compliance with the dealer's franchise, to the extent that the franchise is not in conflict with this chapter;
- (3) the desirability of a competitive marketplace;
- (4) any harm to the protesting franchised dealer; and
- (5) the public interest.⁹

⁷ Applicant's Ex. A-1. Throughout the hearing, Weslaco Motors referred to this scenario as a "relocation" of Cardenas Autoplex to Weslaco. There are currently three Cadillac dealers in the Lower Rio Grande Valley area: Bert Ogden (in Mission), Luke Fruia (in Brownsville), and Cardenas Autoplex (in Harlingen). If Weslaco Motors' application is approved, there will continue to be three Cadillac dealers in the region - giving rise to the Applicant's assertion that a "relocation" will occur if its application is approved. However, use of the term "relocation" is somewhat inaccurate to the extent that Weslaco Motors currently does not have a Cadillac dealership to relocate. However, this is a relocation in the sense that the Cadillac APR associated with Cardenas Autoplex also currently encompasses the proposed Weslaco Motors location. See Applicant's Ex. A-11 (Dr. Ernest Manuel's report) at Tab 2, p. WM-00-1157.

⁸ Applicant's Ex. A-2. If the application is approved, GM will issue a new franchise to Weslaco Motors. There is a pending case in which GM seeks to terminate the franchise of Cardenas Autoplex. Cardenas Autoplex has filed a protest. That matter has been abated, pending the outcome of this case.

⁹ Code § 2301.652(a).

C. Evidence

I. Applicant's Evidence

Applicant presented the testimony of Mr. Edwin "Bud" Payne, the dealer/principal of Weslaco Motors, Bob Grooms, chief financial officer of Weslaco Motors, the expert testimony of Dr. Ernest H. Manuel, and numerous exhibits.

a. Testimony of Edwin Payne

Mr. Payne was born in Weslaco and has lived there all his life. He owns a Dodge-Chrysler-Jeep franchise, a Ford-Mercury franchise, and a Chevrolet-Buick-Pontiac-GMC franchise, all located in Weslaco. He also has a Mitsubishi-Jeep dealership in Harlingen, and a Volkswagen-Suzuki dealership in Brownsville that, until 2008, also included Lincoln-Mercury.¹⁰ He and his wife split the ownership of Weslaco Motors on a 50-50 basis. Neither have been convicted of a felony.¹¹ As a dealer, Mr. Payne is required by GM to stay in compliance with all GM franchise agreements. He testified that he is in compliance with them. Mr. Payne described the qualities he believes make a good auto dealer: having an innate love of the business, having a servant's heart, being actively engaged in, and giving back to, the community,¹² and training.

Mr. Payne said that he seeks to amend his license so that he can add the Cadillac franchise to

¹⁰ The Lincoln-Mercury store was sold by Mr. Payne as part of a transaction involving the closing of a Ford dealership in Mercedes, Texas. Ford assigned its right of first refusal (to own the franchise in Mercedes) to Mr. Payne and Bob Bogus, another motor vehicle dealer in the Valley, who both owned Ford dealerships. Mr. Vackar, the owner/principal of Bert Ogden, also wanted to purchase the Mercedes franchise but, essentially, he was cut out of the deal through the actions of Ford, Mr. Payne, and Mr. Bogus. It appears that this transaction has created tension between Mr. Payne and Mr. Vackar. Mr. Payne sold his Lincoln-Mercury franchise to Mr. Bogus who moved it to his existing Lincoln-Mercury dealership in Harlingen. Tr. 36.

¹¹ Tr. 55.

¹² Mr. Payne described his involvement in the community. He is a member of a number of organizations and has served on their boards: The Valley Chamber of Commerce, the Land Fund (a non-profit that works to preserve the South Texas native habitat), the Nature Center (preservation organization for the Mid-Valley area), Knapp Hospital, Weslaco Chamber of Commerce, Economic Development Board, Rio Grande Valley Economic Development Council, Humane Society of Hidalgo County, the Texas Automobile Dealers Association, and the Valley Auto Dealers Association. Additionally, the dealership contributes to the Little League system and a scholarship program.

his existing Chevrolet-Buick-Pontiac-GMC store.¹³ The addition of another product line will allow him to use some currently unused space in the facility and will provide an opportunity for him to expand and maximize his existing resources related to the sales of used vehicles and the service department.¹⁴ He has sold Cadillacs in the past and testifies that he is generally familiar with the product.¹⁵

Demographics of the Valley

As a lifetime resident of the Lower Rio Grande Valley (Valley or LRGV), Mr. Payne testified about its characteristics and demographics. He said the Valley has a population comprised of approximately 85-87% Hispanic residents. Noting that the Valley has low overall household income figures, he testified it is common for many families to combine their resources in order to contribute to the economic family.¹⁶ But, he added, there are also quite a few wealthy people in the Valley, especially in the Mission/McAllen area.

According to Mr. Payne, employment rates in the Valley have increased in recent years, and the overall unemployment rate has decreased to just a point above the national average during the last three to four years. He noted that the area has one of the fastest growing populations in the United States, particularly among the 18 to 29-year-old age range.

Mr. Payne provided testimony about the sizes of towns in the Lower Rio Grande Valley. He said that the population of McAllen is 80-90,000; the population of Weslaco is 40,000; the population of Harlingen is 60,000; the population of Brownsville is over 200,000, and the population of Mission is around 65,000. The communities of Harlingen, Brownsville, San Benito, La Feria, Olmito, and South Padre Island are located in Cameron County, which has an overall county population of approximately 400,000. The communities of Mission, McAllen, Weslaco, and

¹³ Tr. 38.

¹⁴ Tr. 77-78; Applicant's Ex. A-5. There is about 6,000 square feet of unused space. Tr. 127.

¹⁵ Mr. Payne said that he had sold program Cadillacs and used Cadillacs in the past.

¹⁶ Tr. 56.

Mercedes are located in Mission County. The population of Mission County is about 800,000. If Mr. Payne's application is approved, the Cadillac dealership will be moved from Harlingen in Cameron County to Weslaco, in Hidalgo County.¹⁷ The population count in Hidalgo County is two to one that of Cameron County.

Additionally, he noted the proximity of several cities in nearby Mexico, including Matamoros, with a million-plus people, and Reynosa, with about 750,000 people, to the Valley. In addition, there are approximately 500,000 people living between those two communities. Also, in close proximity is Monterrey, which Mr. Payne said was an hour and a half away from the Valley and was made up of around four million people. He testified that the Valley was the closest place for people in those cities to shop for many types of retail sales, including luxury vehicles.

Mr. Payne testified that automobiles in the United States can be legally sold to Mexican citizens if the purchaser has a U.S. address. He identified several bridges between the United States and Mexico: a bridge in the Mid-Valley area five miles south of Weslaco leading to Nuevo Progreso, Mexico; three bridges and a free-trade bridge used mainly for truck traffic in Brownsville; a bridge that will soon be built south of Donna; and a bridge in Reynosa. These bridges provide access to the Valley for Mexican citizens. Mr. Payne testified that sales to Mexican citizens are an important part of the revenue stream of his GM dealerships.

In Harlingen, eleven Cadillacs were sold in the area of primary responsibility (APR) for that dealership in 2007.¹⁸ The majority were "pump-ins"¹⁹ by Luke Fruia. Mr. Payne said that most of the business available to a car dealer in the Valley comes from Valley residents who tend to purchase

¹⁷ Tr. 63-65.

¹⁸ An APR is the area a manufacturer allots for a franchise. There is only one dealer of the same make in each APR; however, a dealer is not restricted to making sales only within his APR.

¹⁹ A "pump-in" occurs when a vehicle is sold into the APR of another dealer as demonstrated by its registration in that APR. Tr. 121.

vehicles from dealerships located closest to them. As an example, he said that 90% of the business for his Chevrolet dealership in Weslaco comes from within 25 miles of his dealership, while only about 2% of his GM sales come from outside the Valley.²⁰

Distances between Valley communities

Mr. Payne discussed the distances between various towns in the Valley, including the three that currently have Cadillac dealerships. He testified that the Bert Ogden Cadillac dealership, located in Mission, is approximately 22 miles from Weslaco.²¹ There are approximately five miles between Weslaco and Mercedes. According to Mr. Payne, it is about 11 miles from Mercedes to Harlingen, and 20 miles from Harlingen to Brownsville. McAllen is about 19 miles from Weslaco. Mr. Payne said that Weslaco is viewed as the center of the Valley, although the McAllen/Mission/Edinburg area is the economic driver and population center.

Agreement to buy Cardenas Cadillac franchise in Harlingen

In order to purchase the Cadillac assets of Cardenas Autoplex, Mr. Payne has entered into an Asset Purchase agreement (a buy-sell agreement) with Cardenas.²² He testified that his dealership was looking for ways to strengthen its Weslaco operations, and a former GM sales representative suggested buying the Cadillac dealership in Harlingen and moving it to Weslaco, while keeping it within its APR.

Mr. Payne discussed the rationale behind APRs, *i.e.*, to allow dealers some exclusivity so that they will have a sufficient market to support their operations, due to the high cost in purchasing, building, and running a dealership. As testified to by Mr. Payne, GM allows a dealer to move his

²⁰ Tr. 123-124.

²¹ Tr. 39-40.

²² An Asset Purchase agreement (a buy-sell agreement) and an Advance Agreement constitute the documents that memorialize that transaction. Tr. 66; Applicant's Ex. A-1. Cardenas Autoplex cannot literally sell the franchise; only GM can approve a franchise.

dealership within his own APR, subject to its approval. As part of a relocation process, a dealer submits guidelines (describing areas and space devoted to parts, service, sales, capital requirements,²³ image, tools, facility size, training, and personnel²⁴) for GM's approval.

In this case, Mr. Payne described the Asset Purchase agreement as giving him the right to do business in the Cardenas APR, as well as ownership of the customer list, parts, service equipment, manuals, and signage. The purchase price was \$1.5 million.²⁵ However, he has not yet taken title to any of the assets due to the pending protest by Bert Ogden, even though GM and the MVD have approved the sale.²⁶ At the present time, Cardenas is still operating the Cadillac franchise in Harlingen, although Mr. Payne stated that he did not believe it was aggressively doing so.

According to Mr. Payne, an auto manufacturer has a "right of first refusal" in a situation in which a dealer enters into a buy-sell agreement with another party. This right allows the manufacturer to buy the franchise itself and then get rid of it, buy it, and give it to somebody else, or to buy it and close the dealership. GM has not exercised its right of first refusal in the Weslaco-Cardenas buy-sell scenario.

Noting that the Cardenas operation has been a disappointment to GM to the extent that GM has sent a notice of termination of the franchise, Mr. Payne said the relocation will help the Cadillac brand because it will have increased sales, better awareness of the product, stronger marketing, more accessibility to customers, and good service if relocated to Weslaco. He also testified that Cardenas has not dedicated himself to taking care of the Cadillac customer.²⁷

²³ To insure there is enough working capital in the company to promote, sell, and service the product. Tr. 70.

²⁴ Mr. Payne testified that a Cadillac dealer was required to have factory-trained and certified Cadillac technicians. Further, he stated that it is prudent to also have certified salespeople. Tr. 71. The dealer pays for the costs associated with travel and lodging for training; the factory provides the training.

²⁵ Mr. Payne described the Advance Agreement that provides for payment of the \$1.5 million up front, to be returned if the relocation is not approved. Mr. Payne conceded that the payment arrangement was unconventional, but that, at the time, Mr. Cardenas "had some issues" and the purchase was negotiated that way. Tr. 74-75.

²⁶ Tr. 72-73.

²⁷ Tr. 111-112.

Opportunity for better service to Cadillac customers

Mr. Payne testified that with the addition of Cadillac, his GM dealership could be much stronger in the parts and service departments, resulting in better service to his customers due to GM's requirement to have trained and certified repair technicians.

Mr. Payne also discussed the two types of repair service: warranty service and retail (or customer-paid) service. He said that only a certified GM dealer can perform warranty work, absent a unique situation. In order to service their Cadillac, a consumer has to go to either the Cardenas dealership in Harlingen (20 miles from Weslaco; 40 miles from Mission), the Bert Ogden dealership in Mission (22-23 miles from Weslaco; 40 miles from Harlingen) or the Luke Fruia dealership in Brownsville (40 miles from Weslaco; 60 miles from Mission). Mr. Payne testified that he has seen studies indicating a buyer of a new vehicle is located within 13 miles of the nearest dealership carrying that product. For used cars, most buyers are located within seven miles of the dealership from which the vehicle is purchased. For service, he believes that people want to be closer than 13 miles.²⁸

Mr. Payne testified about the types of reports used by General Motors to determine the performance of the dealerships. One report is a customer satisfaction index (CSI); another is the standards for excellence program (SFE). Mr. Payne testified that his dealership generally ranks well on these. The SFE is an exclusive GM program that measures sales performance and customer satisfaction, including purchase delivery satisfaction (for new vehicle deliveries) against the ratings of other dealers. There is a financial reward depending on the performance of the dealer.²⁹

²⁸ Tr. 103-104.

²⁹ Tr. 52-54.

Location advantages for Weslaco Cadillac dealership

Mr. Payne testified that the Weslaco facility is located on Expressway 83 upon which approximately 70,000 cars travel each day.³⁰ He said that this volume is around 50 times greater than the number of vehicles that travel on the roadway to get to the Cardenas dealership. He said that factors such as visible location, accessibility, and a high traffic count are important to the financial success of a dealership.³¹

Mr. Payne described the process for starting up a new product line. If his application is approved, he will order new Cadillac product from the Cadillac Division and will receive a monthly allocation that can be chosen based on availability and the dealer's production. According to Mr. Payne, a dealer pays for the vehicles "up front" through financing with GMAC; the dealer then pays GMAC.³² For used cars, a dealer obtains them through trades, purchases on the wholesale market (through auctions and wholesalers), purchases from individuals, and consignments.³³

"Dualing" means to add a franchise to an existing parts and service department or, put another way, to add another line, product, or make to a dealership.³⁴ "Dualing" Cadillac with the other GM brands at his dealership in Weslaco will allow Mr. Payne to share personnel, training, expenses, parts, and service similar to the operations at Bert Ogden's dealership in Mission, creating a "synergy" between the product lines. He said that he has sold program Cadillacs and used Cadillacs and is familiar with the product.

At his current location, Mr. Payne plans to use an existing empty building to house the Cadillac showroom. GM has approved the facility plans, including the sales and service center. The

³⁰ Tr. 79; Applicant's Ex. A-6.

³¹ Tr. 80.

³² This method of payment is called "floorplaning" or "whole floorplan financing." Tr. 86.

³³ Tr. 86. There are also certified used cars bought through GMAC or GM, depending on the owner. Tr. 87.

³⁴ Tr. 181.

dealership will follow GM's rules for selling and servicing product in Weslaco, including making required changes to the facility related to the appearance or image.

Mr. Payne testified that he cannot operate the Cadillac line in Harlingen because he does not own a facility there and it would cost between \$2.5 to \$4 million to build one. Further, he said that he does not believe that a stand-alone Cadillac dealership anywhere in the Valley (except possibly the Mission/McAllen area) could return a profit because there would not be enough sales volume or parts and service business.³⁵

He does not believe that moving Cadillac out of the Harlingen area will inconvenience Cadillac customers because west Harlingen is as close to Weslaco as it is to Cardenas (who is on the east side), and there have been so few Cadillac sales from that dealership.³⁶

National economic situation's effect on auto industry

Mr. Payne testified that, in general, manufacturers are downsizing the number of dealers to obtain efficiencies in marketing and distribution processes. This is so because of the declining domestic market share. Other manufacturer considerations may be under-performing dealers, bad locations, or bad facilities. The downsizing process affects markets in which there are too many or under-performing dealers.

With respect to the current economy, Mr. Payne testified that, in his opinion, the auto business is cyclical. He has seen downturns and upturns and he has observed that the people who position themselves for the long term seem to come out ahead. He believes that if GM goes into a bankruptcy, it will be a planned one to alleviate a lot of their financial problems. He plans to position himself with the Cadillac franchise for the long term and believes that the business will be profitable.

³⁵ Tr. 95-96.

³⁶ Tr. 116-117.

Mr. Payne believes that some of the money given by the federal government to the auto industry will be used to help the current strained availability of credit resources. He noted that GMAC has cut back on financing for customers with beacon credit scores under 700; however, he believes that a lot of Cadillac consumers have credit scores exceeding 700. He testified that he was not required to use GMAC financing solely, although there is an incentive to do so. Mr. Payne described a qualified buyer for Cadillac as someone, in general, with a \$50,000-plus income level, with good credit.

Mr. Payne testified that his dealership did well in 2006 and 2007. His sales of new vehicles increased in 2006 over those in 2005, but were about the same in 2006 and 2007.³⁷ In 2008, he said the increased pressure resulting from emphasis of the "green movement" for more environment-friendly vehicles and the increased price of gas greatly affected sales. As he described it, truck sales (which has comprised the bulk of his sales) came to a roaring halt.³⁸ Mr. Payne testified that a dealer cannot adjust operations rapidly when dealing with inventories in order to respond to changing economic times. However, he stated that he wishes to position himself for the long term and needs to acquire the Cadillac franchise and product now because of the difficulty in doing so on an accelerated basis when the economy improves.³⁹

In 2008, the Westaco dealership experienced a decrease in profitability, and sold about an equal number of trucks and cars. For the period January to September 2008, the dealer showed a loss of \$382,451.⁴⁰ The number of new cars sold during that time was 119. New truck sales totaled 382.⁴¹

³⁷ Tr. 177-178.

³⁸ Tr. 179-180.

³⁹ Tr. 180-181.

⁴⁰ Tr. 152-153; Protestant's Ex. P-9.

⁴¹ Tr. 154-155; Protestant's Ex. P-9.

Mr. Payne believes that adding Cadillac will not take away from his truck sales because Cadillac is a luxury product, and there is a market for Cadillacs in the Mid-Valley area. He testified that Cadillac does not compete with a lot of other products in the Valley - it sells 4 to 1 over Lincoln.⁴²

In 2008, Weslaco Motors reported a profit through September of \$103,272.⁴³ In 2006, the dealership made a profit of \$631,984.⁴⁴

Advertising

Mr. Payne testified that GM establishes marketing associations in which dealers within a defined area develop a marketing plan for the product within that area. He said that advertising can increase sales in a good market, but may not work in a bad market. However, he noted that advertising can raise the perception of the brand in the community. Also, the point of advertising is not only to increase sales, but also to increase the image of the dealership and achieve top-of-the-mind awareness by the consumer of the product. Advertising can also lead to "bleedover" sales for another dealer.⁴⁵ Mr. Payne believes that having two dealers in Mission and Weslaco will result in more awareness of the Cadillac product.

With respect to the Bert Ogden dealership, Mr. Payne described Bob Vackar, the principal/owner of Bert Ogden, as a very good dealer with aggressive marketing. He believes it is a strong and well-capitalized competitor. According to Mr. Payne, the Bert Ogden dealership spends more on advertising and is twice as big as any other auto group. He described Bert Ogden as being the largest dealer group in the Valley in terms of new units sold, with either the Payne or Bogus dealerships being the next largest.

⁴² Tr. 192-193.

⁴³ Tr. 197; Applicant's Ex. A-4.

⁴⁴ Tr. 200.

⁴⁵ Tr. 101.

Mr. Payne believes that he will sell a lot of used cars as a periphery to the Cadillac franchise. He believes he can compete successfully with Bert Ogden and that there is enough business to support three Cadillac dealers (after the relocation from Harlingen to Weslaco) because all the dealers carry products in addition to Cadillac, yielding economies of scale in the costs of operations.⁴⁶

b. Testimony of Bob Grooms

Mr. Grooms is the chief financial officer for Weslaco.⁴⁷ He testified that the application to the TxDot MVD was a request to amend its current dealership license to add the Cadillac line to its other GM lines.⁴⁸

Mr. Grooms was responsible for preparing the application to GM for a Cadillac franchise. Originally, Weslaco Motors proposed operating the Cadillac franchise as a stand-alone franchise, but GM indicated that it should be made part of the overall group of franchises operated at that location.⁴⁹ According to Mr. Grooms, Weslaco Motors was required to resubmit part of its application to GM with that modification, among others, through the internet.⁵⁰

GM also requested a revision of the number of new retail units projected to be sold by Weslaco Motors. Mr. Grooms testified that the first pro forma (a forecast of sales) submitted with the original application to GM projected sales of 480 new units per year. This number was changed

⁴⁶ Tr. 115-116.

⁴⁷ He has also been a motor vehicle dealer for Ford, Nissan, and Subaru in Denver, Colorado, and for Chevrolet-Hyundai in Beaumont, Texas. Tr. 211.

⁴⁸ Tr. 246-247.

⁴⁹ Tr. 226.

⁵⁰ The application admitted into evidence does not include the re-submitted changes. Applicant's Ex. A-2; Tr. 225.

when he and Mr. Payne were advised that the GM planning volume (number of units GM expected to be sold) was 220 new units per year.⁵¹ Because Weslaco Motors was exceeding its planning volume for sales of the other lines, Mr. Grooms stated that they decided to revise the number to 300, instead of 220.⁵²

The pro forma also includes a gross profit projection of \$3,000 per unit for new cars,⁵³ and a gross profit per unit for used cars of \$949.⁵⁴ According to Mr. Grooms, the dealership will be profitable if it sells more than 90 units a year, although profits become marginal at the 90 unit-per-year level.⁵⁵ While Mr. Grooms acknowledged the recent change in the economic climate, he testified that a projection of 220 units is still a reasonable forecast for sales.⁵⁶ He testified that the dealership spends more than half a million dollars to advertise its GM products each year.

Mr. Grooms stated that Weslaco has completed all the conditions that GM required in order to approve the application, with the exception of some facility imaging.⁵⁷ He also discussed some of the other GM requirements that Weslaco Motors had complied with, such as maintaining a line of credit, requiring the dealer operator to own at least 15% of the business and maintaining sufficient net working capital (the operating capital available to operate the dealership, including parts inventories, used car inventories, and prepared assets that are current). Mr. Grooms said that GM required the dealer to have \$2.4 million in operating capital with a line of credit of \$1.5 million, and that GMAC issued a line of credit for that amount.

⁵¹ Tr. 216. Another change that has occurred since the application was submitted was a change in the number of employees. He testified that Weslaco Motors no longer employs 300 people in the Valley. Tr. 231.

⁵² Tr. 234-236. Although 120% of 220 units would result in 265 units, Mr. Grooms testified that the number was rounded-up to 300 based on discussions with the sales managers and Mr. Payne. Tr. 236.; Applicant's Ex. A-2; p. WM-00312.

⁵³ Tr. 240.

⁵⁴ The pro forma included a projection of 381 used cars to be sold from all the line makes, including Cadillac, Buick, Pontiac, and GMC. Tr. 242; Applicant's Ex. A-2, p. WM-00312.

⁵⁵ Tr. 245.

⁵⁶ Tr. 239.

⁵⁷ Tr. 213.

Mr. Grooms reviewed the financial statements provided by Bert Ogden Cadillac. He noted that the dealership did not report its profits derived from used car sales for 2006, 2007, or 2008.⁵⁸ According to Mr. Grooms, the failure to report the vehicle sales distorts the profitability as reported by the dealership.⁵⁹ He also discussed other discrepancies in the financial statements. For example, he questioned the report of a negative parts inventory. Noting that a service department must be able to service vehicles, Mr. Grooms said that the dealer would have to maintain a parts inventory from which to draw necessary parts for the repairs. He added that a negative parts inventory, such as that reported by Bert Ogden, essentially means that it did not have any parts.

He also observed that the reported net profit of \$1.1 million for 2006 cannot be verified because the supporting information for the dealer's financial statements was not provided. In 2006, it appeared that Bert Ogden sold 522 new Cadillac vehicles, with an overall gross profit per vehicle (including cars and trucks) of \$2,402 (compared to Weslaco's projected overall gross profit per vehicle of \$3,000).⁶⁰ He could not account for the difference because he did not know what Bert Ogden included in the cost of sales.

c. Dr. Ernest Manuel report and testimony

Dr. Ernest Manuel is president of The Fontana Group which provides economic consulting services and expert testimony regarding the retail motor vehicle industry, among other industries. Protestant did not object to Dr. Manuel's qualifications to provide expert testimony in this case.⁶¹ Dr. Manuel concludes that the Protestant has standing to bring his protest because: (1) both dealerships will be located in the same county, Hidalgo; (2) the relocation is greater than one mile; and (3) the proposed location will be closer to Protestant than before the relocation.

⁵⁸ Tr. 254-255.

⁵⁹ Tr. 254-255.

⁶⁰ Tr. 265-266.

⁶¹ Dr. Manuel's qualifications can be found in Applicant's Ex. A-11. Dr. Manuel prepared an initial report, Applicant's Ex. A-11, and a rebuttal report, Applicant's Ex. A-30. Additionally, he prepared supplemental exhibits A-105 through A-108.

Location of Proposed Dealership

Dr. Manuel performed an optimal location analysis and determined that the "optimal location"⁶² for the Cardenas Cadillac franchise is far to the west of its current Harlingen location and even farther west than the proposed Weslaco location.⁶³ However, he concluded that the proposed location in Weslaco would better serve the consumers in the market and offer more convenience for current and prospective Cadillac customers than one in the Harlingen area. Additionally, he notes that there are substantially higher traffic counts at the Weslaco dealership than at Cardenas providing increased sales opportunities.

According to Dr. Manuel, the proposed relocation of the Harlingen franchise to Weslaco would result in it being located 20 miles away from the Protestant's Cadillac dealership and more than 25 minutes away in actual drive time. When considering the distance between the Weslaco location and the Bert Ogden Cadillac location in terms of "air miles," the proposed Weslaco location is approximately 21 miles air distance from Bert Ogden and 26 minutes away in drive time.⁶⁴ This is comparable, Dr. Manuel found, to the distance between the current Cardenas location and the Luke Fruia location in Brownsville which are presently 20 miles apart and approximately 28 minutes away in drive time.

Dr. Manuel observed that relocating the Cadillac franchise from Harlingen to Weslaco will likely result in GM abolishing the Harlingen APR and creating a Weslaco APR for the Applicant. The new APR will be comprised of census tracts taken from both the current Harlingen APR and the McAllen APR. The remaining Harlingen APR census tracts would be reassigned to the Brownsville APR. Because GM has not yet defined the new APRs, Dr. Manuel attempted to approximate the

⁶² An "optimal location" analysis determines the location for a relocated dealership that provides the greatest efficiency in the average travel time for a prospective and current Cadillac customer to get to one of the three dealerships. Applicant Ex. A-11, p. WM-00-1113; Tr. 318.

⁶³ A consequence of this would be much less impact on the Bert Ogden dealership. Tr. 318.

⁶⁴ According to Dr. Manuel, GM establishes APR territories based on the use of "air distance" miles and census tracts. Applicant's Ex. A-11.

APR, based on his understanding of how GM defines them. In doing so, he assigned the census tract in the market to the dealer that was closest in air distance to the centroid of the census tract.⁶⁵

Dr. Manuel stated that the air distance dealer area represents the geography within which a dealer has an absolute proximity advantage over every other dealer of the same brand. A customer within that APR will find it more convenient to shop at the resident dealership than at any other dealership of the same brand. He said that most manufacturers and distributors use the air distance dealer area as the starting point for evaluating a dealer's sales performance.⁶⁶

Dr. Manuel also concluded that the Lower Rio Grande Valley's demographic patterns favor the relocation because there is a greater concentration of high income households in the western portion of the market near the proposed Weslaco location than in the current Harlingen location. Households and population in the areas surrounding both the Applicant and Protestant are projected to continue their substantial growth in the coming years.⁶⁷

More households with income levels of over \$100,000 are located on the western side of the market. The Payne dealer area is projected to grow in population from 331,397 in 2007 to 358,191 in 2012. This dealer area is expected to increase by 8.1% in population and 9.1% in number of households. The Bert Ogden area is expected to grow at a much higher rate. In 2007, the estimated population was 561,209 with a projected population of 647,560 in 2012. About 188,407 households are projected by 2012. The dealer area is projected to grow 15.4% in population and 16.8% in number of households.

With respect to registration and demographic trends, registrations of new retail Cadillacs sold to customers who registered them to addresses in the Lower Rio Grande Valley increased nearly

⁶⁵ Tr. 346-348; 450-459.

⁶⁶ Dr. Manuel used the terms "APR" and air distance dealer area interchangeably. Applicant's Ex. A-11, p. WM-00-1115.

⁶⁷ Dr. Manuel relies upon data from Claritas, Inc., concerning population, household counts, projections, and income. Applicant's Ex. A-11, p. WM-00-1113.

300% in 2007, from 281 in 2001 to 838 in 2007. In 2008, it is expected that Cadillac registrations will be 1,027. There was similar growth in Cadillac registrations in McAllen and Weslaco dealer areas, but it leveled off in the McAllen area after 2006.

Assessment of the Marketplace and Representation of the Brand

Dr. Manuel states that many luxury brands, including Acura, Audi, Infiniti, Lexus, and Porsche, among others, do not have a dealer in the Lower Rio Grande Valley. He concludes that there is much less inter-brand competition for Cadillac than in other markets in Texas who have a greater number of luxury dealers. Because of the lower competition with other luxury brands, he explained, the Cadillac brand should, and does, achieve a higher market share in the Lower Rio Grande Valley than in Texas as a whole.⁶⁸

With respect to measuring a brand's market share performance, Dr. Manuel noted that several methods could be used. The simplest method compares the number of Cadillac registrations in the area to the number of registrations of all brands. The resulting ratio is the market share of the brand, also called "market share," "market penetration," and "market performance."⁶⁹

Once a brand's market share in an area has been calculated, that market share can be compared to the market share in a benchmark area. As a benchmark area, GM uses the market share for the state as a whole. Other manufacturers use a local area, the state, a multi-state region, or the nation as a whole for their benchmarks.

Another refinement in measuring market share performance is to apply "segmentation analysis." Segments refer to vehicle categories such as small car, mid-size car, large car, small SUV, small pickup, etc. Segmentation analysis adjusts the expected brand market share in the local market

⁶⁸ "Market share" refers to the number of sales of that brand divided by the number of sales of all brands combined. Applicant's Ex. 1-11, p. WM-00-1112. Dr. Manuel notes that for a brand such as Cadillac, a more common definition of market share is the number of Cadillac sales divided by the number of sales of all brands' models that GM considers to be competitive with Cadillac's models, together with the Cadillac models.

⁶⁹ These terms are used interchangeably, according to Dr. Manuel. Applicant's Ex. A-11; p. WM-00-1117.

for differences between the local area and the benchmark area in the relative demand for each product segment. The adjustment is performed by calculating the number of registrations that the brand would need to have in each product segment in the local area in order to have the same market share in each product segment that the brand has in the benchmark area. Adding the numbers across all segments in the local area results in a number of "expected" registrations for the brand in the local area that are needed to match the market share of the brand in each product segment in the benchmark area.⁷⁰

A limitation to segmentation analysis (though it is widely used) is that it does not adjust for differences in inter-brand competition between a benchmark area and the market under study. This limitation is a significant problem in using the whole state of Texas as a performance benchmark for measuring the Lower Rio Grande Valley because the Valley has no representation of many inter-brand competitors, such as Acura, Audi, Infiniti, Lexus, Porsche, etc., that are normally considered competitive with Cadillac. Therefore, Cadillac performance in the Valley is artificially elevated when compared to Texas.⁷¹

Dr. Manuel compared the performance of all represented competitive brands in the Lower Rio Grande Valley based on those brands' performance in Texas. Without the competition found elsewhere in Texas, those brands (as a whole) performed approximately 40% better in the Lower Rio Grande Valley than in the state of Texas as a whole. Dr. Manuel concluded that using the state of Texas as the benchmark is using too low of a benchmark.

Dr. Manuel reported that Cadillac's segment-adjusted market share is not uniform throughout the Lower Rio Grande Valley: It performs much better in the eastern portion (containing Brownsville) than in the western portion (containing McAllen and Weslaco). This reduced performance, he claims, offers substantial available opportunity for additional Cadillac sales by the relocated franchise. If Cadillac had performed as well in the McAllen and Weslaco area as it

⁷⁰ Applicant's Ex. A-11; p. WM-00-1117.

⁷¹ Applicant's Ex. A-11, p. WM-00-1118.

performed in the Brownsville area, there would have been nearly 200 additional Cadillac sales in the McAllen and Weslaco areas in 2007.

“Registration effectiveness” refers to the ratio of the actual number of registrations to the expected number. When the ratio is 1, the brand is 100% “registration effective”. In determining market share performance for brands like Cadillac (with a limited product line), another method is to take the number of Cadillac registrations in the area divided by the number of registrations in the area of all brands’ models that GM considers to be competitive with Cadillac’s models. This model is called a “competitive” registrations model.⁷²

When the state of Texas is used as the benchmark, using data from 2007, there were 3,183 competitive registrations among the six GM-defined segments for Cadillac, leading to a calculation of 585 expected Cadillac registrations in the Valley. The actual number of registrations in the Valley in 2007 was 838, thus showing a ratio of 143.25%. Thus, Cadillac was 143.25 percent registration effective in the Valley based on the Texas benchmark.⁷³

Cadillac’s market share as a percent of competitive registrations is much higher in the Valley than in the rest of the state (for 2005, it was 144%, for 2006, it was 166%, for 2007, 167% and through March 2008, it was 174%).⁷⁴ Cadillac registrations in the state of Texas as a percent of competitive registrations are 15.67%; for the lower Rio Grande Valley, it is 26.33%.⁷⁵ The LRGV outperforms the state by 167.98%.⁷⁶

Dr. Manuel determined that an appropriate benchmark to determine whether the brand is adequately represented in the market would be a more-similar market than the state of Texas as a whole. He determined that using the Brownsville dealer area, after the proposed relocation, as a

⁷² Applicant’s Ex. A-11, p. WM-11-1117.

⁷³ Tr. 344.

⁷⁴ Applicant’s Exs. A-11 and A-4.

⁷⁵ Tr. 342.

⁷⁶ Tr. 342.

benchmark was appropriate because the Texas benchmark was too low; the Brownsville demographics, including income and ethnicity, were more similar to McAllen and Weslaco than the Texas demographics; inter-brand competition with the Brownsville dealer area after relocation is comparable to that in the combined McAllen-Weslaco dealer areas; and, Cadillac has strong customer acceptance in the Valley.⁷⁷ Further, it is Dr. Manuel's opinion that Brownsville is more like the rest of the Valley than is the state of Texas.⁷⁸

This analysis, involving the consideration of census tracts and measuring performance against the Brownsville dealer area after relocation, demonstrates that there is substantial shortfall on the western side of the market between Weslaco and McAllen. According to Dr. Manuel, this is because of the weak performance by Cardenas, who sold only 13 new Cadillacs in 2007.⁷⁹ In contrast, Bert Ogden Cadillac reported selling 492 new Cadillacs in 2007.

Dr. Manuel testified that he was aware that it had been reported in the newspaper that GM plans to close nine plants and 1,750 dealerships by 2012.⁸⁰ However, because of the superior performance of Cadillac in the Valley, he believes it is unlikely that GM will reduce dealerships there.

Competition

Cardenas (in Harlingen) made only 11 new retail Cadillac sales that were registered in 2007. Replacing this weak dealer with a stronger dealer in Weslaco will provide a more competitive marketplace for current and prospective Cadillac consumers.

⁷⁷ Tr. 314.

⁷⁸ Tr. 315. Using Brownsville as a benchmark resulted in an apples to apples comparison. Tr. 451.

⁷⁹ Only 11 Cadillacs were registered as a retail sale in 2007.

⁸⁰ Tr. 430-431.

The Weslaco dealer will provide a much larger sales facility than the Cardenas dealership and will spend substantially more money on advertising, thereby increasing consumer awareness of the Cadillac brand in the Valley and leading to an overall increase in Cadillac sales.

Replacing Cardenas with a stronger, better-located competitor will provide a more competitive marketplace for current and prospective Cadillac consumers.

Impact on Protestant

In determining harm to dealer, Dr. Manuel considers "harm" to be a material injury to profit on a long-term basis.⁸¹ He views one to two years as a short-term period, with five years or more as a long-term period. He noted that quantifying a material injury is difficult, but he testified that the state of New Jersey has determined a loss in profit of 25% to constitute a material injury. Dr. Manuel thinks that the New Jersey standard may provide a good threshold benchmark, but that other factors should be considered.⁸²

He suggests that the most important factor is the expected number of sales a new dealer would likely make, in comparison to the available sales opportunity in the area. If the opportunity is larger than the expected number of sales, most or all of the new dealer's sales are probably incremental additions to the market rather than sales taken from an existing dealer. He believes that is the situation with Weslaco. The second factor to consider is the size of impact that would occur in the event the new dealer's sales are not mostly incremental. If this were the situation (which he disputes), Bert Ogden would lose 7% of its Cadillac registrations, 8.8% of expected Cadillac registrations, and 8.3% of competitive registrations. Using 2007 data, the Bert Ogden dealer area would lose 20.9% of its population and 19.6% of its households. The number of high income households, a better indicator of potential Cadillac customers, would decrease by 9.7%. The 2012 data predicts similar changes.

⁸¹ Tr. 330.

⁸² Tr. 332.

Dr. Manuel emphasizes that Mr. Payne sells more GM vehicles than the number that GM expects him to sell ("expected sales") given the size of Mr. Payne's market area. If he is as successful in his Cadillac franchise, the sales above the number sold by Cardenas would still be lower than the available opportunity for Cadillac sales in the McAllen/Weslaco areas, suggesting that the adverse impact on Bert Ogden from the proposed relocation would be low, and Bert Ogden would remain highly profitable and a strong competitor with Weslaco.

Even after the proposed relocation to Weslaco, the Bert Ogden dealer area will still be substantially larger than the other two dealer areas, containing more than five times the number of Cadillac registrations as the proposed Weslaco dealer, and more than four times the number of expected Cadillac and competitive registrations. Bert Ogden's dealer area would also remain substantially larger than that of Luke Fruia. It would still contain approximately 70% more people and households than the proposed Weslaco dealer area, and over 90% more people and households than the Brownsville dealer area. It would also have more than twice as many households with incomes of \$100,000 or more than the other dealer areas. Based upon these factors, Dr. Manuel concluded that Bert Ogden Cadillac would still have a very substantial business base even after the relocation.⁸³

After reviewing Bert Ogden's information on sales and repair orders, Dr. Manuel concludes that approximately 5.9% of Bert Ogden's Cadillac customers in 2007 would have been closer to the Payne dealership than Bert Ogden in 2007, resulting in a possible loss of used Cadillac sales of 14.3%, lost service sales of 8.1%, and lost body shop sales of 8%. He noted that this suggested possible lost sales by Bert Ogden in the event of the proposed relocation. However, he used a retail sales index analysis using the Brownsville dealer area as a benchmark. The number of expected Cadillac registrations in the dealer areas containing the Applicant and Protestant were 152 and 626 units, for a total of 778 units in 2007. When compared to the 580 actually registered in those two dealers areas, 580 (91 plus 489), there is a shortfall of 198 units (778-580), demonstrating a lost opportunity for sales.

⁸³ Applicant Ex. A-11, p. WM-00-1113 and pp. WM-00-1121-1123.

Weslaco's overall sales effectiveness for its four GM franchises was 120.92% in 2007.⁸⁴ Applying that sales effectiveness ratio to the number of expected Cadillac registrations in the proposed Weslaco dealer area, Weslaco would have sold 184 Cadillacs nationwide in 2007 (which is 173 units higher than those sold by Cardenas who sold 11.) Because the 173 unit projected increase is lower than the 198 units of lost opportunity for Cadillac in McAllen and Weslaco, it demonstrates that there will be a low risk of adverse impact to Bert Ogden. If Dr. Manuel had used the state average, the projected increase in sales would be even lower. In analyzing lost sales, Dr. Manuel concluded that it could cost an estimated reduction of \$141,382 in net profit before taxes for 2007. However, he noted that Bert Ogden would also have had a 22% profit as a percentage of net worth, the industry average in 2007. Profit as a percent of sales would have been 2.4% which was well above the industry average of 1.5% in 2007. However, the more likely outcome is that there would be little or no impact at all.

According to Dr. Manuel, Bert Ogden is a strong dealer for Cadillac, offering an attractive facility, high levels of customer satisfaction, competitive new vehicle gross profits,⁸⁵ above average profitability and above state average sales performance.⁸⁶ It has had strong financial performance over the past several years and should be able to compete effectively against the proposed Weslaco dealership.

In summary, Dr. Manuel concluded that increased market share can be achieved in the Lower Rio Grande Valley by relocating the franchise from Harlingen to Weslaco, improving accessibility and visibility for the Cadillac brand for the higher income households in the Valley. The large amount of uncaptured Cadillac opportunity in the McAllen and Weslaco dealer areas, together with the strengths of the Bert Ogden dealership, should allow the relocation to occur without any material

⁸⁴ Dr. Manuel stated that GM uses this ratio to evaluate sales performance of its dealers. The ratio is called the Retail Sales Index. Applicant's Ex. A-11, p. WM-00-1122. The ratio is calculated by the number of new vehicles that the dealer sold anywhere that year in the numerator divided by the number of expected registrations in the dealer's APR in the denominator.

⁸⁵ According to Dr. Manuel, "gross profits" refers to the dealer's markup on the car, i.e., the difference between what the dealer paid for the car and what the customer paid for the car. Applicant's Ex. A-11, p. WM-00-1114.

⁸⁶ Applicant's Ex. A-11, p. WM-00-1124.

impact on Bert Ogden. Even if some impact occurred, it is likely to be small and Bert Ogden would still be highly profitable.⁸⁷

Dr. Manuel criticized Dr. George Berry's (Protestant's expert witness) projected impact to Bert Ogden of 28 to 30% loss of profits because his analysis was premised on the use of Highway 81 as the western boundary for the Weslaco APR, which Dr. Manuel said is contrary to the way any manufacturer does it.⁸⁸ By moving the boundary east of 281, Dr. Manuel claims that Dr. Berry took a number of census tracts outside the Mission-McAllen dealer area and put them into the Weslaco dealer area, resulting in an inflated loss of territory for Mission and McAllen.⁸⁹ Dr. Manuel contended that, even using drive times based on the actual highway network and population centroids, the Weslaco dealer area would still fall short of Highway 281.

Dr. Manuel noted that the reports related to profitability for Bert Ogden do not contain information about the used car business because it is reported as part of its Chevrolet store.⁹⁰ According to Dr. Manuel, this means a profit center is missing from the financial statement so that the reported profitability for the dealership is probably understated, leading to an impression that it would suffer greater loss from the operations of the Weslaco dealership than it actually would. He noted that this is so because, usually, the used car component of a dealership is a profitable..

2. Protestant's Evidence

Protestant presented the testimony of Dr. George Berry and Robert Vackar, the dealer/principal of Bert Ogden Cadillac, and numerous exhibits.

⁸⁷ After preparing his report, Dr. Manuel was deposed and Dr. Berry were deposed. Based on those depositions and in response to supplemental exhibits from Protestant, Dr. Manuel prepared some updated exhibits. Applicant's Exs. A-105, 106, 107, and 108. Dr. Manuel recalculated "available opportunity" of Dr. Berry's conclusion that Weslaco could make 91 retail sales. He subtracted the 11 actual Cardenas sales and concluded that there would be a projected sales gain of 80 retail sales (instead of the 198 he calculated) for the available opportunity. Tr. 311-312; Ex. A-105.

⁸⁸ According to Dr. Manuel, manufacturers assign individual census tracts based on proximity to the dealer. Accordingly, he used the same method in his analysis.

⁸⁹ Tr. 471-472.

⁹⁰ Tr. 477.

a. **Dr. George Berry's reports and testimony**

Dr. Berry provided economic, demographic and financial consulting services primarily within the State of Texas. His qualifications can be found in Protestant's Ex. P-1. Applicant did not object to Dr. Berry's qualifications to provide expert testimony in this matter.

Dr. Berry asserted that the impact of the relocation of the Cadillac dealership to Weslaco to Bert Ogden will be from a number of factors: (1) the current trend for a declining Cadillac market; (2) the decline in total sales for motor vehicles; (3) the negative general conditions; (4) the apparent financial problems of General Motors; and (5) a number of other factors. He further contended there will probably be no incremental increase in the market because it is already super-adequately served.⁹¹ He further asserts that there will be an impact on Bert Ogden caused by the loss of almost 33% of the market area population, 24% of the households with incomes of \$50,000 or more, and an 18% loss in the number of households with incomes of \$100,000 or more.⁹²

Dr. Berry testified that his main point of disagreement with Dr. Manuel was that Dr. Manuel failed to consider the current economic situation. He notes that Dr. Manuel's information is based upon data from 2007 and partial 2008. He testified that he believes the focus for determining impact on Bert Ogden should be on the last three to four months. Dr. Berry testified that GM's plan of reorganization includes cutting down 1,750 dealerships and that Congress must help GM to survive. He also testified that Cadillac sales were down 55% on a national average and that Cadillac sales with Bert Ogden were down 50%. He anticipated a continued decline of sales into the future, citing to *Automotive News* that reports Cadillac's 2008 share of the market through September was 1.2%.⁹³ The reported sales for September 2007 vehicles were 20,398 vehicles and for September 2008, the sales were 12,432, indicating a decline in sales of 39.1%.⁹⁴

⁹¹ Exhibit P-1, p. 13.

⁹² Dr. Berry's report, Exhibit P-1, Tab 10.

⁹³ Tr. 502; 661.

⁹⁴ Tr. 505-508.

According to Dr. Berry, Bert Ogden has calculated a break even point of 25 Cadillac units per month. He said that they sold 20 units or less in November 2007, so they are operating unprofitably. In that situation, he testified that each additional lost sale will magnify the losses even more.⁹⁵ He contended that the state is in a recession, and it is appropriate to look at the near future to determine whether the proposed relocation should be approved.⁹⁶

Dr. Berry asserted that the percentage of households with an income level of \$100,000 or above is lower in Weslaco than in the Brownsville or Mission/McAllen areas, and the median household income is lower in Weslaco than those areas, as are the per capita income and the population growth. Consequently, he believes that Weslaco is not comparable to the other two areas and wholly rejected use of the Brownsville dealer area as a basis for determining whether the brand is adequately represented and whether there will be harm to Bert Ogden.⁹⁷

Dr. Berry testified that Bert Ogden is operating at a loss and any additional competition would cause additional harm to Bert Ogden to the general detriment of the public.⁹⁸ As he noted, "you can continue to operate unprofitably, and you can survive for a period of time, but you can't survive indefinitely."⁹⁹

The opening and closing of a Cadillac dealership in Weslaco would not be in the public interest.¹⁰⁰ Dr. Berry said it is the usual practice for a manufacturer to intervene in these proceedings and take a position, one way or the other, but that GM did not do so.¹⁰¹ He believes competition would be ruinous because it would cause loss to Bert Ogden.¹⁰²

⁹⁵ Tr. 507.

⁹⁶ Tr. 523-526.

⁹⁷ Tr. 533-556.

⁹⁸ Tr. 584.

⁹⁹ Tr. 529.

¹⁰⁰ Tr. 585.

¹⁰¹ Tr. 585-586.

¹⁰² Tr. 589.

Dr. Berry disputed that Payne's experience in GM products provides a plausible comparison to Cadillac sales because Weslaco's GM line includes lower-priced and more popular vehicles (Chevrolet and GMC light trucks) in contrast to the higher priced Cadillac, with a smaller consumer population. If this assumption is used, Dr. Berry claimed that Bert Ogden would experience 28% lost sales.

Dr. Berry says the impact of the proposed dealership will be significant and will render Bert Ogden unprofitable due to the loss of market area and declining sales due to unfavorable economic conditions. In particular, Dr. Berry opined that the APR of Bert Ogden would be changed if the relocation is approved and would most likely result in the Weslaco market being extended to Highway 281.¹⁰³ However, Dr. Berry agreed that GM would not use this method of locating the market area, agreeing that GM used the population centroids and straight-line distance as discussed by Dr. Manuel.¹⁰⁴ He also admitted that moving the western boundary for the Weslaco market area allowed him to count more households into his adverse impact analysis.¹⁰⁵

The impact analysis used by Dr. Berry showed a loss for new car sales ranging from 18 to 30%.¹⁰⁶ At the 18% level, Dr. Berry testified this would mean that Weslaco would take 89 vehicles from Bert Ogden. A 20% level would mean that Weslaco would take 98 vehicles; a 28% level would mean that Weslaco would take 138 units; a 30% level means that Weslaco would take 138 units; and a 30% level is derived from lost sales of 148 units.¹⁰⁷ However, he acknowledged that he does not believe Weslaco will make 91 sales as predicted by Dr. Manuel.¹⁰⁸

Dr. Berry contended that the investment and method of operation for Bert Ogden are effective and that this dealership has demonstrated its ability to provide excellent service to the general public.

¹⁰³ Tr. 552-555.

¹⁰⁴ Tr. 552-556.

¹⁰⁵ Tr. 555-556.

¹⁰⁶ Tr. 559.

¹⁰⁷ Tr. 559-560.

¹⁰⁸ Tr. 560-561.

As such, Dr. Berry contended Bert Ogden should be allowed to continue with his successful operation without the hardship that will result from the Weslaco dealer's operations.

b. Testimony of Robert Vackar

Mr. Vackar is the principal of Bert Ogden Cadillac. He testified that he is in compliance with his dealer's franchise from GM. He has been in the Cadillac business since 1997. It is his understanding that Cadillac will likely drop some of its product lines as a result of the economic situation. He testified that GMAC used to have a Smart Buy program to help younger buyers purchase the Cadillacs; however, that was cancelled in October 2008. GMAC has run into financial difficulty. Mr. Vackar testified that he turned down more inventory that was offered by GM because he had plenty of inventory that was available for sale.¹⁰⁹

Mr. Vackar testified that he does not believe in the future of the GM brand and he cannot sell his GM franchise, although others have contacted him to buy some of his other franchises, such as Nissan/BMW. He said he would sell his GM franchise to the factory if they would pay him for the real estate.¹¹⁰ Mr. Vackar also testified that he was concerned about the ability to get product from Cadillac in the future.¹¹¹

Mr. Vackar testified that it was difficult to move buyers of the other luxury lines into Cadillacs because they were more definite about what they wanted. Mr. Vackar said that he can be profitable if he makes 25 sales of Cadillacs per month. In November 2007, he only sold 22. Mr. Vackar testified that if sales were only 20 units per month, he will lose \$250,000. He has had to cut pay at the dealerships, cut bonuses, forfeit his consultant fee per car, and forfeit collecting rent, among other measures, in order to cut costs. He testified that he believes he will lose \$500,000 based on Cadillac sales of only 20 units per month. He testified that he believed the economy would stay in a downturn for a while longer, probably until 2011 or so.

¹⁰⁹ Tr. 610.

¹¹⁰ Tr. 618-619.

¹¹¹ Tr. 626.

Mr. Vackar's Cadillac franchise has made a profit since 1997. However, in November 2007, it did not. He reported profits as follows: in 2003, \$136,000; in 2004, \$923,000; in 2005, \$995,000; in 2006, \$1,099,328; in 2007, \$526,000; in 2008, through September, \$526,000; and in October 2008, \$10,000.¹¹²

Mr. Vackar disputed Dr. Manuel's conclusion that he could increase his sales of Cadillac because of the inter-brand competition with Mercedes, BMW, Land Rover, Volvo, and Jaguar. He said "I'd love to have a Cadillac dealership in Harlingen or Brownsville. I have no competition. I'm getting - I'm getting beat to death. I tell you, I'm very, very satisfied with my numbers. I don't think there's anywhere to go."¹¹³ He claims that he is successful because there are, in reality, only two Cadillac dealers in the Valley with sixty miles between them.¹¹⁴

D. Analysis

This is a difficult case, due to factors related to the Lower Rio Grande Valley (LRGV) and the current economic situation in the nation. It is undisputed that the LRGV is an insular region, with unique characteristics when compared to the rest of the state of Texas. It contains a population that continues to greatly increase in number, unemployment rates that have closed the gap to be almost the same as that of the rest of the country (after being much greater for years), and an income level lower than the median income level for households in Texas.

News of the national financial situation has been prominent for the past months. As the parties discussed, the auto manufacturers have requested money from the federal government to continue their operations. Even upon receiving the funds, it is not certain that the major domestic manufacturers will continue to stay in business. GM may be required to file for bankruptcy. While there is much speculation about whether and when the economy will rebound, no one knows for certain. It is not known how the national economic situation will affect the various states, including

¹¹² Tr. 624-625.

¹¹³ Tr. 628.

¹¹⁴ Tr. 628.

the State of Texas and, in particular, the portion comprising the LRGV. Consequently, there are many unknowns about the financial stability of the auto manufacturers and the country that, while undoubtedly may have an effect on the final result in this matter, are too speculative to attempt to predict. Consequently, the ALJ does not purport to "see into the future" to make predictions about the future economic situation or to base her recommendation in this case on such matters.

Instead, the evidence clearly demonstrates that Cadillac is a strong luxury automobile product that is bought and registered in the LRGV at a rate far exceeding the Texas average, despite the lower overall income level of the population in the LRGV. Further, other luxury model cars are also bought and registered in the LRGV at a rate exceeding their overall sales average for the rest of the state. It is clear that luxury vehicles have a viable and active purchasing market within the LRGV and, while there was evidence that the immediate demand for these products may have slowed, there was no evidence that it has been extinguished.

The evidence established that Edwin Payne of Weslaco Motors and Bob Vackar of Bert Ogden Cadillac are experienced and successful dealers. They have each consistently scored well in measures for success for the GM products sold. Both dealers understand the dealer business and competently run their dealerships. However, they strongly disagree that Weslaco Motors should be allowed to amend its license to obtain a Cadillac franchise. Mr. Vackar of Bert Ogden contends that this would significantly affect his business, and that his currently unprofitable Cadillac business would further decline to a point of severe, negative impact. Weslaco Motors contends that there is sufficient lost sales opportunity and an overall market in the LRGV that will satisfactorily support three Cadillac dealers when the relocation of the Cardenas Cadillac franchise occurs.

The two expert witnesses in this case are both well-qualified, experienced economists. They provided useful analysis in this matter. However, the ALJ was ultimately persuaded by Dr. Manuel's testimony and reports because his analysis appeared to be based on specific conclusions, based upon the performance of dealers in the same location of the State, thereby resulting in a more accurate prediction of lost sales opportunity and impact on Bert Ogden. The ALJ will address each of the statutory factors in light of the evidence presented.

a. Adequate Representation of Cadillac

In the mid-Valley Cadillac market, every GM dealer outperformed the Texas average market share benchmark for their GM products by 20% to 74%.¹¹⁵ Dr. Manuel contends this is due to disparate demographics between the benchmark (Texas) market and the Valley market, creating the appearance that dealers are over-performing when that might not be the case. For example, he contended that consumers in the market may prefer the product at issue to a greater degree than the consumers in the benchmark market. Because of this, Dr. Manuel advocated the use of a different benchmark other than the Texas benchmark.¹¹⁶ On the other hand, Dr. Berry contended that the Texas benchmark is an appropriate one and indicates that there is adequate representation in the Valley.

Dr. Manuel developed a different benchmark which he referred to as the "Brownsville benchmark." He noted that in the Valley, there is considerably less competition for luxury vehicles than in the state of Texas as a whole.¹¹⁷ This leads to the expectation that Cadillac dealers in the Valley will outperform the Texas average market share because of less competition. Dr. Manuel's testimony that the Brownsville benchmark is more appropriate for the analysis was persuasive. He noted that income levels, employment levels, product preferences, inter-brand competition levels, ethnicities, and proximity to the Mexican market were more similar to the mid-Valley market than was the state of Texas market.¹¹⁸ By comparing the performance of the Cadillac dealers serving the mid-Valley area to the Cadillac dealers serving the Brownsville market, he concluded that there would be an additional 200 sales based upon 2007 data.¹¹⁹ These additional sales represent "lost

¹¹⁵ Payne sold approximately 120% of the Texas benchmark in 2007 for all GM brands combined (Applicant's Exhibit A-13, Tab 18, p. 1); Bert Ogden sold approximately 127% in 2007 (Applicant's Ex. A-13, Tab 26, p. 5); Frula Cadillac sold approximately 174% in 2007.

¹¹⁶ There was evidence that GM uses the Texas benchmark. Applicant explains that most manufacturers use a benchmark geography which can be used conveniently and consistently for the maximum number of dealers, such as a state, region, or national market share. Tr. 460-461. Dr. Berry did not sufficiently explain why he believed his deviation of the 6m methodology was warranted.

¹¹⁷ He noted that a number of luxury brands are not present in the Valley, such as Acura, Infinity, Audi, Lexus, and Porsche.

¹¹⁸ Tr. 314-316.

¹¹⁹ Tr. 311-312, Applicant's Ex. A-13, p. 4.

opportunity” in the mid-Valley Cadillac market and demonstrate inadequate representation. Applicant contends he will be able to capture the lost opportunity by moving the Harlingen Cadillac store to the Weslaco store.

Applicant suggests that Mr. Vackar's testimony regarding Cadillac inventory that he refused, coupled with his testimony that he no longer believed in the future of Cadillac, may be indicia of inadequate representation. The ALJ is not persuaded by this argument. It was clear from Mr. Vackar's testimony that he was frustrated with the state of the economy and his dealership. Applicant did not present any authority to support such a finding and the ALJ declines to adopt this rationale.

Dr. Manuel also supported his belief of inadequate representation by performing an optimal location analysis. This analysis looks at the registration data from purchases to determine the location of those buyers who have purchased a high line product, such as Cadillac, BMW, or Mercedes. Dr. Manuel concluded that an optimal location for an additional Cadillac dealer would be several miles west of Highway 281; however, this would put the Weslaco dealership inside Bert Ogden's APR. After relaxing his criteria, Dr. Manuel determined that the optimal available location would be within the census tract in the vicinity of Weslaco Motors. Locating the dealership here will result in improved customer convenience and should result in increased sales of the brand. Further, customer service and sales should increase for actual and prospective customers in the McAllen/Mission/Edinburg area because they will have to travel only 20 miles to Weslaco for competitive sales and service. Additionally, the Harlingen customers will also be better served because it is more convenient for customers on the west side of Harlingen to travel to Weslaco than to travel to the east side where Cardenas is located.

b. Substantial Compliance with Franchise

Applicant acknowledges that this issue would not normally be of concern because both dealers testified that they were in compliance with their respective franchise agreements.¹²⁰ However, Applicant cites to Mr. Vackar's testimony that he was not currently buying Cadillac product from GM as evidence of a contractual breach of his franchise agreement.¹²¹ However, the ALJ is unpersuaded that this testimony establishes a lack of substantial compliance. Mr. Vackar also testified that he had plenty of inventory available at his dealership when he was asked to take some. Based on his reduced sales volume of only 22 Cadillacs per month, he told GM that he did not need any additional inventory. No evidence was offered indicating that a one-time refusal of additional inventory violated the franchise agreement, nor that GM considered Mr. Vackar to have breached his franchise agreement. Based upon the evidence presented that related to this issue, the ALJ finds that Protestant was in substantial compliance with his franchise.¹²²

c. Desirability of a Competitive Marketplace

Approval of the proposed license and the resulting operations of a third, active Cadillac dealership in the Valley will result in increased competition for Cadillac sales in this part of the state of Texas. As demonstrated above, the ALJ was persuaded that Applicant met its burden of showing that there is a "lost opportunity" for sales. As such, the three dealers will be in active competition for those sales, resulting in more opportunities for the public to be exposed to Cadillac through additional advertising. While the Protestant does not want increased competition, it did not offer evidence or legal authority for the proposition that an application should not be approved because it

¹²⁰ Mr. Payne at Tr. 76; Mr. Vackar at Tr. 596.

¹²¹ Tr. 620; Applicant's Ex. A-12, "Standard Provisions," Article 6.4, p. GM-00147.

¹²² The significance of a finding that a Protestant is not in substantial compliance is that the Protestant may not have standing to maintain his protest. See, e.g., *Gene Hamon Ford v. David McDavid Nissan*, 997 S.W.2d 298, 311 fn. 16 (Tex. App. - Austin 1999)

will result in increased competition. Protestant, a large and successful dealership, will have sufficient ability to compete with Weslaco Motors. Additionally, the degree of harm that will result to the Protestant by approving the application is not so great that it should outweigh the desirability for a competitive marketplace. While there were claims that another dealer would significantly harm Bert Ogden Cadillac, there simply was not sufficient evidence presented to support this contention.

Further, the additional customer market from Mexico and the demographics indicating that the Valley population will continue to grow, along with income and employment levels support a conclusion that, despite the current national economic crisis, the Valley is a viable market, with the potential for greater sales.

d. Any Harm to the Protesting Franchised Dealer

The evidence established that Protestant will suffer some harm as a result of the insertion of Weslaco Motors into the Cadillac business in the area. However, the ALJ found the expert report and testimony of Dr. Manuel to be more persuasive on this issue in terms of quantifying the degree of harm. Dr. Manuel's analysis showed that Protestant will experience an 8-10% decrease in profitability due to the sales anticipated by Weslaco Motors. This level of loss does not approach the 20-25% factor that has been considered by the state of New Jersey to demonstrate significant harm. While the MVD has not adopted a similar standard of harm, the New Jersey standard is useful in determining the degree of harm that is relevant in evaluating whether the positive effects resulting from increased competition outweigh the detrimental effects to the protesting dealer, including the possibility that the dealer would be forced out of business. It seems illogical that any showing of harm to a Protestant should result in a *per se* denial of an application and the Protestant in this case does not present this argument. Instead, the Protestant offered evidence, through Dr. Berry and Mr. Vackar, that they believe the level of harm would be a significant harm, resulting in potentially devastating consequences.

It is Dr. Berry's opinion that Protestant would be harmed by 20 to 30% in lost sales as a result of Weslaco's designation as a Cadillac dealer. Dr. Berry believes that the proximity of the Weslaco

dealership (some 20 miles away) necessarily means that some of the Ogden Cadillac customers will be attracted to the Weslaco dealership, resulting in sales through that dealer. In short, this evidence amounts to the conclusion that there is a fixed amount of potential customers ("the pie") and every customer for Weslaco means there is one less customer for Bert Ogden. While this argument has intuitive appeal, Dr. Manuel's evidence indicates that the pie is larger than that due to the opportunity for lost sales and that some of the customers who will purchase from Weslaco are not customers that Bert Ogden would have made a sale to anyway. It is the placement of the dealership in Weslaco, as opposed to Harlingen, that expands the overall pie of available customers.

Additionally, the Harlingen dealer did not appear to be attempting to fully develop his Cadillac business. A model of harm that assumes the existing number of Cardenas customers comprises the only available customer base, as suggested by Protestant, does not appear to acknowledge other factors suggested by Dr. Manuel, such as the inaccessibility of the Harlingen dealership in terms of being located away from a visible location by a major roadway and the overall absence of any sales promotion, which would explain why that customer base is so low. By changing these factors, Dr. Manuel concludes that the Weslaco dealership will increase the "pie" so to speak, and consequently, expand the overall customer base. Indeed, based on the analysis of Dr. Manuel, the relocation will result in the Luke Fruia dealership gaining customers while the Bert Ogden dealership may lose a small percentage of customers.

Additionally, Dr. Manuel's analysis did not include projected sales based upon the projections for increased population growth in the Valley, increased household income levels, and increased employment opportunities. If this market area continues to expand, there will be potentially more opportunities for sales for all three dealers. Consequently, Dr. Manuel's projections may be less than what can be reasonably anticipated.

Dr. Berry's analysis of harm appeared to be based on reports of dealer profitability that may not have included complete information, given the lack of information regarding used car sales and the failure to explain why this was reported on the Chevrolet-line reports that were not submitted by Protestant as part of the record. This lack of information called into question the accuracy of

Dr. Berry's overall impact analysis. Dr. Mamel testified that this was puzzling and resulted in impact numbers that may be inaccurate. The ALJ was persuaded by this argument. It seems that the profitability conclusions reached by Dr. Berry may be distorted and incomplete, resulting in an inflated assertion of harm.

This factor is also related to the factor of competition. Some level of competition is desirable - it encourages a dealer to continue to provide high quality performance such as for repairs, maintaining the appearance of the dealership, and operations, among other things. If a dealer believes that he may lose sales due to a nearby competitor, he may be more likely to insure that his dealership has something more to offer to the customers, such as improved service. If so, the public will benefit from this scenario.

e. The Public Interest

The evidence supports a finding that the public interest will be served by approval of the application and harmed if the application is not approved. If Weslaco begins operations as a Cadillac dealer, the public will have three active Cadillac dealers from which to choose in terms of competitive shopping. Currently, while there are three dealers, one is not very active and a proposal for termination of its franchise is pending. As noted by Applicant, if the Cardenas franchise is terminated, it will result in a greater amount of area to be covered by only two dealers, requiring Cadillac customers to drive a greater distance. For example, a potential customer from the McAllen-Edinburg-Mission area (Bert Ogden dealer area) will have to travel 60 miles to Brownsville (Luke Fruia dealer area) in order to comparison shop. Likewise, a prospective consumer from Brownsville would have to travel 60 miles to Mission to comparison shop. A Weslaco consumer would have to travel either 20 miles to Mission (the closest dealer) or 40 miles to Brownsville (Luke Fruia), while a Harlingen consumer would have to travel 20 miles to Brownsville (Luke Fruia) or 20 miles to Mission (Bert Ogden).

Mr. Payne testified that new vehicle buyers generally purchase vehicles within 13 miles of their residence, while used car buyers purchase used vehicles within a seven mile radius. He added

that service customers usually seek service within a 10 mile radius.¹²³ Mr. Vackar also testified that a majority of his sales come from within 25 miles of his dealership. Consequently, having 60 miles between two dealers (Bert Ogden and Luke Fruita) will not serve the public's interest in either ability to purchase vehicles or obtain service.¹²⁴ This takes on greater significant in the area of warranty service. The evidence in this case established that only authorized Cadillac dealers are permitted to perform warranty service on Cadillacs, except under limited circumstances.¹²⁵ In this situation, it is even more important for customers to be able to access a dealer within a reasonable distance in order for the warranty-covered repairs to be made.¹²⁶

Besides offering a convenience factor to the public, Mr. Payne's dealership offers a background of operation by someone who is an experienced and competent dealer. Mr. Payne is the dealer principal for a Dodge-Chrysler-Jeep store in Weslaco, a Ford-Mercury store in Weslaco, a Volkswagen-Suzuki dealership in Brownsville, a Mitsubishi-Jeep dealership in Harlingen, and the Pontiac, Buick, Chevrolet and GMC dealership in Weslaco. Mr. Payne's history as a successful dealer gives confidence to the public that the Cadillac dealership will be operated in a competent manner and that they can rely upon his past experience to do so. The evidence also established that Mr. Payne is actively involved in the local community and has engaged in substantial charitable and community service work.

Further, the application has been approved by GM, giving rise to an inference that GM finds some validity to the concept of having three Cadillac dealers in the LRGV. If not, it would have simply proposed to terminate the Cardenas dealership and disapproved Weslaco's application. This would have resulted in there being only two Cadillac dealers in the LRGV, a fact of which GM was aware. It is significant that the relocation of the dealership is within the same APR as the Cardenas

¹²³ Tr. 103.

¹²⁴ Tr. 641-642.

¹²⁵ Applicant's Exhibit A-109.

¹²⁶ As noted by Applicant, one of the MVD's key duties is to "provide for compliance with manufacturer's warranties." TEX. OCC. CODE § 2301.001(2). This duty may be undermined if consumers' accessibility to service in compliance is diminished because they will be more likely to have the service performed by someone other than an authorized Cadillac dealer.

dealership. There was testimony that the APR is the population base to which the dealer is most conveniently located, thereby providing sufficient business to the dealer.¹²⁷ GM reserves the contractual right to approve or disapprove relocations of its franchises and, as a policy matter, will ordinarily only allow relocations within the relocating dealer's own APR.¹²⁸ Because the auto dealership business is so capital-intensive, the establishment of an APR contributes to the financial viability of the business because the majority of sales most likely will come from within that APR.¹²⁹

In particular, while not having received evidence from GM that specifically states so, the ALJ has inferred from its approval of the Weslaco application and the relocation of a Cadillac dealership from Harlingen (the Cardenas dealership) that GM has concluded that three Cadillac dealerships in the LRGV are appropriate at this time. GM has provided a notice of termination of the Cardenas Cadillac franchise in which it states that the basis for termination is non-compliance with the franchise of the Cardenas dealership.

The MVD has also approved the application, subject to the protest. No evidence was presented to the ALJ as to what weight should be given to the MVD's approval. Nonetheless, the MVD's approval can be interpreted as establishing that there was nothing on the face of the application that caused concern to the MVD about the application.

As discussed above, the evidence does not support a finding that approval of the application and the resulting Cadillac operations by Weslaco Motor will result in the failure of an existing dealer, that of Bert Ogden, or a reduction of service to the public.¹³⁰

¹²⁷ Tr. 68-69.

¹²⁸ Exhibit A-12, pp. GM 00139-140, Sections 4.1-4.3; Tr. 69.

¹²⁹ Applicant contended that GM's contractual right to approve or disapprove relocations of franchise would be prejudiced if the application is not approved. The record does not contain evidence as to whether other remedies would exist to GM and the ALJ does not have to make this finding in order to concur with the rationale behind it.

¹³⁰ See, e.g., *Austin Chevrolet, Inc. d/b/a Munday Chevrolet/Geo and General Motors v. Motor Vehicle Board and Motor Vehicle Division of the Texas Department of Transportation*, 212 S.W.3d 425 (Tex. App. - Austin 2006).

E. Recommendation

Based upon the evidence and argument presented by the parties and the proposed Findings of Fact and Conclusions of Law set forth below, the Administrative Law Judge recommends that the Motor Vehicle Division approve the application filed by Weslaco Motors, L.P., to operate a Cadillac dealership at 2401 E. Expressway 83, Weslaco, Hidalgo County, Texas, and dismiss the protest to the application filed by Bert Ogden Chevrolet, Inc. d/b/a Bert Ogden Cadillac.

III. FINDINGS OF FACT

1. On or about August 8, 2007, Weslaco Motors, L.P. (Weslaco Motors or Applicant) as purchaser, entered into an Asset Purchase Agreement and an Advance Agreement with Cardenas Autoplex, Inc., of Harlingen, as seller, to purchase certain assets constituting substantially all of the assets of seller as a Cadillac automobile dealership.
2. The principal dealer operator of Weslaco Motors is Mr. Edwin "Bud" Payne.
3. By letter of September 20, 2007, Weslaco Motors submitted an application to General Motors (GM) for a Cadillac franchise to be located at 2401 E. Expressway 83, Weslaco, Hidalgo County, Texas.
4. Weslaco Motors currently operates a GM facility at the same location at which it proposes to sell Cadillac. It sells Chevrolet, GMC, Buick, and Pontiac motor vehicles as part of its GM facility.
5. By letter of November 29, 2007, GM approved the proposal of Weslaco Motors, subject to certain conditions, including obtaining all licenses necessary to operate a Cadillac dealership at the proposed location.
6. On or about December 7, 2007, Weslaco Motors submitted an application to the Motor Vehicle Division (MVD) of the Texas Department of Transportation to amend its Motor Vehicle Dealer's License to operate a Cadillac dealership at 2401 E. Expressway 83 in Weslaco, Hidalgo County, Texas.
7. On February 28, 2008, Berg Ogden Chevrolet, Inc. d/b/a Bert Ogden Cadillac, Inc., (Bert Ogden or Protestant) filed a notice of protest to the license application of Weslaco Motors with the MVD.
8. GM did not intervene in this matter and did not participate in the contested case hearing.

9. Bert Ogden's Cadillac franchise is currently located at 1400 E. Expressway 83 in Mission, Hidalgo County, Texas.
10. The Cadillac area of primary responsibility (APR) of Bert Ogden as designated by GM extends to Texas Avenue in Weslaco, Texas. It also includes Mission, McAllen, and Edinburg.
11. The proposed location of the Applicant's Cadillac franchise is approximately 21 miles from the Weslaco proposed Cadillac dealership and more than 25 minutes away in drive time.
12. The Applicant's Cadillac dealership, if approved, and the Protestant's Cadillac dealership will both be located in Hidalgo County, Texas.
13. Protestant is in compliance with its franchise from GM.
14. The MVD has approved Applicant's license application, subject to resolution of the protest by Ogden Cadillac.
15. GM has approved the application of Weslaco Motors to acquire the Cadillac franchise in Harlingen, Texas, and relocate it within the Harlingen APR established by GM.
16. GM has approved Applicant's proposed location, facility, and operations by a Letter of Intent, dated August 12, 2008.
17. An APR is a geographic area assigned by manufacturers to dealers and it is used to measure the effectiveness of dealer representation. It is comprised of a collection of census tracts assigned to a dealer by GM on an equidistance basis, and it is calculated to provide a penetrable population base sufficient to support a dealership.
18. Applicant's dealer principal, Edwin M. (Bud) Payne, is a skilled and experienced dealer operator who is capable of adequately serving the public interest in the mid-Valley market of the Lower Rio Grande Valley (Valley).
19. The Valley is comprised of the counties of Hidalgo, Starr, Cameron, and Willacy.
20. The mid-Valley market area of the Valley is comprised of the communities of Weslaco, Mercedes, and the surrounding communities.
21. The Valley is a relatively insular market for Cadillac because it is so far removed, geographically, from neighboring Cadillac markets, such as San Antonio and Corpus Christi, as to experience relatively low "in-sell" from markets outside the Valley.
22. "In-sell" refers to the registrations in the Valley market by dealers located outside the Valley market. This is also known as a "pump-in."

23. A motor vehicle dealer can make sells of vehicles to anyone, whether they reside within the dealer's APR or not.
24. All new vehicles are required to be registered in the location where the purchaser resides.
25. Mexican citizens can purchase vehicles in the United States so long as they are registered to an address within the United States maintained by the purchaser.
26. There are currently three franchised Cadillac dealers in operation in the Valley: Bert Ogden in Mission, Luke Fruia in Brownsville, and Cardenas Autoplex in Harlingen.
27. GM has filed a Notice of Termination to terminate the Cadillac franchise of the Cardenas Autoplex, located in Harlingen. That proceeding is currently abated.
28. In 2007, Cardenas made only eleven new retail sales of Cadillac.
29. The proposed relocation of the Cadillac franchise from Cardenas Autoplex in Harlingen to Payne Motors in Weslaco would still be within the Harlingen APR.
30. A motor dealer can relocate its GM dealership within his designated APR, subject to notice and approval by GM.
31. "Adequate representation" is defined, for purposes of these proceedings, as the number and placement of Cadillac dealerships in such a manner as to conveniently serve current and prospective Cadillac customers in the mid-Valley area without material harm to other Cadillac dealers.
32. GM measures Cadillac adequacy of representation using a Texas benchmark which is a comparison of Cadillac registration performance in a given area to Cadillac performance in the entire state of Texas.
33. The "Texas benchmark" for Cadillac registrations as a percent of competitive registrations in 2007 was 15.67 % in the State and 26.33% in the Valley.
34. In 2007, actual Cadillac registrations in the Valley, by segments, were 143.25% of expected Cadillac registrations based on comparison to the Texas benchmark. (Manuel Tab 6, p. 1).
35. Adequacy of representation can be determined by using methods other than the Texas benchmark.
36. One way of determining adequacy of representation is by comparing Cadillac market shares between the mid-Valley market and a like-kind benchmark market.

37. A "like-kind" benchmark market to the mid-Valley market is the Brownsville market because it is substantially similar to the mid-Valley market in terms of demographics, product preferences and proximity to the Republic of Mexico market.
38. A comparison of the Cadillac market shares between the Brownsville market and the mid-Valley market reveals available opportunity for a Cadillac dealer in the mid-Valley market.
39. Inter-brand luxury competition in the Lower Rio Grande Valley market is less than in the State of Texas market because a number of luxury brands are not available at franchised dealers in the Valley, such as Acura, Audi, Infiniti, Lexus, and Porsche.
40. The lack of inter-brand luxury competition has resulted in higher market shares for Cadillac in the (Valley) than in Texas as a whole. It also has resulted in a higher segmented-adjusted market share than in Texas as a whole.
41. "Market share" is the number of sales of a brand divided by the number of sales of all brands combined. In the case of Cadillac, which has a limited product line, it is defined as the number of Cadillac sales divided by the number of sales of all brands that GM considers to be competitive with Cadillac.
42. In general, the population buys new cars from dealers located between 10-25 miles from them and will go to a dealer located 7-13 miles for service.
43. If the Cardenas Cadillac franchise is terminated and Applicant does not receive approval for its license to operate a Cadillac franchise, there will be only two Cadillac dealers in the Valley, *i.e.*, Luke Fruia in Brownsville and Bert Ogden in Mission.
44. The distance between the Luke Fruia and Bert Ogden Cadillac dealerships is approximately 60 miles.
45. Only authorized Cadillac dealers are permitted to perform warranty work on Cadillacs, except under emergency conditions.
46. If Applicant's application is denied, current and prospective Cadillac owners in the mid-Valley market would have to travel up to 20 miles to Mission or 40 miles to Brownsville for Cadillac sales or service.
47. An "optimal location" for a dealership is a location which conveniently services the highest and densest concentration of actual and prospective customers of the brand represented by the dealer.
48. Applicant's designated location for its Cadillac dealership is within the optimal location for a Cadillac dealer.

49. Cadillac's segment-adjusted market share is not uniform throughout the (Valley). In the eastern portion of the Valley (containing Brownsville), Cadillac performs much better than it does in the western portion (containing McAllen and Weslaco).
50. If Cadillac performed as well in the McAllen and Weslaco areas as it performed in the Brownsville area, there would have been nearly 200 additional Cadillac sales in the McAllen and Weslaco areas in 2007.
51. There is a competitive marketplace for Cadillac motor vehicles in the Valley.
52. There is an available opportunity for additional Cadillac sales by the proposed franchise.
53. All Cadillac dealers in the Lower Rio Grande Valley have access to a large, but unquantifiable, base of consumers in nearby Mexico.
54. The demographics for households and population conducive to the purchase of luxury vehicles are projected to continue their substantial growth in the Lower Rio Grande Valley in the coming years.
55. High income households, which are more likely to purchase Cadillac vehicles, are more concentrated in the western portion of the market near the proposed Weslaco location than in the current Harlingen location.
56. The Luke Fruia Cadillac dealership in Brownsville accounted for 83.1% of Cadillac sales in the Brownsville APR in 2007.
57. Luke Fruia made 29 sales in the McAllen/Mission APR in 2007.
58. Luke Fruia and Bert Ogden Cadillac dealerships accounted for 65.7% of Cadillac sales in the Harlingen APR in 2007.
59. The Bert Ogden Cadillac dealership is a well-run dealership in an attractive facility with high levels of customer satisfaction and an above average sales performance.
60. Bert Ogden Cadillac accounted for 83.8% of Cadillac sales made in its APR in 2007.
61. One contributor to the above average sales performance of Bert Ogden Cadillac has been the weak Cadillac sales performance of Cardenas Autoplex.
62. Bert Ogden Cadillac's sales through November of 2006 were 460. In 2007, sales were 445 and through November of 2008, they were 371.
63. Bert Ogden's Cadillac dealer principal, Mr. Robert Vackar, is a capable and experienced dealer operator.

64. Bert Ogden Cadillac enjoys above GM-average profitability with competitive new car grosses.
65. Bert Ogden's Cadillac dealer location enjoys high traffic counts on Expressway 83, as well as advantageous expense and personnel sharing between its GM lines in Mission, Texas.
66. Bert Ogden Cadillac is a component of the largest "dealer group" in the Lower Rio Grande Valley and spends more money on advertising than any other dealer group in the Lower Rio Grande Valley.
67. A "dealer group" is an organization that owns and/or manages multiple dealerships.
68. Bert Ogden Cadillac is a profitable dealership and is not operating at an overall loss.
69. Bert Ogden Cadillac is positioned to successfully compete with Weslaco Motors Cadillac at its designated location.
70. Bert Ogden Cadillac will not be materially harmed by approval of the requested application.
71. In its initial application to GM, Applicant submitted a pro forma projecting sales of 480 Cadillac vehicles in the first year of operation.
72. GM has suggested that Applicant use a planning volume of 220 Cadillac vehicles.
73. Applicant projects sales of 300 Cadillac vehicles in the first year of operation.
74. If Applicant's application is approved, it is likely that there will be increased Cadillac sales in the mid-Valley market for the benefit of both the Cadillac brand and Cadillac dealers.
75. Approval of the application will result in increased Cadillac advertising and brand awareness in the Lower Rio Grande Valley, producing more opportunity for Cadillac sales.
76. Increasing Cadillac sales in the mid-Valley market will benefit the Cadillac brand and contribute to more adequate representation of the brand in the mid-Valley market.
77. From October 2007 to October 2008, total Cadillac sales in the United States decreased by 55%, from 21,267 to 9,541.
78. The overall economy of the United States and the financial soundness of the automobile manufacturers has decreased substantially in late 2007 and continues to date.
79. Domestic auto manufacturers, including GM, are downsizing product lines and dealerships to reflect decreased overall market share.

80. By 2012, GM intends to close nine plants and 1,750 dealerships.
81. Despite the current state of the economy, Applicant would like to have a GM franchise for the long-term prospects of profitability.
82. In 2007, Bert Ogden Cadillac sold 508 new cars, for an average of 42 per month.
83. In November of 2008, Bert Ogden sold 22 Cadillacs.
84. Approval of the application may result in decreased profitability to Bert Ogden, but it does not appear to be substantial harm over the long-term.
85. Operation of the application as proposed will promote the public interest.
86. On March 5, 2008, the MVD notified the parties that a hearing on the matter was referred to the State Office of Administrative Hearings. The notice contained a statement of the time, place, and nature of the hearing; a statement of the legal authority and jurisdiction under which the hearing was to be held; a reference to the particular sections of the statutes and rules involved; and a short, plain statement of the matters asserted.
87. The hearing on the merits was held on December 2-4, 2008. All parties appeared and participated in the hearing. The record was held open to allow for the preparation of the hearing transcript and to allow the parties to file post-hearing written closing arguments. The record closed on February 24, 2009.

IV. CONCLUSIONS OF LAW

1. The Texas Department of Transportation's Motor Vehicle Division has jurisdiction and authority over the subject matter of this case. TEX. OCC. CODE §§ 2301.652; 2301.701-713; and 43 TEX. ADMIN. CODE (TAC) §§ 8.105-8.107.
2. The State Office of Administrative Hearings has jurisdiction over all matters relating to the conduct of a hearing in this matter, including the preparation of a proposal for decision with findings of fact and conclusions of law. TEX. OCC. CODE § 2301.704; TEX. GOV'T CODE ch. 2003.
3. Notice of the protest and of the hearing on the merits was provided as required. TEX. OCC. CODE §§ 2301.652; Tex. Gov't Code 2001.051 and 2001.052; 43 TAC § 8.106.
4. Protestant is in substantial compliance with its franchise agreement.
5. The Cadillac brand is not adequately represented as to the service and sale in the existing Harlingen APR of Cardenas Autoplex.

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PROPOSAL FOR DECISION

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6. The establishment of a Cadillac dealership as proposed by Applicant will not result in substantial, long-term harm to Protestant.
7. The establishment of a Cadillac dealership as proposed in Weslaco, Texas, will promote a competitive marketplace.
8. The public interest will be best served by the establishment of a Cadillac dealership by Weslaco Motors in Weslaco, Texas.
9. Based upon the above Findings of Fact and Conclusions of Law, Applicant has demonstrated good cause to establish the proposed Cadillac dealership at 2401 E. Expressway 83, Weslaco, Hidalgo County, Texas.

SIGNED April 27, 2009.

SUZANNE FORMBY MARSHALL
ADMINISTRATIVE LAW JUDGE
STATE OFFICE OF ADMINISTRATIVE HEARINGS

APPENDIX

TAB 4

Atomik Enterprises Decision

TEXAS MOTOR VEHICLE COMMISSION

ATOMIK ENTERPRISES, KAWASAKI	X	
SALES,	X	
Applicant,	X	
	X	PROCEEDING NO. 85
SPORT CITY, INC.,	X	
Protestant.	X	

FINAL ORDER

BY THE COMMISSION:

The Texas Motor Vehicle Commission, having duly considered the Supplemental Hearing Report of the Hearing Examiner, including the revised findings of fact, conclusions and recommendations contained therein, and no exceptions thereto having been filed by the parties, does hereby enter its Final Order in this proceeding as follows:

IT IS ORDERED:

1. That the Supplemental Hearing Report filed in this proceeding, including the Hearing Examiner's opinion, revised findings of fact, conclusions and recommended action, be and they hereby are adopted by the Commission; and
2. That the application of Atomik Enterprises Kawasaki Sales, for a New Motor Vehicle Dealer's License for a Kawasaki motorcycle dealership at 9801 Montana Avenue, El Paso, Texas, be and it hereby is approved, and that the said license shall be issued to the Applicant upon the completion of the proposed facilities and the filing with the Commission of a copy of an executed franchise or dealer agreement with Kawasaki Motors Corporation; and

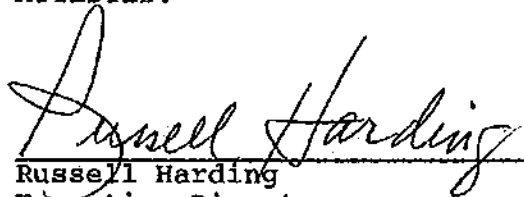
3. That the protest of the Protestant in opposition to the aforesaid application be and it hereby is denied.

Date: April 6, 1978



Erwin A. Elias, Chairman
Texas Motor Vehicle Commission

ATTESTED:



Russell Harding
Executive Director

TEXAS MOTOR VEHICLE COMMISSION

ATOMIK ENTERPRISES, KAWASAKI	X	
SALES,	X	
Applicant,	X	PROCEEDING NO. 85
	X	
SPORT CITY, INC.,	X	
Protestant.	X	

SUPPLEMENTAL HEARING REPORT

Pursuant to the Order of the Texas Motor Vehicle Commission dated October 27, 1977, granting Applicant's Motion For Rehearing and remanding the above-captioned proceeding for further hearing to receive such additional evidence as may have become available since the date of the original hearing in this matter held on February 2, 1977, and which may be material to the issues relating to the consideration of the subject application and the protest thereof, a hearing to receive such evidence was held before the Hearing Examiner on December 2, 1977, at the Commission's offices in Austin, Texas.

Testifying at the hearing as witnesses for the Applicant were Mr. Joseph J. Roseborough, a partner in the Applicant company; Mr. Paul Miller, Dealer Procurement Manager for Kawasaki Motors Corporation; and Dr. Kenneth W. Olm, professor at the University of Texas at Austin and a management consultant. The Applicant was represented at the hearing by its attorney, William R. Crocker of Austin, Texas.

Testifying as a witness for the Protestant was Mr. Harvey D. Lattner, President and Manager of the protesting dealership. The Protestant was represented at the hearing by its attorney, Byron H. Rubln of the law firm of Diamond & Rubln of El Paso, Texas.

OPINION OF HEARING EXAMINER

In the initial Hearing Report issued in this proceeding, it was the recommendation of the Hearing Examiner that the application be denied. The Hearing Examiner's recommendation was based upon his findings of fact and conclusions drawn therefrom, that the evidence in the record was not sufficient to establish that (1) the Kawasaki line was not being adequately represented in the El Paso metropolitan area; (2) there is an adequate market in the El Paso metropolitan area

to sustain two Kawasaki motorcycle dealerships on a profitable basis; and (3) good cause in the public interest for an additional Kawasaki dealer license exists (See Hearing Report, pp. 18-21).

As explained in the Hearing Report, it was the Hearing Examiner's opinion that the decline in Kawasaki market penetration in El Paso over a nine month period in 1976 was not sufficient to establish inadequate representation, considering other factors such as the Protestant's having consistently attained a market penetration higher than state and national levels over an extended period of time; the fluctuation of the total motorcycle market at the national, state and local levels; the speculation as to the future growth of the motorcycle market in El Paso and Kawasaki's ability to attain 20% of that market; and the uncertainty of the effect upon the motorcycle market of the El Paso economy (see Hearing Report, pp. 14-17). The conclusion of the Hearing Examiner that good cause in the public interest was not shown to exist at that time, was explained as being based upon the Hearing Examiner's findings of a probability of undue detriment to the existing dealer should the application be approved (See Hearing Report, pp. 17-18).

It is the contention of the Applicant and Kawasaki Motors Corp., that the additional evidence adduced at the rehearing establishes justification for the approval of the application. It is contended that the evidence shows that since the time of the original hearing: an additional dealership for a competing motorcycle line has been established in El Paso, leaving Kawasaki as the only one of the four major motorcycle manufacturers having only one sales outlet in the El Paso market area; Kawasaki sales have continued to decline in terms of market share and actual sales in El Paso, while the El Paso motorcycle market has shown tremendous growth; and the state of the El Paso economy is good and is growing, and there is ample market potential for two Kawasaki motorcycle dealers to operate profitably (Applicant's Closing Brief After Rehearing, p. 2).

It is the contention of the Protestant that no evidence was presented at the rehearing on December 2, 1977, which would materially affect the Hearing Examiner's original findings and recommendations in this proceeding. It is contended that the opening of a second Suzuki dealership in El Paso is not significant as Suzuki has been a minor factor in the El Paso motorcycle market. Moreover, Protestant contends that the two Honda dealerships and the two Yamaha dealerships are commonly owned and managed and that the El Paso market cannot support two separate and independently operated Kawasaki dealerships. The Protestant further contends that the registration and total market statistics for the El Paso area have not changed significantly since the original hearing and that the El Paso

economy remains mixed and has not recovered to a substantial degree (Protestant's Closing Brief After Rehearing, pp. 2, 4-9).

The evidence given at the rehearing can be summarized briefly as follows:

In support of the application, Mr. Joe Roseborough testified that since the date of the original hearing a new Suzuki dealership has been constructed and is ready to open for business. This dealership is located across the street from the Applicant's proposed location (Tr. 5-6). In addition, the Yamaha Northeast dealership is relocating further out on Dyer Street, which will be somewhat closer to Protestant's dealership (Tr. 8). The Applicant is still ready, willing and able to establish the proposed dealership, and the witness stated that the proposed area of El Paso where the dealership is to be located is expanding even faster than before (Tr. 11). In Mr. Roseborough's opinion, there has been no decline in the motorcycle market in El Paso and the potential for marketing Kawasaki motorcycles in the southeastern area of El Paso is greater than it was in February, 1977, because of the growth of that part of town. He still feels that there is an adequate market to sustain two Kawasaki dealerships profitably in El Paso (Tr. 12-14). He does not believe that his opening a dealership will result in the Protestant going out of business, because with two aggressive Kawasaki dealers, they will take business away from Yamaha (Tr. 14). Mr. Roseborough testified that Honda, Yamaha and Suzuki each have two dealerships in El Paso, while Kawasaki has but one dealership (Tr. 23-26).

Mr. Paul R. Miller, Dealer Procurement Manager for Kawasaki Motors Corporation, testified that at the initial hearing registration and market performance statistics were available through August, 1976 and that information for the period from September, 1976 through August, 1977 is now available. Referring to Applicant's Exhibit 19, containing Kawasaki's market penetration figures for El Paso County, state of Texas and national, Mr. Miller testified that Kawasaki's market penetration in El Paso exceeded the state market share in January, 1977 and the national market share in February, 1977, and these were the only two months from September, 1976 through August, 1977, in which the Kawasaki market share in El Paso exceeded either the state or national market penetration figures (Tr. 31-32). Through August, 1977, Kawasaki's market penetration in El Paso was 11.49% compared with 15.28% for the state of Texas and 17.13% nationally (Tr. 33). According to Mr. Miller, when Kawasaki had two dealerships in El Paso, their penetration exceeded that of the state and national levels and since the closing of the second store, their market share in El Paso has dropped below national and state levels while the market itself has grown (Tr. 35).

The total motorcycle market in El Paso in 1976 was 2,068 units, a 42.82% increase over 1975 sales of 1,448 units (Tr. 36). During the same period, Kawasaki's market share decreased 7.59% and actual sales decreased by 22 units (Tr. 37). As of August, 1977, the total market in El Paso has increased 13.15% over the prior year, while Kawasaki registrations have decreased by 24 units and its market share has decreased 3.25 percentage points, which represents a decrease of 11.76% (Tr. 38). Assuming a total market increase in El Paso of 13.15% for the entire year, this would result in a total market of 2,340 motorcycles, 20% of which would result in 468 units sold (Tr. 38-40). Mr. Miller stated that based upon total Kawasaki sales in El Paso of 268 units, an 11.76% decrease in 1977 would result in total sales of 236 units in El Paso for the year (Tr. 41).

Mr. Miller testified that Kawasaki believes there is an adequate market in El Paso to sustain two dealers profitably and they feel that El Paso is a market where they should do better than their national average. He stated that there is no reason why the opening of a second dealership will cause financial injury to the Protestant (Tr. 44). Mr. Miller testified that Honda and Yamaha are the competition they are after and without another dealership they do not believe they will ever achieve a competitive position in El Paso (Tr. 45). In Mr. Miller's opinion, Kawasaki is not adequately represented in the El Paso market because of the location of the existing dealer and because Honda, Yamaha and Suzuki have locations in the fastest growing part of El Paso and Kawasaki is not represented in that area (Tr. 45). In his opinion there is good cause in the public interest for an additional Kawasaki dealer in El Paso, as it will provide a more convenient facility to the people in an area where there is not now a Kawasaki facility and this will provide another convenient location for parts and service in that area so that customers there do not have to drive across town (Tr. 46-47).

Mr. Miller testified that the public always benefits from the introduction of competition in a market, from the additional exposure of a line not now represented and in the sense of providing competing models and prices against other lines. In his opinion, the introduction of another Kawasaki dealer will stimulate business in general in the market and will help both dealers. It has been Kawasaki's experience that the stimulation of business by a new dealer creating more product awareness, helps the existing dealers (Tr. 48-49). Mr. Miller stated that he knows of no reasons why the introduction of the Applicant's dealership into the El Paso market would injure the Protestant's business, and Kawasaki is convinced that there is an adequate market in El Paso for two Kawasaki dealers to exist profitably (Tr. 49). Kawasaki is not critical of the Protestant, but Kawasaki's position is

that the El Paso market simply cannot be served by a single dealer at the Protestant's location (Tr. 51).

On cross-examination, Mr. Miller acknowledged that for the period from September, 1976 through August, 1977, Kawasaki's market share decreased .7% in Texas and .43% nationally, as well as decreasing in El Paso from 13.3% to 11.79% (Tr. 57-58). There are areas in Texas where the Kawasaki market share is 20%, such as Midland-Odessa, Lubbock, San Angelo, Brownsville and Austin (Tr. 59). Because of their past history in El Paso when they achieved a 20% market share with two dealers, this indicates to them that with two aggressive dealers they can do as well as and better than Kawasaki does nationally (Tr. 64).

Dr. Kenneth Olm was called as a witness for the Applicant and testified regarding the state of the economy and general business conditions in El Paso since the first of the year, 1977 (Tr. 148-205). According to Dr. Olm, El Paso has continued to be one of the fastest growing areas of the state and its population is generally younger than the rest of the state (Tr. 148-149). Retail sales have recovered from a severe decline, and are good, but not as good as the rest of the state. Employment and income is up, other than in the apparel industry, and bank debits are up significantly (Tr. 149-151). In general, the economy is reasonably strong, but not as good as in the rest of the state (Tr. 151-152). In Dr. Olm's opinion, if Kawasaki is selling essentially the same product as Honda and Yamaha, then he feels they are not adequately represented in the total market and the problem can be rectified either by a second dealer or by the relocation of the existing dealer (Tr. 166-167).

On cross-examination, Dr. Olm testified that the economy in El Paso is better now than at the time of the previous hearing (Tr. 174). Reviewing the motorcycle registration statistics, he stated that there has been no dramatic change since the last hearing, except that the percentages are less favorable and the situation has deteriorated, but to a relatively slight degree (Tr. 179). According to Dr. Olm if Kawasaki was able to obtain 18% to 20% market penetration at one time, this indicates that they have the product that permits them to do it and if you can do it once and still have the same quality of product, then you can do it again, and the question then becomes one of marketing effort (Tr. 180). He feels that this is reason enough to allow Kawasaki to set up the marketing system that will enable them to achieve that goal (Tr. 181). Based upon all of the information since the prior hearing, the figures show some continuing deterioration, but not large. The general market and business climate in El Paso has improved and it appears that the motorcycle market had improved dramatically, but became less dramatic in September. If the improvement trend turns back up approach-

ing the June and July levels, then there is a significant difference (Tr. 186). If the trend continues downward, then he would say that the situation has not dramatically changed for the better (Tr. 186).

Dr. Olm stated that if the Kawasaki market penetration is declining, even by small margins, then looking down the road you have a situation which is untenable (Tr. 187) and if the penetration figures continue downward, then this is an important factor to take into consideration (Tr. 188). It appears to him that in general motorcycle sales are up and because of an increase in population he cannot see how you can help but predict that sales will continue to be up, and it appears that Kawasaki's penetration is trending downward (Tr. 189). In his opinion, if the present dealer maintained at or around the Kawasaki state average, this would indicate adequate representation, unless there is some reason for El Paso to be a better market. The Kawasaki market share is now approaching a point of inadequacy and if it continues it would definitely be inadequate (Tr. 189-191). Achieving 14% of a total market of 2,250 units would present a tight situation for two dealers, although he believes it is possible in 1978 for two dealers, properly designed, planned and managed, to sell 400 units, assuming a 17% market penetration (Tr. 193, 198). On redirect examination, Dr. Olm stated that based on the existing dealer being 24.8% under the state penetration level and 32.9% under the national penetration level, either the existing dealer is mislocated or the dynamics of the market are forcing two dealerships or multiple points (Tr. 200).

Mr. Harvey D. Lattner, President of the protesting dealership, testified in opposition to the application. Mr. Lattner testified that it was assumed at the previous hearing that the motorcycle market in El Paso would be 2,160 units and it was further assumed that the market would grow by 10% in 1977 meaning actual sales would be 2,376 units. However, actual registrations through September, 1977 are 1,754, an increase of 8.271% over the same period in 1976, and projecting the same increase for the entire year would result in total sales of 2,239 units, although Mr. Lattner doubts that sales will reach this figure (Tr. 73). Based on this estimate, Mr. Lattner stated that the projection of 2,376 total sales made at the previous hearing, would be an overestimate of 6.1% (Tr. 74). Referring to Protestant's Exhibit 11, Mr. Lattner stated that the increase in the motorcycle market through September, 1977 of 8.271% over September 1976, is less than the 10% increase projected by Kawasaki, and that while the figures did show a 30.36% increase as of June, 1977, this has declined to an 8.271% increase through September, 1977 due to motorcycle sales having dropped off sharply since June (Tr. 76). Referring to Protestant's Exhibit 12, Mr. Lattner testified that it would require the additional sale of 88.50 units for

the entire year for his dealership to achieve the state penetration figures, and he also stated that in the last three months his market share has increased in each month (Tr. 81-82).

Concerning the June market penetration figure of 8.27%, shown on Protestant's Exhibit 12, Mr. Lattner stated that this result was even after a big co-op advertising campaign with Kawasaki, which he believes was unsuccessful because he did not have the prices to compete (Tr. 84). Concerning Protestant's Exhibit 13, Mr. Lattner stated that since El Paso is in the Kawasaki Western Region, a more valid comparison would be with the Kawasaki Western Region which has only 13% of the market, whereas the rest of the state of Texas is in the North Central Region (Tr. 89-90). Referring to Protestant's Exhibits 9b and c, Mr. Lattner stated that there were 206 Kawasaki motorcycles sold through September, 1977, compared with 228 units sold through September, 1976, a decrease of 22 units or 9.64% (Tr. 91-92). In his opinion the El Paso market will continue the same downward trend which started in June and he feels his 1977 sales will be very close to equalling the 268 units sold in 1976 (Tr. 92-94). Mr. Lattner testified regarding Protestant's Exhibits 14 and 15, Kawasaki and Honda dealer price lists, to show that Kawasaki is at a price disadvantage competitively and which he believes explains the reason for the low market penetration in June of 8.27% (Tr. 95-100). During the advertising campaign, which featured the 400 c.c. unit, he sold about five of these motorcycles (Tr. 99).

It is Mr. Lattner's opinion that Kawasaki is being adequately represented in the market, considering the stiff pricing competition and he still feels that Kawasaki is slow in meeting the prices of its competition (Tr. 101-102). He stated that his prediction at the last hearing of a 6 or 7% increase in the market is the closest to what actually occurred and he feels the market will be about the same in 1977 as in 1976 (Tr. 102). While the first six months of 1977 looked good, the last six months have tapered off (Tr. 103) and it has not been due to a lack of effort that he had some bad months in 1977 (Tr. 103-105). In Mr. Lattner's opinion, there is no need in the public interest for a new Kawasaki motorcycle dealership in El Paso at this time as there has not been any great increase in the market to justify a new dealership, although another dealership might be justified in the future (Tr. 106). He believes he can adequately represent Kawasaki in El Paso with only one dealership (Tr. 106) and he does not feel that the present market in El Paso is such as to allow two full size Kawasaki dealerships separately operated to survive and prosper (Tr. 107).

On cross-examination, Mr. Lattner testified that his

dealership had a loss of \$7,800 for the fiscal year ending June 30, 1976 and a profit of \$7,780 for the fiscal year ending June 30, 1977 (Tr. 113). He does not think that he and the applicant together could get a 20% market share, because of Kawasaki's slow reaction in the market and because Kawasaki's market share at the state and national levels are also declining (Tr. 125). He stated that he needs to sell about 300 motorcycles a year to break even (Tr. 126) and he agrees that the establishment of another dealer would probably increase sales up to the state level of penetration of 15.5% (Tr. 128).

OPINION OF HEARING EXAMINER

Having carefully reviewed the evidence received at the re-hearing in this matter as well as that presented at the original hearing, it seems clear that some changes have occurred since the original hearing in this matter held in February, 1977. First, a second Suzuki motorcycle dealership has been established in El Paso and is located across the street from the Applicant's proposed dealership location. With the establishment of a second Suzuki dealership, the result is, as Applicant states, that Kawasaki is now the only one of the four major motorcycle manufacturers having but one retail sales outlet in the El Paso metropolitan area (Tr. 5-6, 23-26, 45). Second, the economy and general business climate in El Paso appear to have improved considerably. While some economic indicators are mixed, and while the economy may not be as strong as in the rest of the state, the evidence does indicate that the economy is nevertheless good and is improved over what it was at the time of the original hearing (Tr. 11, 12-14, 148-152, 174). Finally, the evidence does indicate that the motorcycle market in El Paso has continued to increase, although not at the rate projected at the initial hearing, and that Kawasaki's market penetration and actual sales have continued to decline (Tr. 31-33, 36-38, 57-58, 73-74, 76; App. Ex. 19, 20, & 21; Prot. Ex. 11).

The question before the Commission at this time concerns the significance of this additional evidence in light of the previous findings and recommendations, and whether this evidence is sufficient to change these findings and recommendations. It is necessary therefore, to evaluate the evidence received at the rehearing in light of the previous findings and recommendations and the evidence upon which they were based.

At the original hearing in this proceeding, Kawasaki's market share trend statistics for El Paso, State of Texas and National levels were available for the years 1973, 1974,

1975 and for the first nine months of 1976, excluding only Kawasaki's national penetration figures as of September, 1976 which was not then available (App. Ex. 3). These figures showed that Kawasaki's market penetration in El Paso in 1973, 1974 and 1975 was significantly in excess of its market penetration at the state and national levels, but began to decline upon the closing of the second Kawasaki dealership at the beginning of 1976, and for the first time fell below the national average in April, 1976 and below the state average in July, 1976 (App. Ex. 3). Applicant's Exhibit 19, introduced at the rehearing, is a continuation of Kawasaki's market share trend statistics commencing with September, 1976 and continuing through August, 1977 (or an additional 12 months' information) and shows a continuing decline from the Kawasaki market penetration in El Paso of 14.07% in September, 1976 to 11.49% through August, 1977. Kawasaki's market penetration for the state of Texas and at the national level remained relatively constant during the same period, declining from 15.85% to 15.28% at the state level and declining from 17.70% to 17.13% at the national level (App. Ex. 19).

Considering the foregoing market share information in total, what is presented is a showing of strong market penetration by Kawasaki in El Paso in the years 1973, 1974 and 1975, with a sharp decline commencing in February, 1976 and continuing through August, 1977 (App. Ex. 3, 19). While Protestant is undoubtedly correct that Kawasaki's penetration at the state and national levels have also declined, such decline has been slight compared with the decline in El Paso. It is the Hearing Examiner's opinion that the foregoing evidence is of significance in considering the subject application. The Hearing Examiner's conclusion in the original Hearing Report was not based upon an affirmative finding that the Protestant was adequately representing Kawasaki in the El Paso market, but rather was based upon the Hearing Examiner's opinion that the evidence of a market share decline over a period of nine months in 1976, when considered together with other factors, was not sufficient to establish that Kawasaki was not being adequately represented in the El Paso metropolitan area. The evidence presented at the rehearing constitutes an additional 11 or 12 month period for analysis and reflects a continued decline in Kawasaki's market penetration in El Paso. While the Protestant is correct the market penetration has deteriorated to a relatively slight degree since the previous hearing from 14.07% in September, 1976 to 11.79% in September, 1977, the significant thing in the Hearing Examiner's opinion is the fact of continued deterioration of this market penetration. And, as Applicant's expert witness testified, while the deterioration has been relatively slight, a continued situation of market share decline becomes untenable (Tr. 187). The Hearing Examiner does not believe that a manufacturer or distributor should

be required to wait until its market position has become totally eroded before taking necessary measures to protect its position, including the establishment of new dealerships. It is the Examiner's opinion, therefore, that the additional evidence presented at the rehearing does establish a deteriorating market penetration in El Paso over a sufficient period of time as to constitute a showing of inadequate representation.

In addition to the foregoing, it is the Hearing Examiner's opinion that the establishment of a second Suzuki dealership in El Paso, leaving Kawasaki as the only one of the four major motorcycle manufacturers with a single sales outlet, is another significant development which has occurred since the previous hearing and which must be considered in an analysis of adequacy of representation. For a manufacturer to have but one sales outlet in a major market area while its competitors have two sales outlets places the manufacturer at an obvious competitive disadvantage.

As indicated in the initial Hearing Report, other factors had a bearing on the Hearing Examiner's conclusion and these factors must also be reconsidered at this time. One of these factors concerned the state of the El Paso economy and additional evidence on the state of the economy was presented at the rehearing. A fair summary of the testimony of Applicant's expert witness, Dr. Olm, is that El Paso continues to be one of the fastest growing areas of the state, and that while some economic indicators are mixed, the economy and general business conditions in El Paso are reasonably strong, but not as good as the rest of the state, and is better now than at the time of the previous hearing (Tr. 148-152, 174). It is the Examiner's opinion that the additional evidence received at the rehearing is sufficient to remove the question of the state of the El Paso economy as a factor in this proceeding.

The most troublesome question in the initial Hearing Report concerned the adequacy of the motorcycle market in El Paso to sustain two Kawasaki motorcycle dealers. This continues to be a troublesome question and obviously one which cannot be answered with any real certainty from the evidence in this record. The total motorcycle market in El Paso is not particularly large, but it has shown considerable growth and increased from 1,448 units in 1975 to 2,068 units in 1976. Through August of 1977, the total market has shown an increase of 13.15% over that of August, 1976 (Tr. 36-37; App. Ex. 20, 21). Kawasaki points out that during this period of substantial growth in 1976 over 1975, only Kawasaki of all the major motorcycle lines showed a decrease in market share as well as total units sold (Tr. 37; App. Ex. 21). Protestant's evidence shows that the motorcycle market in El Paso in 1976 failed to

increase to the extent predicted by Kawasaki at the initial hearing, and that while the first six months of 1977 showed a dramatic growth of over 30% over the same period in 1976, the market increase as of September, 1976 was only 8.271% over the same period in 1976, less than the 10% increase predicted by Kawasaki (Tr. 73; Prot. Ex. 9). Protestant did, however, show a profit for his fiscal year ending June 30, 1977, of \$7,780 (Tr. 113).

Looking solely at the motorcycle market figures for El Paso, it would be difficult to conclude that there is an adequate market in El Paso. However, these figures cannot be isolated and must be considered together with the other evidence to obtain a complete picture of the situation in El Paso. For instance, there is no question but that Honda and Yamaha are finding a growing market in El Paso. Applicant's Exhibit 21 shows that Honda's sales increased over 50% in 1976 over 1975 and Yamaha's sales increased over 53% in 1976 over 1975. During the same period Suzuki's sales increased 114%, while Kawasaki's sales decreased by 7.59%. As of September, 1977, Honda's sales were 624 units compared to 484 through September, 1976, and Yamaha's sales were 727 units compared to 612 through September, 1976. Suzuki's sales showed a decline during this same period from 89 units sold through September, 1977, compared to 128 sales through September, 1976. Kawasaki's sales also showed a decline from 228 units through September, 1976 compared with 208 units through September, 1977 (Prot. Ex. 9). Apparently in response to its decline in sales, Suzuki has established a second retail outlet. In view of the continued dramatic growth evidenced by Honda and Yamaha, it is difficult to accept the proposition that Kawasaki must be forever relegated to a market performance below that which it attained for a long period of time and also below its state and national performance levels. This is particularly true in light of the testimony showing that El Paso is one of the fastest growing areas of the state, with a generally younger population. Moreover, the Commission cannot ignore the fact that the establishment of a second Kawasaki dealership is bound to generate additional sales, and it is a possibility that the establishment of a second dealership will be beneficial to the Protestant rather than detrimental.

Applicant's witness Dr. Olm stated that if Kawasaki was at one time able to attain a 20% market share, this indicates that they have a product which enables them to do so and thus they should be able to do so again with proper marketing effort. Protestant maintains that the primary cause for the low market penetration attained in El Paso is Kawasaki's slowness in responding to its competition in terms of competitive pricing (Tr. 84, 95-100). This may indeed be a factor affecting Protestant's performance and this was recognized

by the Examiner in the initial Hearing Report as being one of the unknown factors to be considered in evaluating the issue of adequacy of performance. However, the Hearing Examiner does not believe that the evidence in the record on this particular point is sufficient to explain the decline in Kawasaki's performance in El Paso. Accordingly, it is the Hearing Examiner's opinion that the evidence received at the rehearing is of sufficient significance to require a finding at this time that the Kawasaki line is not being adequately represented in the El Paso metropolitan area.

With respect to the Hearing Examiner's conclusion in the initial Hearing Report that good cause in the public interest was not shown to exist at that time, such conclusion was based upon the Examiner's finding of a probability of undue detriment to the existing dealer. The bases for this finding were the questions which existed regarding the adequacy of the El Paso market to sustain two dealers, together with the Protestant's testimony that he had not earned a profit since 1974 and that a second dealer would bankrupt him. In view of the Hearing Examiner's analysis of the El Paso market and its growth, plus the showing that Protestant has been able to operate profitably, the Examiner does not believe that a conclusion such as was reached in the initial Hearing Report can be maintained at this time. As indicated in the initial Hearing Report, the Commission has recognized that the availability of a convenient sales and service facility to a large number of residents of a particular segment of a community or metropolitan area may very well constitute good cause in the public interest for an additional dealership. Such is the case in this instance, and the Examiner does not believe that an overriding showing of undue detriment can be sustained at this time.

In summary, the Hearing Examiner's analysis of this matter is that considering the evidence received at the rehearing, together with the evidence presented at the initial hearing, the record considered in its entirety at this time compels a reversal of certain of the Hearing Examiner's prior findings and conclusions and the substitution therefor of appropriate findings and conclusions in support of a recommendation that the subject application be approved. The record in this proceeding, considered as a whole, indicates that the decline in the Kawasaki market penetration which began in January, 1976 has continued through September, 1977; that from September, 1976 through August, 1977, except for the months of January and February, 1977, Kawasaki's market penetration in El Paso was below that of its market penetration at the state and national levels; that the total motorcycle market in El Paso has continued to grow; that the economy and general business climate in El Paso have improved and can be considered as being reasonably strong; that the establishment of a second

Suzuki dealership in El Paso leaves Kawasaki as the only major motorcycle line with but one sales outlet; that Honda and Yamaha have continued to increase their sales in El Paso at a dramatic rate; that while the potential of the El Paso motorcycle market is not capable of being ascertained with any certainty and while the potential effect upon the Protestant's business of the establishment of a second Kawasaki dealership is also speculative, the evidence in the record is not sufficient to justify a denial of the application.

The consideration by the Commission of a protest of a license application is an extremely serious matter, and the Commission cannot lightly deny any license application. The implications of proceedings of this nature are obvious, and the Hearing Examiner believes that once a prima facie case has been made by an applicant, an application for license should not be denied except upon a very clear showing that the consequences likely to result from the granting of the application will be more detrimental than beneficial, considering the interests of the parties involved and that of the public. In this instance, the evidence received at the rehearing, when considered together with the evidence presented at the initial hearing, is sufficient to constitute a prima facie case for the granting of the application, and it is the Hearing Examiner's opinion that no clear showing of undue harm or detriment has been made in this case. Certainly some very serious and legitimate questions have been raised by the Protestant. Nevertheless, the Hearing Examiner believes that more is required to justify the denial of a license than the evidence offered in this instance, in view of the nature of this type of proceeding, the result of which may be the exclusion of a potential competitor from the market. It is the Examiner's opinion that the evidence in the record in opposition to the application, in view of the additional evidence received at the rehearing, does not provide adequate grounds for the denial of this application.

FINDINGS OF FACT

1. The record in this case, including the evidence received at the rehearing, requires no change in Findings of Fact No. 1 through 4, 6, 8 through 14, 16, and 20, as contained in the initial Hearing Report, and such Findings are hereby reaffirmed and incorporated herein without modification.
2. Finding of Fact No. 5, as contained in the initial Hearing Report is deleted and the following is substituted therefor:
 - "5. Honda, Yamaha and Suzuki each have two dealers in El Paso, while Kawasaki and Harley-

Davidson each have one dealership (Tr. 44-45; App. Ex. 2; Rehearing Transcript 5-6, 8, 23-26, 45). The two Honda dealerships are owned by the same person or group of persons, and the two Yamaha dealerships also have common ownership (Tr. 54)."

3. Finding of Fact No. 7, as contained in the initial Hearing Report is deleted and the following is substituted therefor:

"7. The Protestant's business was not profitable during the period from 1974 through the end of its fiscal year ending June 30, 1976. Protestant's business did earn a profit of \$7,780 for its fiscal year ending June 30, 1977 (Tr. 289; App. Ex. 15; Rehearing Transcript 113)."

4. Finding of Fact No. 15, as contained in the initial Hearing Report is deleted and the following is substituted therefor:

"15. The motorcycle industry as a whole sustained a decrease in sales in 1974 from its performance in 1973, and sales further declined in 1975 from 1974 levels. The motorcycle market in El Paso decreased in both 1974 and 1975, and at the state level Kawasaki's market share decreased approximately 15% from August, 1975 to September, 1976, and sustained a further decline in the last three months of 1976. However, the total motorcycle market in El Paso in 1976 was 2,068 units, a 42.82% increase over 1975 sales of 1,448 units, while during the same period, Kawasaki's percentage of market share in El Paso decreased 7.59% and actual sales decreased by 22 units. As of August, 1977, the total market in El Paso has increased 13.15% over the prior year, while Kawasaki registrations have decreased by 24 units and its market share has decreased 3.25 percentage points, representing a decrease of 11.76% (Tr. 53-54, 72, 229-230, 235-236; Rehearing Transcript 36-38; App. Ex. 19, 20 & 21)."

5. Findings of Fact 17, 18, 19 and 21, as contained in the initial Hearing Report are deleted, and the following are substituted therefor:

"17. The Kawasaki share of the market in El Paso County through December, 1976 was 12.96%, while the Kawasaki share of the

market for the state of Texas was 15.76% and 17.11% for the nation (App. Ex. 19)."

"18. The Kawasaki share of the market in El Paso County through August, 1977 was 11.49%, while the Kawasaki share of the market for the state of Texas was 15.28% and 17.13% for the nation (App. Ex. 19)."

"19. In 1976, all major motorcycle lines, except Kawasaki, recorded significant sales increases over 1975 levels, with Honda having an increase of over 50%, Yamaha having an increase of over 53% and Suzuki having an increase of 114%. Through September, 1977, Honda's sales had increased to 624 units compared to 484 through September, 1976, and Yamaha's sales were 727 units compared to 612 through September, 1976. Kawasaki's sales and Suzuki's sales did show declines during this same period (App. Ex. 20, 21; Prot. Ex. 9)."

Note: Finding of Fact No. 20, as contained in the initial Hearing Report remains unchanged.

"21. The justification offered for the application, in addition to the claim of inadequate representation, is Kawasaki's projected increase in the total motorcycle market and the attaining of a market share in El Paso of about 20%, both of which projections are somewhat speculative, although there is no doubt that the establishment of a second Kawasaki dealership will result in increased sales and market share (Tr. 60-61, 70, 92-93, 94-95; Rehearing Transcript 38-40, 44, 48-49, 128).

"22. The decline in the Kawasaki market share in El Paso County may have been affected in part by various factors beyond the control of the existing dealer, such as a depressed economy in El Paso, an extremely high rate of unemployment, and the slowness of Kawasaki in reacting to meet competition from other brands. However, El Paso continues to be one of the fastest growing areas of the state and the economy and general business climate in El Paso have improved considerably and

can be considered as being reasonably strong (Tr. 251, 284, 286-287; Rehearing Transcript 12-14, 84, 101-102, 148-152, 174; App. Ex. 15; Prot. Ex. 14, 15).

"23. The disproportionately high market share obtained by the Yamaha dealers in El Paso has been primarily at the expense of Honda and Suzuki, but the continued decline of Kawasaki sales and market share is evidence that some of that high market share is also at the expense of Kawasaki (App. Ex. 19, 20, 21; Prot. Ex. 2)."

"24. The evidence in the record is conflicting and the record is inconclusive as to the effect of the granting of the application upon the Protestant's business (Tr. 37, 104, 120-121, 245, 264; Rehearing Transcript 12-14, 44-45, 48-49, 106, 107, 113; App. Ex. 15)."

CONCLUSIONS

Based upon the Findings of Fact in this matter, as modified following the taking of additional evidence at the rehearing, no change is required in Conclusions No. 1 and 2, as contained in the initial Hearing Report and such Conclusions are hereby reaffirmed and incorporated herein without modification. Conclusions No. 3, 4 and 5 are deleted, and the following substituted therefor:

"3. The Kawasaki line is not being adequately represented in the El Paso metropolitan area."

"4. Good cause in the public interest for an additional Kawasaki motorcycle dealer license at the proposed location in El Paso, Texas, has been shown to exist."

RECOMMENDED ACTION

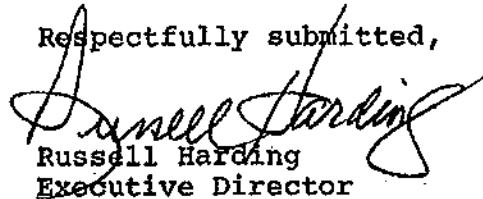
It is the recommendation of the Hearing Examiner, based upon the revised Findings of Fact and Conclusions as set forth above, that the Texas Motor Vehicle Commission enter an order in this proceeding as follows:

1. That the application of Atomik Enterprises Kawasaki Sales, for a New Motor Vehicle Dealer's License for a Kawasaki motorcycle dealership at 9801 Montana Avenue, El Paso, Texas, be approved, and that the said license be issued to the Applicant upon the completion of the proposed facilities and the filing with the Commission of a copy of an executed franchise or dealer agreement with Kawasaki Motors Corporation; and

2. That the protest of the Protestant in opposition to the aforesaid application be denied.

Date: January 30, 1978

Respectfully submitted,



Russell Harding
Executive Director

TEXAS MOTOR VEHICLE COMMISSION

ATOMIK ENTERPRISES, KAWASAKI	X	
SALES,	X	
Applicant,	X	
	X	PROCEEDING NO. 85
SPORT CITY, INC.,	X	
Protestant.	X	

ORDER GRANTING APPLICANT'S
MOTION FOR REHEARING

BY THE COMMISSION:

On this the 27th day of October, 1977, there came to be heard before the Texas Motor Vehicle Commission the Motion For Rehearing filed by the Applicant in the above-captioned proceeding; and the Commission having duly considered the Applicant's said motion and having duly considered the response thereto filed by the Protestant; and it appearing to the Commission that there may now exist additional facts and evidence not available at the hearing in this matter held on February 2, 1977, which may materially affect the findings, conclusions and recommendations of the Hearing Examiner and the decision of the Commission in adopting such findings, conclusions and recommendations; and it further appearing to the Commission that such additional facts and evidence should be considered by the Commission prior to the entry of a final order in this proceeding; and good cause for the granting of the Applicant's Motion For Rehearing having been shown;

NOW, THEREFORE, IT IS ORDERED by the Texas Motor Vehicle Commission that:

1. Applicant's Motion For Rehearing be, and it hereby is granted; and
2. The Final Order of the Commission entered on September 15, 1977 be and it hereby is set aside; and
3. The Hearing Examiner is hereby directed to convene a hearing in this matter at the earliest date convenient to the parties for the purpose of receiving such additional evidence which has become available since the date of the original hearing held on February 2, 1977, and the Hearing Examiner is directed to prepare and submit to the Commission a supplemental hearing report containing the Hearing Examiner's findings, conclusions and recommendations taking into consideration the original record in this proceeding and any additional evidence received at the additional hearing hereby ordered by the Commission.

Date: October 27, 1977



Erwin A. Elias, Chairman
Texas Motor Vehicle Commission

ATTESTED:



Russell Harding
Executive Director

TEXAS MOTOR VEHICLE COMMISSION

ATOMIK ENTERPRISES, KAWASAKI	X	
SALES,	X	
Applicant,	X	PROCEEDING NO. 85
	X	
SPORT CITY, INC.,	X	
Protestant.	X	

FINAL ORDER

BY THE COMMISSION:

The Texas Motor Vehicle Commission, having duly considered the Hearing Report of the Hearing Examiner, including the findings of fact, conclusions and recommended action contained therein and the exceptions thereto filed by the Applicant; and having heard and considered oral arguments by counsel for the parties; and having considered Applicant's Motion For Leave To Present Additional Evidence in this matter, does hereby enter its Final Order in this proceeding as follows:

IT IS ORDERED:

1. That Applicant's Motion For Leave to Present Additional Evidence, be and it hereby is denied;
2. That the Hearing Report filed in this proceeding, including the Hearing Examiner's opinion, findings of fact, conclusions and recommended action, be and they hereby are adopted by the Commission; and
3. That the application of Atomik Enterprises Kawasaki Sales, for a New Motor Vehicle Dealer's License at 9801 Montana Avenue, El Paso, Texas, be and it hereby is denied.

Date: September 15, 1977



John N. Cleveland, Vice Chairman
Texas Motor Vehicle Commission

ATTESTED:



Russell Harding
Executive Director

TEXAS MOTOR VEHICLE COMMISSION

ATOMIK ENTERPRISES, KAWASAKI	X	
SALES,	X	
Applicant,	X	PROCEEDING NO. 85
	X	
SPORT CITY, INC.,	X	
Protestant.	X	

HEARING REPORT

This matter is before the Texas Motor Vehicle Commission as a result of a protest filed with the Commission by Sport City, Inc. ("Protestant") in opposition to the application made by Atomik Enterprises, Kawasaki Sales ("Applicant") for a New Motor Vehicle Dealer's License for a proposed dealership at 9801 Montana Avenue, El Paso, Texas, to sell the Kawasaki line of new motor vehicles.

The said protest was filed pursuant to the Commission's Rule 067.02.00.004 which provides that upon receipt of an application for a New Motor Vehicle Dealer's License, the Commission shall give notice of the filing of such application to all licensees holding franchises for the sale of the same line of new motor vehicles in the same trade area and that any such affected licensee may protest the granting of such license, whereupon the Commission shall hold a public hearing to consider the matters set forth in Section 4.06(c) of the Texas Motor Vehicle Commission Code.

An application for a license to establish a new dealership in El Paso, Texas, to sell the Kawasaki line of motor vehicles was filed by the Applicant on October 21, 1976, and a notice of protest in opposition to the application was timely filed with the Commission by the Protestant. A pre-hearing conference in this matter was held in the Commission's offices in Austin, Texas, on December 13, 1976, and a public hearing for the taking of evidence was held in the Commission's offices pursuant to proper notice to all parties, on February 2, 1977. The hearing was held before Russell Harding, Executive Director of the Commission, who acted in the capacity of Hearing Examiner.

The Applicant was represented at the hearing by its attorney, William R. Crocker of Austin, Texas. Testifying at the hearing as witnesses for the Applicant were Joseph J. Roseborough and Michael J. Roseborough, partners in

the applicant company; Paul R. Miller, Dealer Procurement Manager for Kawasaki Motors Corporation; Dr. Kenneth W. Olm, professor at the University of Texas at Austin and management consultant; and Mr. Hiroshi Noda, Market Development Manager for Kawasaki Motors Corporation.

Protestant was represented at the hearing by its attorney, Byron H. Rubin of the law firm of Diamond & Rubin of El Paso, Texas. Testifying at the hearing as a witness for the Protestant was Harvey D. Lattner, President and manager of the protesting dealership.

The transcript of testimony given in this proceeding comprises 316 pages, and the record also includes various exhibits introduced by the parties. Copies of the transcript of testimony and of all exhibits received in evidence, except those listed below*, and copies of the briefs filed by counsel for the parties, have been provided to all members of the Texas Motor Vehicle Commission for their review and reference in considering the Hearing Report and the findings, conclusions and recommendations of the Hearing Examiner. This Hearing Report, and the findings of fact, conclusions and recommended decision and order contained therein, are based solely upon the record in this case which is comprised of the application for license filed by the Applicant, the testimony of the witnesses and other evidence received at the hearing, and the briefs of counsel for the parties.

ISSUES

The ultimate question to be decided in this proceeding is whether the application made by the Applicant for a New Motor Vehicle Dealer's License for a proposed dealership in El Paso, Texas, to sell the Kawasaki line of motorcycles should be granted or denied. In order to answer this question, an evaluation of the evidence in the record of this proceeding must be made in light of the statutory provision on which this protest is based and which sets forth the specific grounds upon which the Commission may deny such application. Section 4.06(c) of the Texas Motor Vehicle Commission Code, which governs this proceeding, provides that the Commission may deny an application for a new dealership in a community

* The following exhibits, due to size or bulk, were not distributed to the members of the Commission, but are available for examination and review at the Commission's offices: Applicant's Exhibit 1 - Applicant's license application; Applicant's Exhibit 2 - map of El Paso; and Applicant's Exhibit 15 - deposition of Harvey Lattner.

or metropolitan area where:

- (1) the same line-make of new motor vehicle is then represented by a dealer who is in compliance with his franchise agreement with the manufacturer or distributor; and
- (2) the existing dealer is adequately representing the manufacturer or distributor in that community or metropolitan area in the sale and service of its new motor vehicles; and
- (3) no good cause is shown for an additional dealer license in the public interest.

In the instant case, the Kawasaki line is represented in the El Paso metropolitan area by the Protestant and it was stipulated by the parties that the protesting dealer is in compliance with its franchise agreement. Accordingly, the sole issues with which we are concerned in this case are those referred to in (2) and (3) above.

Evidence in Support of Application

Mr. Joseph J. Roseborrough, a partner in the applicant company testified in support of the application (Tr. 6-29; 39-40). Mr. Roseborrough testified that upon completing his career in the U.S. Army he first entered the real estate business in El Paso and then operated a mobile-home park both of which were successful business operations. He has had a long time interest in motorcycles personally and through the racing interests of his sons. His investigation of the El Paso area showed Honda and Yamaha to be well represented while Kawasaki had only one dealer. He felt that a more aggressive, well-operated shop would be a profitable venture and he contacted Kawasaki concerning a proposed dealership (Tr. 11-12). Mr. Roseborrough testified regarding the proposed dealership facility, which will be a cinder block building of 4,000 square feet for sales, service, parts and office areas (Tr. 14). He also testified concerning the capitalization of the dealership, the proposed inventories of motorcycles and parts and accessories, and concerning the dealership personnel. Mr. Roseborrough and his older son will be partners in the business and the dealership will be a family operated business with additional personnel to be employed as needed (Tr. 15-16, 39-40).

Mr. Roseborrough stated that he selected the Kawasaki line because it is one of the top three motorcycles in the United States, and Honda and Yamaha appeared to have adequate

coverage of the market. He selected the southeast area of El Paso due to its location which is close to the geographical center of El Paso and it is also the growth area of the city. He does not believe that residents of this area have convenient access to a Kawasaki sales and service facility (Tr. 16-19). It is his opinion that Kawasaki was not being adequately represented in the El Paso market and that there is good cause in the public interest for the additional dealer license (Tr. 19-21). Mr. Roseborough is familiar with the El Paso economy and business community and it is his feeling that business there is flourishing and that the devaluation of the Mexico peso will not have a significant effect on the motorcycle market (Tr. 21-23).

On cross-examination, Mr. Roseborough testified that the distance between the existing dealership and the proposed dealership location was approximately 10 miles and the driving time between the two locations was from 10 to 14 minutes (Tr. 26). It is his belief that the southeastern part of El Paso will be the primary area where most of the sales for the new dealership will come from (Tr. 26-27). His contention that the El Paso market can sustain two Kawasaki dealerships is based upon the growth of the southeastern area (Tr. 28) and because the existing dealer is just too far from the southeastern area (Tr. 28).

Mr. Michael J. Roseborough, who is a partner with his father in the proposed dealership also testified in support of the application (Tr. 30-38). Mr. Roseborough is currently employed by IBM in Lexington, Kentucky. He has bachelors degrees in mathematics and mechanical engineering from the University of Texas at El Paso and a masters degree in mechanical engineering from the University of Texas at Austin. It is his intention to move back to El Paso and manage the motorcycle dealership with his father and to obtain his PhD from UTEP. He started riding motorcycles at age 13, he has continued his interest in motorcycles and has been racing professionally for the past six years (Tr. 30-32). He grew up in El Paso, visits there frequently and is familiar with the area. It is his opinion that the residents of the southeastern area do not have convenient access to Kawasaki sales or service facilities and he believes there is good cause in the public interest for the proposed dealership (Tr. 33-34). On cross-examination, Mr. Roseborough testified that motorcycle buyers are predominantly convenience buyers and that since Honda and Yamaha are represented in the southeastern area and since Kawasaki does not have a dealer in the area, he believes Kawasaki is not adequately represented in the area (Tr. 37).

Mr. Paul Miller, Dealer Placement Manager for Kawasaki Motors Corporation testified in support of the application

(Tr. 41-96; 131-163). Mr. Miller's primary responsibility is to solicit and establish new dealerships in areas designated by Kawasaki as open points. The considerations involved in establishing a new dealer in a particular area include a review of the existing dealer network in the area, the base motorcycle industry sales in the area and Kawasaki's market share of those sales (Tr. 42). Referring to Applicant's Exhibit #2, a map of the city of El Paso and vicinity, Mr. Miller testified that Honda and Yamaha each have two dealers in El Paso, while Suzuki, Kawasaki and Harley-Davidson each have one dealership, and that these five brands represent the largest portion of the motorcycle industry (Tr. 44-45). Mr. Miller has measured the distance between the existing dealer and the proposed dealership and found it to be right at 10 miles, with a driving time of about 17 minutes (Tr. 45-46). Mr. Miller testified that it is his opinion that Kawasaki is not represented well in the entire El Paso area and that there are existing Kawasaki owners and potential Kawasaki buyers in the southeastern area who do not have convenient access to sales or service facilities for Kawasaki motorcycles (Tr. 46-47). It is his opinion that there is good cause in the public interest for the additional dealer license (Tr. 48). He also testified that Kawasaki is in an excellent inventory situation and that there are no motorcycles in the line that are not readily available to any dealership (Tr. 48). Kawasaki has a manufacturing and assembly plant in Lincoln, Nebraska which is operating at about one-sixth of capacity (Tr. 48-49).

On cross-examination, Mr. Miller stated that it is Kawasaki's contention that the proposed new dealership will draw most of its customers from the southeast area immediately surrounding the proposed location and that this area can sustain a Kawasaki dealership (Tr. 50). Based upon motorcycle sales in El Paso in the first 9 months of 1976, which were 1,620 units, he agreed with an estimated figure of 2,160 units for the entire year (Tr. 52-53). Motorcycle sales in El Paso in 1973 totaled between 2,100-2,200 units which was the peak year in El Paso, and sales did decrease in 1974 and 1975. In 1976, sales are about the same as 1973 figures (Tr. 53-54). The two Honda dealerships in El Paso are owned by the same person or persons, and the two Yamaha dealerships are also owned by the same persons, and Kawasaki will be the only one of the three major brands with two separately owned dealerships (Tr. 54). Mr. Miller's contention that one dealership cannot adequately represent Kawasaki in El Paso, is based upon R. L. Polk registration figures showing a steady decline in Kawasaki's registrations in El Paso and the growth of the southeastern area (Tr. 55).

Concerning Protestant's Exhibit #1, Mr. Miller testified that in 1973, 1974, 1975 and through June, 1976, Kawasaki's

percentage of the market was greater in El Paso County than Kawasaki's percentage of the market in Texas, and the period from June 30, 1976 through September 30, 1976, is the only period that the Kawasaki market share in El Paso has been below that of the state, the difference being approximately 1.85% (Tr. 57-59). Kawasaki's decision to establish another dealer in El Paso is not based solely on the 1.85% difference, but goes back to December 31, 1975 when Kawasaki had 20.03% of the market which has continued to decline (Tr. 60). Kawasaki believes that its market penetration in El Paso should be 25% of the market by the end of 1977 (Tr. 60-61). In 1973, with one Kawasaki dealership, there were 379 Kawasaki motorcycles registered in El Paso representing a market share of 16.63% (Tr. 63). They feel that the proposed dealership can sell between 200-250 motorcycles in its first year (Tr. 63-64), and that the existing dealer would maintain his 1976 sales level and hopefully grow from that (Tr. 64). This feeling is based upon the disproportionate share of the market in El Paso held by the Yamaha dealer which is 37.77% while the Yamaha market share for the entire state through September, 1976, is only 22.67% (Tr. 64, 66; Protestant's Exhibit #2). Mr. Miller does not believe that the increased Yamaha sales are coming at the expense of Honda and Suzuki, even though Honda and Suzuki are doing more poorly in El Paso than Kawasaki in comparison to their statewide performances (Tr. 67, 68).

It is Kawasaki's contention that a market of 2,160 units, with a projected growth by Kawasaki of 10% of the market, would mean an increase in the market in El Paso to 2,376 units in 1977, which would be sufficient to sustain two Kawasaki dealerships (Tr. 70). The industry declined in 1974 and 1975, and in El Paso the decline was in line with the national decline (Tr. 72). Kawasaki has never had 25% of the market in El Paso, but using the 20% figure which was the highest market penetration achieved by Kawasaki when there were two dealerships, the result would be 475 total sales, assuming a total market of 2,376 units in 1977 (Tr. 73-74). But if Kawasaki were only to maintain its statewide market penetration of 16% in El Paso, this would result in total sales of 380 units and if the existing dealer sold 60% of the total, this would result in 228 units sold (Tr. 75-76). Kawasaki would not be satisfied to achieve its statewide market share in El Paso because they feel this market should exceed the statewide percentage, and this feeling is based upon Yamaha's disproportionate share of the market (Tr. 77). Kawasaki expects to do worse than its state average in some areas and better in others, but they look at El Paso as an opportunity to achieve a higher percentage than its statewide percentage (Tr. 77-78). Mr. Miller believes that a realistic market share that Kawasaki would maintain with a second dealer in El Paso for the entire year of 1977 would be between 20% and 25% and after the first full year of operation of the

second dealership they could attain 25% of the market (Tr. 79). Mr. Miller agreed that if Kawasaki does not attain the projected 20% of the market, and maintains only 16%, the result would be detrimental to the existing dealer, and if they thought that this would occur they would not even propose a second dealer (Tr. 92-93). While Kawasaki's market share in Texas has decreased in 1976, they expect to increase their market share in 1977 through an increase in dealerships and an increase in the total motorcycle market (Tr. 94-95). Concerning the availability of product, Mr. Miller stated a limited number of 1975 and 1976 models are still on hand, as well as the new 1977 models (Tr. 133).

On redirect examination, Mr. Miller stated that 1973 was a "high water mark" year for motorcycle sales and when the oil embargo and gas shortage came about, motorcycle sales took a dramatic leap in the last few months of 1973 and the first four or five months of 1974 and they do not foresee this type of situation happening again (Tr. 134-135). He stated that Kawasaki's percentage of the market in El Paso declined from 20.03% of the market in El Paso in December, 1975, to 14.07% as of September 30, 1976 (Tr. 136), a decrease of about one-third (Tr. 137), while for the state as a whole in the same period, its market share declined only 1.54% or approximately 10% (Tr. 137, 152-153). He states that Honda and Yamaha have dealerships located at about the same locations as the existing dealer and the proposed dealership (Tr. 139-140) and from this he believes there is some correlation between locations and market penetration in El Paso (Tr. 141). According to Protestant's Exhibit #2, Kawasaki's market share nationally has increased since 1973, while in El Paso it has declined except in 1975 when it had a high of 20% (Tr. 142-143). Kawasaki's position is that a dealer located in the northeast cannot adequately represent the entire area (Tr. 143-144). Assuming a total market in El Paso of 2,376 units, if Kawasaki maintains only 16% of the market, this would be 380 units and this would not be a profitable situation for the new dealer as the break even point for the new dealer would require the sale of 170 to 175 units (Tr. 146). Mr. Miller testified that the consumer benefits from price competition between dealers, until you reach the point that a dealer cannot maintain an adequate level of service (Tr. 47). He believes that there are people in El Paso now buying other brands who would buy Kawasakis if there were another dealership (Tr. 148) and also that entirely new customers will be found due to the interest generated by the additional dealer (Tr. 149). Kawasaki's experience has been that by virtue of the stimulus of competition, greater sales are created by competition itself (Tr. 149).

On re-cross examination, Mr. Miller testified that nationwide Kawasaki increased its market share .15% from December 31,

1975 to September 30, 1976 (Tr. 153-154) and it can be assumed that it will take one or two years at least to attain a 20% national market share (Tr. 155). The only major city in Texas that Mr. Miller could recall where Kawasaki has 20% to 25% of the total market is in Midland/Odessa where they have better than 25% (Tr. 155).

Dr. Kenneth W. Olm, professor at the University of Texas at Austin and a management consultant testified as a witness for the Applicant (Tr. 97-130). Dr. Olm stated that he was previously a member of the faculty of the University of Texas at El Paso; has lived in El Paso; has continued his visits and contacts in El Paso since moving to Austin; and is familiar with the El Paso area. He has performed management consulting work for automobile dealerships and other businesses in El Paso and he is familiar with the shopping habits of retail buyers in El Paso, although he has had no prior involvement in the marketing of motorcycles (Tr. 98-101). He has not personally studied motorcycle buying habits, but based upon his studies of the buying habits of automobile and quality furniture customers, and for products which are not absolute necessities, the dealer must be as convenient as possible to the segment which the dealer wishes to serve. El Paso is geographically an extremely difficult city to service all of the population and it is his opinion that the southeast sector is not conveniently served by a northeast location (Tr. 102-103).

While not based on any study, his understanding is that at the lower price levels motorcycles are considered to be more or less interchangeable, and that the main factors dictating a buyer's choice of dealers is a combination of convenience, price, quality of service, reputation of dealer, etc. (Tr. 104), although these may differ with respect to more sophisticated motorcycles (Tr. 105). Based upon his experience in the automobile industry, it seems that in most cases a second dealership point does promote an increase in sale and penetration as desired by the factory (Tr. 107), but he is unable to make an estimate of what will occur in the instant case (Tr. 107). He believes that an additional dealer would be in the public interest as it would be convenient for customers, would increase the quality of service offered by the existing dealer, and with two dealers the manufacturer would be better able to compete with other manufacturers (Tr. 108). His knowledge of the El Paso economy is that business is not suffering and in many retail sales areas it is quite good (Tr. 109). However, employment is down and unemployment is up, largely related to difficulties in the garment trades which is, in part, depressed (Tr. 110), but he does not believe that this would significantly affect the potential market for motorcycle sales (Tr. 111).

On cross-examination, Dr. Olm testified that if there were a dealership in the southeast El Paso area, most if not all of the existing dealer's customers in that area would shop at the new location provided it was more than just competent, was a clean facility, and had a good reputation (Tr. 120-121). He does not feel that it is possible in El Paso for one motorcycle dealership to adequately represent a manufacturer, because of the geography of the area he cannot provide convenient sales and service facilities (Tr. 121-122).

On further examination, Dr. Olm was not able to express an opinion as to the validity of the Kawasaki market forecast nor as to the consequences if that forecast turns out to be incorrect (Tr. 127-128).

Mr. Hiroshi Noda, Market Development Manager for Kawasaki Motors Corporation, also testified in support of the application (Tr. 165-236). Mr. Noda's responsibility is to develop and increase Kawasaki's market, by recommending new dealers in particular markets or the upgrading of existing dealers. Mr. Noda had made an analysis of Kawasaki's market position in the El Paso, Texas market and testified regarding various exhibits prepared by him. Applicant's Exhibit #3 is a market share trend analysis comparing Kawasaki's market shares by month from April, 1973, through August, 1976, in El Paso County, State of Texas and National. The exhibit shows that up until February, 1976, Kawasaki had a high market share, but after the closing of the second Kawasaki dealership in February, 1976, Kawasaki's market share has been decreasing month after month (Tr. 168). Applicant's Exhibit #4 is a comparison of motorcycle registrations in El Paso County taken from R. L. Polk figures, for the first nine months of 1975 and 1976. The exhibit shows that in the first nine months of 1976, the total industry increased 46.34%, while Kawasaki declined by 5%. This would represent a loss of 100 sales from what Kawasaki would have achieved had it had 20% of the market (Tr. 170-173). Applicant's Exhibit #5 is a graph plotted from the market share trend figures shown on Exhibit #3 (Tr. 174-175).

Mr. Noda testified concerning Applicant's Exhibits #6 and #7, charts and graphs showing sales made by the protesting dealer and also by Kasa Kawasaki during the periods 1973, 1974, 1975 and through November 11, 1976, and which show the zip code areas where buyers of such motorcycles reside. Mr. Noda testified that these exhibits show that one dealer cannot serve the entire El Paso market and that Protestant's dealership can adequately serve only the northeast area. Mr. Noda agreed that the warranty registration figures used to prepare these exhibits do not coincide with R. L. Polk registration figures, there being a discrepancy of 42 units

in 1976, and that the latter are considered more authoritative (Tr. 176-195). Mr. Noda also testified concerning Applicant's Exhibits #8 and #9, which contain calculations based upon population, housing and income statistics for particular sections of the city of El Paso, and which show that according to the number of warranty registrations per thousand people and per billion dollars of income, Kawasaki is well represented in the northeast but not well represented in the southeast, lower valley and central areas, except in 1975 when there were two dealers (Tr. 195-205). Applicant's Exhibits #11 and #12 are a chart and a graph entitled Comparison in Buying Power, showing the percentage of Kawasaki's registrations in the five sections of El Paso compared to the buying power of those sections, and which indicate that the northeast and lower valley areas are well represented compared to their respective buying power figures, but that the northwest, southeast and central areas are not well represented (Tr. 207-213). Applicant's Exhibit #10 is a chart entitled Comparison of Growth, showing relative sales performance of Kawasaki compared to total industry in El Paso County from 1973 through the first nine months of 1976. According to Mr. Noda this exhibit shows that the industry as a whole in 1976 made a greater recovery toward a return to 1973 figures than did Kawasaki (Tr. 214-215).

Mr. Noda testified that from his statistical analysis, he concludes that Kawasaki is very well represented in the northeast area of El Paso, and that it is not well represented in other areas, and that good cause in the public interest exists for another dealer license (Tr. 215-216).

On cross-examination, Mr. Noda testified that Applicant's Exhibit #4 shows an increase in the total motorcycle market in El Paso of 46.3% in the first nine months of 1976 over the first nine months of 1975, and he has no information or data to indicate another such increase (Tr. 217), but the Kawasaki marketing staff expects the industry to catch up to 1973 (Tr. 218). To the best of his recollection, total industry sales in 1973 were approximately 1,300,000, of which Kawasaki had about 12%. Total industry sales in 1976 were about 785,000 units, of which Kawasaki has about 17% (Tr. 218-221). The first time since 1973 that Kawasaki's market share in El Paso County fell below Kawasaki's statewide market share was in July, 1976 (Tr. 226).

On further examination, Mr. Noda testified that since August of 1975 there has been a steady decline in the Kawasaki market share in El Paso County of between 30% to 40% and that this decline causes a decline at the state level, meaning that the problem in Texas is in El Paso County (Tr. 227-228). However, at the state level, Kawasaki's market share decreased about 15% from August, 1975, to September, 1976 (Tr. 229-

230). Generally, Kawasaki is weak in wintertime, as Kawasaki is strong in street motorcycles which are sold mostly from February through September (Tr. 233) so it is probable that the Kawasaki market share declined in Texas in the last three months of 1976 but he does not believe the decline would be as much as occurred in El Paso County (Tr. 235-236).

Evidence in Opposition to Application

Mr. Harvey D. Lattner, President and manager of the protesting dealership testified in opposition to the application (Tr. 242-312). Mr. Lattner has been involved in the motorcycle business in various capacities following his discharge from the service in 1957 and he acquired the Kawasaki franchise in 1968 (Tr. 242-243). The reason for his protest is not that he is opposed to another dealer, but it is his analysis that the market is not going to grow by leaps and bounds next year and the addition of another dealer means dividing the sales which would probably bankrupt him. He does not feel the market is large enough to sustain two dealerships (Tr. 245). He had a second Kawasaki dealership in El Paso which opened in May, 1974 (Tr. 246) and the two dealerships were maintained as separate entities insofar as the public was concerned (Tr. 247-248). The second dealership was closed on January 1, 1976. During 1975, the two dealerships together sold 290 motorcycles, 178 of which were sold by Sport City and 11 of which were sold by Kasa Kawasaki (Tr. 248). The Kasa Kawasaki dealership was closed because it was broke due to insufficient market (Tr. 249). If Kasa Kawasaki had remained open through 1976, he estimates it would have sold about 100 units in addition to the 256 sold by Sport City (Tr. 249).

With reference to Protestant's Exhibit #1, Mr. Lattner testified that during the years 1973, 1974, 1975 and through June, 1976, the Kawasaki market share in El Paso was always larger than Kawasaki's statewide market share, and only in the last six months has the Kawasaki state market share exceeded its market share in El Paso (Tr. 250). It is Mr. Lattner's opinion that the decline suffered by Kawasaki in El Paso in the last six months is due to Kawasaki's slowness in reacting to meeting competition from other brands (Tr. 251). He testified regarding Protestant's Exhibits #4, #5 and #6, which are newspaper advertisements for Kawasaki, Honda and Yamaha motorcycles, showing Honda and Yamaha dealers offering comparable motorcycles at prices considerably lower than Lattner's prices for Kawasaki's and at prices which in some instances were below his cost (Tr. 253-256; Protestant's Exhibits 7 and 8). Part of the reason for the Kawasaki decline in business in the latter part of 1976 was this competition

from Honda and Yamaha. Kawasaki has now started a program to make its prices competitive, but it is three or four months late (Tr. 256). He does not believe that good cause exists for an additional Kawasaki dealer under the present circumstances and he feels that the addition of another dealership would be a substantial hardship to his business (Tr. 258-259). He does not feel the market in El Paso is large enough to sustain two dealers at this time (Tr. 259).

He stated that two-thirds of the Kawasaki line is not competitive price-wise with other brands and in many cases his competitors were retailing motorcycles at prices equivalent to his cost (Tr. 259-260). Mr. Lattner stated that the Yamaha dealer in El Paso is very aggressive and that Yamaha's large market penetration has not come at Kawasaki's expense but at the expense of the other brands (Tr. 261). A breakdown of his sales shows that 51% of his customers come from the northeast area, 24% from Fort Bliss, 20% from the southeast, and the remaining portion from the northwest, central and other areas (Tr. 262). About 20% of his customers come from the southeast and lower valley areas near the proposed new dealership and it is his opinion that the 10 mile or 15 minute drive between dealerships will not deter customers from shopping at his dealership as customers previously would shop at both Kasa Kawasaki and Sport City (Tr. 263). If the proposed dealership is established, he believes that most if not all of his business in the southeast area would be lost, and that many customers from the Fort Bliss area would also be lost (Tr. 264).

Mr. Lattner testified that his present investment in new motorcycles is \$125,000.00, with an additional \$25,000.00 in used motorcycles and \$65,000.00 in parts (Tr. 264-265). Considering his overhead costs and the fact that his service department is on a break even basis, he would have to sell between 300 to 325 motorcycles to break even. In 1976, his dealership had a net loss (Tr. 268-269). He does not believe 1977 will show great growth in El Paso, possibly from 2% to 5%, due to high unemployment and the peso devaluation. He does not believe the southeast area by itself can sustain an additional dealership without his business suffering and that any increase in the total market over 1976 will not be sufficiently large to allow both dealerships to do reasonably well (Tr. 270).

On cross-examination, Mr. Lattner described the area where his second dealership had been located (Tr. 271-272), and he stated that while total Kawasaki registrations were down 5% as of September 30, 1976, his Sport City sales were up following the close of the Kasa Kawasaki dealership (Tr. 274-275). He feels that the major factor in the Kawasaki market share decline is Kawasaki's slowness in reacting to

meet competition (Tr. 284, 286-287). Even though his business has not been profitable since 1974, Sport City has gained over the last year and is approaching a period where it will become profitable and he doesn't believe the market will be large enough in El Paso for another shop and allow for growth in his business (Tr. 289). He needs sales of between 300-325 units to break even and he had about 275 sales this past year so he is just about to the break even point (Tr. 290) and regardless of the reasons or the circumstances his dealership is not making money (Tr. 290). Mr. Lattner agreed that 1973 was a unique year for motorcycle marketing (Tr. 291).

On re-direct examination, Mr. Lattner testified that the exhibits show that the latest available figures for statewide Kawasaki registration show that as of September 30, 1976, Kawasaki's market share was 15.92%, a decline of approximately 15% from its September 30, 1975 market share of 18.28% (Tr. 294-295; Applicant's Exhibit 3; Stipulation). He believes that 1977 will be just a "hold-on" year, and that it will be a couple of years in the future before the market in El Paso will be large enough to sustain two Kawasaki dealerships (Tr. 296).

OPINION OF HEARING EXAMINER

As indicated earlier, the issues presented in this proceeding are: (1) whether the existing dealer is adequately representing the manufacturer or distributor in the community or metropolitan area in the sale and service of its new motor vehicles, and (2) whether good cause is shown for an additional dealer license in the public interest. The Commission may deny a license under Section 4.06(c) of the Code only where it is shown that the existing dealer is not adequately representing the manufacturer or distributor and no good cause is shown to exist for an additional dealer license in the public interest.

It is the contention of the Applicant that the distributor is not adequately represented in the sale of its motorcycles in the El Paso metropolitan area. This contention is based upon a steady decline in the Kawasaki share of the total motorcycle market in El Paso from 20.03% of the market in 1975 to 14.07% through September, 1976 (Tr. 60, 136; Applicant's Exhibit 3). Applicant's contention is also based upon its belief that the El Paso market is a unique market where it should obtain a greater market share than it enjoys at the state and national levels (Tr. 77-78), and that the Yamaha dealers in El Paso have a disproportionately high

percentage of the market at the expense of Kawasaki (Tr. 64-66, 77). Applicant also supports its contention by its projection of an overall increase in the motorcycle market of 10% and its projection that the Kawasaki market share in El Paso should be between 20 and 25 percent which it believes can be attained by two dealers (Tr. 60-61, 70). Finally, Applicant contends that good cause in the public interest exists by affording a more convenient facility to a large and growing segment of the population (Tr. 16-21, 33-34, 46-48). The evidence introduced in support of these contentions is outlined earlier in this Hearing Report.

Protestant contends that the Kawasaki market share in El Paso has exceeded both state and national averages in the years 1973, 1974 and 1975 and for the first six months of 1976, and that it cannot be concluded that Protestant is not adequately representing the Kawasaki line based solely on the figures for the period since June, 1976, when the market share in El Paso fell below that of the state average for the first time. It is further contended that the difference of 1.85% is not a sufficient indication of inadequacy of representation (Protestant's Brief, pp 3-6). Protestant further contends that while an additional dealership would increase the number of motorcycles sold, an increase to 25% of the market is mere conjecture and that the failure to attain the 25% market share would adversely affect both dealers (Protestant's Brief, pp. 6-8). Protestant maintains that the El Paso market has not been shown to be sufficiently large to sustain two dealerships and that mere convenience of location is not sufficient to establish the existence of good cause in the public interest when the result of the appointment of a second dealer would be detrimental to the existing dealer (Protestant's Brief, pp. 9-13).

Having carefully considered all of the evidence in the record in this proceeding, it is the opinion of the Hearing Examiner that the record, when considered in its entirety, does not establish that the existing dealer is not adequately representing the manufacturer or distributor, or that good cause exists for the additional dealer license in the public interest.

There is no question that the Kawasaki market share in El Paso through September, 1976, has declined considerably from the 1975 average, and has also fallen below the state and national averages. However, the Hearing Examiner does not believe that this nine month period is sufficient to establish that Kawasaki is not adequately represented in the area, particularly when one considers all of the facts of the case. Protestant has consistently achieved a market share in El Paso well in excess of that attained by Kawasaki in the state and nationally. Applicant's Exhibit 3 shows

that throughout 1973, 1974, 1975 and the first three months of 1976, the Protestant attained a higher share of the market than that attained by Kawasaki at the state and national levels. Moreover, the Kawasaki market share in El Paso continued to exceed that of the state until July, 1976, when it fell below the state average for the first time, and was only 1.85% below the state average as of September 30, 1976. While the Kawasaki share did decline in El Paso from 20% as of December, 1975, it appears that in only eight months out of the entire 41 months shown on Applicant's Exhibit 3 was the 20% market figure attained, and even in the peak periods of 1973 and early 1974, a 20% market penetration in El Paso was not attained. While Applicant's Exhibit 4 does indicate that compared to the first nine months of 1975, the total market in El Paso increased 46% in the first nine months of 1976 while Kawasaki's market share decreased 5%, the Applicant's witness, Mr. Noda, indicated that he did not foresee another such dramatic increase in the future (Tr. 217).

It is undoubtedly true, as Kawasaki maintains, that some market areas can be expected to obtain greater market penetration than the state and national levels, and it is conceivable that El Paso is one such market area. However, the Hearing Examiner is simply not convinced that the relatively brief and limited period relied upon by Kawasaki is sufficient to enable the Commission to conclude with any degree of assurance that a 20% market share in El Paso should be the norm, rather than the approximately 16% consistently attained by the Protestant, which also closely corresponds with the state and national averages. It should be noted that the industry as a whole decreased nationally in 1974 from 1973 levels, and further decreased in 1975 from 1974 levels (Tr. 72), and that at the state level Kawasaki's market share decreased about 15% from August, 1975 to September, 1976 (Tr. 229-230), and in all probability this market share declined further in the last three months of 1976 (Tr. 235-236). The motorcycle market in El Paso also decreased in 1974 and 1975 (Tr. 53-54). Additionally, Kawasaki's contention regarding the disproportionately high share of the market obtained by the Yamaha dealers compared to the other dealers is not convincing. Protestant's Exhibit 2 quite clearly shows that the Honda and Suzuki dealers in El Paso have lost far greater market penetration compared to their respective state averages than has the Protestant.

The record in this case is replete with unknown factors, and while the Commission certainly recognizes that a standard of absolute certainty is not possible in analyzing a market and establishing new dealers, and that a certain amount of risk is always involved in such endeavors, nevertheless, this application would seem to be premature until further

study and analysis indicates with more certainty than now exists that the Protestant is not adequately representing the Kawasaki line in the El Paso market and that the El Paso market can sustain two dealers on a profitable basis. In the instant matter, Kawasaki's justification for the application is also based upon its projection of an increase in the total motorcycle market of 10%, and the attaining of a market share in El Paso of between 20 and 25 percent. While market projections and estimates are appropriate and useful marketing tools, they should not in and of themselves be controlling, particularly where the results of the installation of another dealership could be disastrous to both the Protestant and the Applicant. For example, if the total motorcycle market in El Paso for 1976 was 2,160 units sold, as was assumed in this proceeding, then a 20% share of the market for Kawasaki would be 432 motorcycles. Protestant testified that he sold about 275 motorcycles in 1976, which would leave 157 units for a second dealer, a number which is below the 175 motorcycle sales needed to operate profitably (Tr. 146). By way of further example, if the market of 2,160 grows by only 5%, to a total of 2,268 motorcycle sales, 20% of this market would be 453 units. And, if the Protestant sold the 300 motorcycles which he states he must sell to operate profitably, this would leave 153 units for the second dealer, again an amount below the number of units needed for profitability. In fact, one must assume an increase in the total market of 10% and further assume that the two dealers will obtain a 25% share of the market before two dealers could be expected to operate profitably. For even attaining 20% of a total market increased by 10% as projected by Kawasaki, will mean total sales of 475 motorcycles, and if the Protestant sells 300 motorcycles and the Applicant sells 175 motorcycles, both are operating at marginally profitable levels. It is also noteworthy that the greatest number of Kawasaki motorcycles sold in El Paso County is 379 motorcycles sold in 1973, an admittedly high water mark year when motorcycle sales took a dramatic leap due to the oil embargo and gas shortage (Tr. 134-135).

It is the Hearing Examiner's opinion that an application should not be approved on the basis of such speculation as is proposed in this instance. This is particularly true where the existing dealer has not made a profit since 1974, even with two dealerships, and with a 20% share of the market during a certain period of time (Tr. 249, 289-290).

In addition to the above, there are other factors which could well affect the El Paso motorcycle market and which could be responsible, in part, for the decrease in the Kawasaki market share in El Paso. For example, there is no question that the economy in El Paso has been depressed and that the El Paso area has had an extremely high rate of unemployment.

of over 12% in the four month period from August through November, 1976. The Protestant also testified that a major factor in the Kawasaki market share decline is Kawasaki's slowness in reacting to meet competition from other brands (Tr. 251-256, 259-260, 284, 286-287; Protestant's Exhibits 4, 5 and 6). While there is some question regarding what effect, if any, the El Paso economy and unemployment situations has had on the motorcycle market, there is no question but that these additional factors raised by the Protestant, to the extent that they may have an effect on the motorcycle market in El Paso, are factors beyond the control of the existing dealer and certainly would not be remedied by the appointment of a second dealer. The added uncertainty of these factors merely confirms the need for further study and analysis of the El Paso market prior to the approval of an application for a second dealership.

Turning next to a consideration of the issue of whether or not good cause exists for an additional Kawasaki dealer license in the public interest, it is the Applicant's contention, as well as that of Kawasaki, that there is a need for a new dealership as proposed by the Applicant as one dealer cannot provide convenient sales and service facilities for Kawasaki's customers and potential Kawasaki customers in the entire El Paso metropolitan area (Tr. 16-21, 33-34, 46-48).

The Texas Motor Vehicle Commission Code does not define the terms "good cause in the public interest," nor does it provide any guidelines or standards for use in determining what constitutes such good cause. This issue must, therefore, be considered and decided on a case-by-case basis. The availability of convenient sales and service facilities to a large number of residents of a particular segment of a community or metropolitan area may very well constitute good cause in the public interest in a particular case. However, convenience of the facility to the public is not in and of itself controlling and there may well be other overriding factors which will govern if the consequences of the granting of the license are likely to be more detrimental than beneficial.

There can be no question that it would be more convenient to a certain segment of the public in the El Paso metropolitan area for there to be another Kawasaki dealer in the location proposed by the Applicant. Nor is there any question that the southeast part of El Paso is a rapidly growing and developing area. These factors must, however, be weighed against the detrimental or adverse consequences likely to result from the granting of the application. In view of the serious question which exists as to whether the market in El Paso is sufficient at this time to sustain two Kawasaki dealerships on a profitable basis, and considering the testimony

of the Protestant that he would lose most if not all of his business in the southeast area, as well as many customers from the Fort Bliss area, which could occur if motorcycle buyers are predominantly convenience buyers as was testified to in this case (Tr. 37, 104, 120-121), and considering the Protestant's testimony that the addition of another dealer would probably bankrupt him (Tr. 245, 264), it is the opinion of the Hearing Examiner that from the facts available at this time, the consequences of the granting of the application are likely to be more detrimental than the benefits to be gained from the approval of the application. Surely, it would not be in the interest of the public for the Commission to approve the issuance of a new dealer's license where the likely result will be the demise of the existing dealer who is otherwise operating in an acceptable manner. Moreover, it would not seem that the public would be greatly inconvenienced by having to travel an additional 10 miles, a driving time of 10 to 15 minutes, to get to the Protestant's dealership.

Considering the record as a whole, it is the Hearing Examiner's opinion that good cause in the public interest has not been shown to exist for an additional Kawasaki dealer license at this time.

Finally, it should be noted that no question whatsoever exists regarding the qualifications of the Applicant. From the evidence in the record it appears that the Roseborough family possesses all of the qualifications necessary for a dealership license, and at such time as it can be established, with greater certainty than is shown in this record, that there is justification, under the standards set forth in the Code, for the establishment of a second Kawasaki motorcycle dealership in the El Paso metropolitan area, then the application should be resubmitted.

FINDINGS OF FACT

1. Applicant proposes to establish a motorcycle dealership facility for the sale of the Kawasaki line of motorcycles to be located at 9801 Montana Avenue, El Paso, Texas, and has filed an application with the Texas Motor Vehicle Commission for a New Motor Vehicle Dealer's License for such dealership facility (Tr. 12-14; Applicant's Exhibit 1).

2. While the principals in the Applicant company have no prior personal experience in operating a motorcycle dealership, they have general business knowledge and experience, as well as experience with motorcycles, and are adequately capitalized (Tr. 6-12, 14-16, 30-32, 39-40).

3. Applicant intends to construct a dealership facility having adequate space to display, sell and service the Kawasaki line of motorcycles (Tr. 14).

4. The population of the city of El Paso in 1970 was 322,261, and is expected to increase to 397,000 in 1980 (Applicant's Exhibit 13). The southeast area of El Paso is a fast growing part of the city (Tr. 16-19, 28, 51; Applicant's Exhibit 13) and there is no Kawasaki dealership in the southeast area (Tr. 16-18; Applicant's Exhibit 2).

5. Honda and Yamaha each have two dealers in El Paso, while Suzuki, Kawasaki and Harley-Davidson each have one dealership (Tr. 44-45; Applicant's Exhibit 2). The two Honda dealerships are owned by the same person or group of persons, and the two Yamaha dealerships also have common ownership (Tr. 54).

6. The Protestant is the existing Kawasaki motorcycle dealer in El Paso and has been a Kawasaki dealer in El Paso since 1968 (Tr. 243). The Protestant opened a second Kawasaki dealership in May, 1974 which was operated as a separate dealership insofar as the public was concerned (Tr. 246-248). The second dealership was closed on January 1, 1976 as the dealership went broke (Tr. 248-249).

7. The Protestant's business has not been profitable since 1974 (Tr. 289; Applicant's Exhibit 15).

8. The distance between the Protestant's dealership and the Applicant's proposed dealership location is 10 miles, with a driving time of about 17 minutes (Tr. 26, 45-46).

9. The Kawasaki share of the market in El Paso County for 1973 was 16.63%, while the Kawasaki market share of the market for the state of Texas was 11.34% and 12.07% for the nation (Applicant's Exhibit 3).

10. The Kawasaki share of the market in El Paso County for 1974 was 16.23%, while the Kawasaki share of the market for the state of Texas was 11.83% and 12.82% for the nation (Applicant's Exhibit 3).

11. The Kawasaki share of the market in El Paso County for 1975 was 20.03%, while the Kawasaki share of the market for the state of Texas was 17.46% and 17.23% for the nation (Applicant's Exhibit 3).

12. The Kawasaki share of the market in El Paso County through September 30, 1976 was 14.07%, while the Kawasaki share of the market for the state of Texas was 15.92% and 17.38% for the nation (Applicant's Exhibit 3; Tr. 141-142).

The Kawasaki share of the market in El Paso County through November, 1976 was 13.31% (Tr. 169; Protestant's Exhibit 3).

13. The Kawasaki share of the market in El Paso County in 1973, 1974 and 1975 and the first three months of 1976 exceeded Kawasaki's share of the market at the state and national levels (Applicant's Exhibit 3).

14. The Kawasaki share of the market in El Paso County fell below the state average for the first time in July, 1976, and was 1.85% below the state average as of September 30, 1976 (Tr. 57-59, 250; Applicant's Exhibit 3).

15. The motorcycle industry as a whole sustained a decrease in sales in 1974 from its performance in 1973, and sales further declined in 1975 from 1974 levels. The motorcycle market in El Paso decreased in both 1974 and 1975, and at the state level Kawasaki's market share decreased approximately 15% from August, 1975 to September, 1976, and in all probability sustained a further decline in the last three months of 1976 (Tr. 53-54, 72, 229-230, 235-236).

16. The largest number of Kawasaki motorcycles ever sold in El Paso County was 379 motorcycles sold in 1973, a high water mark year when motorcycle sales took a dramatic leap due to the oil embargo and gas shortage (Tr. 134-135, 291).

17. The application is justified in part upon Kawasaki's projection of an increase in the total motorcycle market of 10%, and the attaining of a market share in El Paso of between 20% and 25% (Tr. 60-61, 70, 92-93, 94-95).

18. The decline in the Kawasaki market share in El Paso County may also be attributable in part to various factors beyond the control of the existing dealer, such as a depressed economy in El Paso, an extremely high rate of unemployment, and the slowness of Kawasaki in reacting to meet competition from other brands of motorcycles (Tr. 251, 284, 286-287; Applicant's Exhibit 15).

19. The disproportionately high market share obtained by the Yamaha dealers in El Paso has been at the expense of Honda and Suzuki dealers rather than the Kawasaki dealer (Protestant's Exhibit 2).

20. The establishment of an additional Kawasaki dealership in El Paso would provide a more convenient sales and service facility to a large and growing segment of the public in El Paso, affording an additional source of vehicles, parts and service to the public (Tr. 16-21, 33-34, 46-47, 102-103, 108).

21. The probability is that the establishment of the Applicant's dealership would result in the loss by the Protestant of a substantial amount of business, and that the result thereof would be the failure of the Protestant's business (Tr. 37, 104, 120-121, 245, 264; Applicant's Ex. 15).

CONCLUSIONS

1. The Kawasaki line of motorcycles is currently represented in the El Paso metropolitan area by the Protestant, Sport City, Inc.

2. The Protestant is in compliance with its franchise agreement with Kawasaki Motors Corp., U.S.A.

3. The evidence in the record does not establish that the Kawasaki line is not being adequately represented in the El Paso metropolitan area.

4. The evidence in the record does not establish that there is an adequate market in the El Paso metropolitan area to sustain two Kawasaki motorcycle dealers on a profitable basis.

5. The evidence in the record does not establish that good cause in the public interest exists for an additional Kawasaki dealer license in the El Paso metropolitan area.

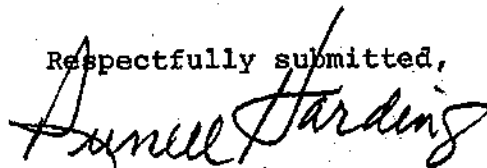
RECOMMENDED ACTION

It is the recommendation of the Hearing Examiner that the Texas Motor Vehicle Commission enter an order in this matter as follows:

That the application of Atomik Enterprises, Kawasaki Sales, for a New Motor Vehicle Dealer's License at 9801 Montana Avenue, El Paso, Texas, be denied.

Date: July 19, 1977

Respectfully submitted,



Russell Harding
Hearing Examiner

85.77

**ATOMIK ENTERPRISES, KAWASAKI SALES, APPLICANT
VS
SPORT CITY, INC., PROTESTANT
APPLICATION FOR LICENSE
El Paso, Texas**

Cited Sections: Section 4.06(c)

Principal Issues: 1. Adequacy of Existing Representation;
2. Public Interest

Held: Application denied.

Rehearing: On rehearing, the Hearing Examiner found that competitive manufacturers had added dealers, the local economy had substantially improved and the market was expanding substantially.

Held: Application approved, protest dismissed.

Original Hearing: October 27, 1977

Hearing Examiner: Russell Harding

Rehearing: April 6, 1978

Hearing Examiner: Russell Harding

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**TABLE CROSS-REFERENCING SECTIONS OF THIS BRIEF
WITH MB OF AUSTIN'S EXCEPTIONS**

Note: The ALJs' findings of fact and conclusions of law are amply supported by the record evidence, cited in the discussion section of the Proposal for Decision. In this reply, MBUSA focused on rebutting MB of Austin's arguments in its exceptions, generally and to specific findings, and not necessarily the particular support for any given finding.

Exception ¶ #	Findings of Fact/Conclusions of Law/General Issues	Section(s) Where Addressed
1	FOF 209-223 (General: effect of COVID-19)	II
2	General: lost sales and service opportunity	III.A. (sales opportunity) and attached 40-mile ring maps IV. (service opportunity)
3	General: unprofitable establishing dealers	III.B. and III.C.
4	PFD at 64 [on "breakeven" issue]	III.B. and III.C.
5	There is no ¶ 5 in the exceptions	
6	PFD at 62 [Swickard's business plans, focus on entry level-vehicles and financial information]	III.B. and III.C.
7	FOF 34	V.C. (adequacy of facilities) VI.C. (incentives)
8	FOF 37	IV.A.
9	FOF 38	IV.A. and IX
10	FOF 41, 125 and 126	V.B.
11	FOF 44	V.B.
12	FOF 121	V.A. (footnote on 40)
13	FOF 122	IV.A. and V.B.
14	FOF 123	IV.A.
15	FOF 127	V.C.
16	FOF 129 [sic 128 in exceptions]	V.C. at 46
17	FOF 130	V.A. (adequacy of sales representation) III.A. (lost sales opportunity)
18	FOF 142	III.B. and III.C.
19	FOF 143	III.A. through III.C. (sales) and IV.A. (service)

Exception ¶ #	Findings of Fact/Conclusions of Law/General Issues	Section(s) Where Addressed
20	FOF 144	VII
21	FOF 146 and 150	VII
22	FOF 147	VII
23	FOF 149	III.B. at 26-28 (entry-level vehicles)
24	FOF 153	VI.B. and VI.D. (general profitability to compete) VII (price competition)
25	FOF 154	VIII
26	FOF 155	VI.A. (correct "harm" standard)
27	FOF 156	IV.A.
28	FOF 157	IV.A.
29	FOF 158	IV.A.
30	FOF 159	IV.A.
31	FOF 160	III.A.
32	FOF 161	III.A., and attached 40-mile ring maps
33	FOF 163	III.A.2.
34	FOF 164	IX (re misstatement, PFD at 62) V.A. (re M-B brand losing to BMW since South Austin dealer opened)].
35	FOF 165	III.A. and III.B.
36	FOF 166	III.A., and attached 40-mile ring maps
37	FOF 167	VI.A. and VI.B.
38	FOF 170	VI.C.
39	FOF 179	III.A., VI.A and VI.B.
40	FOF 184	VI.D.
41	FOF 185	VI.D.
42	FOF 186	VI.D.
43	FOF 189	III.A.2. (Hatch) and VI.D. (Stockton)
44	FOF 190	III.A. and IV.A.
45	FOF 191	VI.B. and VI.C.

Exception ¶ #	Findings of Fact/Conclusions of Law/General Issues	Section(s) Where Addressed
46	FOF 192	III.A. (sales) IV.A. (service) VI.A. and VI.B
47	FOF 193	VIII
48	FOF 194 and 202	III.A and VII
49	FOF 194 [again] and 200	VI.B. and end of VII
50	FOF 195, 199 and 201	III.C. at 32-33
51	FOF 203	VIII
52	FOF 209-223	II
53	FOF 213	II at 9-10 [re MB of Austin being "recession-proof"]
54	Conclusion of Law 8	VIII
55	Conclusion of Law 10	VIII
56	Conclusion of Law 11	VIII
57	Conclusion of Law 12	VIII
58	Conclusion of Law 14	VIII
59	Conclusion of Law 15	VIII
60	Conclusion of Law 16	VIII

I. INTRODUCTION

MB of Austin carries forward throughout its exceptions a legal theory and conclusory statements from its post-hearing brief that were roundly rejected by the ALJs in their Proposal for Decision. MB of Austin argues for standards not supported by the law and then spuriously claims the Applicant failed to meet these standards, largely by arguing there is no evidence in the record of lost sales or service opportunity “realistically achievable” by Swickard’s new dealership that exceeds its breakeven profit point. From that faulty point, MB of Austin argues that a South Austin dealership will “cannibalize” MB of Austin’s sales or service, or will cause MB of Austin to “subsidize” the new dealer’s operations. MB of Austin explicitly states some version of this mantra in 70% of its exceptions to the findings of fact and almost 60% of its exceptions to the conclusions of law, as well as the 22 additional findings it claims must be added at pages 7-9 of its exceptions.

MB of Austin’s exception strategy appears to be an attempt to create a false appearance that the entire case boils down to one or two disputed factual and legal issues, and if MB of Austin can somehow raise enough doubt about just those issues, the entire proposal for decision somehow unravels. Often, MB of Austin tries to undo factual findings by claiming they are “misleading,” presumably because the findings ultimately support the outcome that MB of Austin disfavors. As a very simple example, Finding of Fact 146 states: “A new dealership will increase consumer choice and brand advertising in the Austin market.” Even if this one finding does not, on its own, carry the day for MBUSA, it is nonetheless fundamentally true. MB of Austin attacks this finding with the Exception in ¶ 21 arguing the truth and accuracy of this finding is “misleading” because its accuracy is “outweighed” by MB of Austin’s mantra arguments concerning

“lost opportunity realistically available.” Similarly, Finding of Fact 153 states: “MB Austin is a highly profitable dealership that is in good position for competing in the market.” This finding of fact alone may not be outcome determinative, but it is true. MB of Austin does not address the impressive profitability, financial strength, and diversification of MB of Austin in Findings of Fact 168-178, that underlies this finding, which was based in large part on the unrebutted portions of the testimony of a forensic accountant. Rather, MB of Austin attacks this simple, true, and accurate finding by complaining of what it “implies” in the face of its mantra argument concerning “realistically achievable lost . . . opportunity.” By doing little more than tiresomely repeating the same arguments ad nauseam, MB of Austin should not be able to implicitly undo large swaths of 223 findings of fact made following eight days of testimony, including the testimony of five expert witnesses.

In reality, the ALJs’ findings of fact and conclusions were amply supported by the evidence in the record under the appropriate legal theories. As MBUSA made clear in its Closing Brief, and which the ALJs found more credible and persuasive than MB of Austin’s oft repeated, but weak arguments:

- There is more than ample lost sales and service opportunity to support a new dealer in the market, based on the market analysis of Sharif Farhat, the methodology of which has been approved by both the Board and the Third Court of Appeals in multiple establishment cases, and MBUSA After Sales Manager, Ed Hoefl
- The Board has never adopted a requirement that an applicant or manufacturer prove what the new dealer’s ‘breakeven’ point is, with the exception of some references in the 2004 *Landmark* Proposal for Decision, which the Third Court of Appeals in that case (in *Austin Chevrolet*, discussed below) neither adopted nor addressed, and which the Third Court of Appeals previously, in *Gene Hamon*, roundly rejected.

The applicant and intervenor have the burden of proving good cause to establish the new dealership. Tex. Occ. Code §2301.652(a). While the Board must consider all the statutory factors, “the statute does not place any emphasis on one factor over another”; the “question of how best to resolve the issue, including the weight to be given to each statutory factor, is a matter committed to the [Board]’s discretion,” as is “whether in light of these factors there is ‘good cause’ for licensing a new dealership.” *Grubbs Nissan Mid-Cities, LTD v. Nissan N. Am., Inc.*, 2007 Tex. App. LEXIS 4154, *13 and *20 (Tex. App.-Austin May 23, 2007, pet. denied) (“*Grubbs Nissan*”) (affirming Director of the MVD of the TDOT’s decision dismissing existing dealer’s protest against establishment of new dealership in Grapevine, despite absence of any then current lost opportunity in the market).¹ As the Third Court of Appeals stated in *Grubbs Nissan* (decided, by the way, years after the *Landmark* Proposal for Decision), decisions are made regarding “specific proposals at specific geographic points in specific markets at specific times.” *Grubbs Nissan*, 2007 WL 1518115 at *6.

In contrast, MB of Austin misuses old cases to try to create standards that do not actually exist. Just as the facts and circumstances in *Grubbs Nissan* were vastly different from those in *Landmark*, discussed in *Austin Chevrolet*,² and on which MB of

¹ The circumstances in *Grubbs Nissan* are telling, in light of MB of Austin’s arguments on lost opportunity. There, the Director (the Board-equivalent decider at the time) adopted the proposal for decision’s findings that Nissan was then adequately represented and that there was little to no lost opportunity in the evaluation year. *Grubbs Nissan*, PFD at 25, ¶ 33. The Director nonetheless denied the protest, holding that the anticipated economic growth in the Grapevine area and the likely lack of material harm to the profitable protestant (which would remain profitable, but less so), was enough to outweigh the adequacy of representation and lack of appreciable lost opportunity. *Id.* at 28, ¶ 68, adopted in Final Order, with revisions not applicable. The Third Court of Appeals agreed.

² As examples, the Third Court of Appeals in *Grubbs Nissan* noted that (1) potential for future growth in the Grapevine market was more than sufficient to sustain a new Nissan dealership, with both experts agreeing the future of Tarrant County was “optimistic,” with, for example, a projected Fort-Worth/Arlington population increase of more than 150,000 by 2007 and a job increase of approximately 70,000; (2) automotive retail sales go through up and down fluctuations, but expected 2004 to be the start of an

Austin almost exclusively relies, the circumstances here are dramatically different from those in *Landmark/Austin Chevrolet* and the now 36-year old Board decision in *Lee Trevino Ford*, on which MB of Austin also relies throughout its exceptions.³

As is evident from *Grubbs Nissan*, which places discretion in the Board's hands to address the specific facts of the specific market and time, no Board decision is "precedent," least of which are the *Landmark* or *Lee Trevino* Proposals for Decision, on which MB of Austin repeatedly relies. MB of Austin's continuous assertions that the ALJs' findings and conclusions "violate" the *Landmark* Proposal for Decision are wrong, and even egregious. Prior Board decisions may be persuasive, but are not "precedent" that a subsequent Board "violates," unlike the Third Court of Appeals decisions that do bind the Board.⁴

As is demonstrated in their 98-page Proposal for Decision, the ALJs carefully considered and weighed all of the evidence, including the credibility of the witnesses and the experts' competing analyses, to arrive at their 223 separate findings of fact, all of which supported their conclusions that led them to recommend that the establishment should be allowed to move forward. Notwithstanding the diversity of the findings of fact and conclusions of law in the Proposal for Decision, and at the risk of falling into MB of

"up" period, expecting the retail automotive market to grow more rapidly in Dallas/Fort Worth than in Texas or the U.S.; (3) Grubbs was financially healthy, and improving, with annualized net profit in the protest year of more than \$800,000, which, given the flourishing market conditions, would expect Grubbs to continue to adjust its business strategy to capture the benefits of the projected economic growth; and just as Mr. Hardeman here, (4) by Grubbs's own actions in applying for the new Nissan dealership in Grapevine, it recognized the economic growth potential for the new dealership. *Grubbs Nissan*, 2007 WL 1518115 at *5-*7. Again, *Grubbs Nissan* was decided years after the *Landmark* PFD, as well as its appellate decision in *Austin Chevrolet* in the appeal of the *Landmark* Board Order.

³ *Austin Chevrolet, Inc. v Motor Veh. Bd*, 212 S.W.3d 425 (Tex. App.—Austin, 2006, pet. denied); *Landmark Chevrolet v. General Motors Corp.*, Docket No. 02-0002 LIC (Tex, DMV, MVD, Dec. 9, 2004), adopting Proposal for Decision (Sept. 16, 2004); *Lee Travino Ford v. Payton Wright Ford*, Proceeding 302 (Tex. MVC, March 7, 1984), adopting Proposal for Decision (Jan. 30, 1984).

⁴ E.g., *Grubbs Nissan* and *Austin Chevrolet*, which is the appeal of the *Landmark* protest.

Austin's "trap" of seeming elevating MB of Austin's spurious arguments by dedicating a disproportion amount of time and words rebutting the mantra arguments, MBUSA nonetheless will address these arguments in this reply. For the reasons set out below, and under the facts of this protest, all but three minor portions of MB of Austin's exceptions, discussed in Section IX below, should be rejected.⁵

II. THE ALJs DID CONSIDER EFFECTS OF COVID-19 BEFORE ISSUING THE PROPOSAL FOR DECISION⁶

First, the ALJs took judicial notice of various Executive Orders of Governor Abbott and County Judges in Order Nos. 13 and 15 regarding the pandemic. Thereafter, in their July 1, 2020 Order No. 15, the ALJs denied the second motion of MB of Austin to reopen the record to take testimony or alternatively, to abate this proceeding to some later date. The ALJs expressly denied MB of Austin's second COVID-19 motion "for the reasons urged by MBUSA in its response." Order No. 15 at 2.⁷ Those reasons are as applicable today as they were on July 1, and as they will be when this matter is before the Board. In summary:

- The economic downturn is limited, at most may go into or through 2021, when the pandemic subsides or a vaccine is available
- We are still years before the South Austin dealership would ever open for business, given what remains of the legal process, and the time it will take to construct the new dealership on what is now raw land after this matter is resolved

⁵ MBUSA is providing a cross reference table immediately before the introduction to this reply (at iii) indicating which section of this reply generally corresponds to the numbered paragraphs of MB of Austin's exceptions.

⁶ This section addresses MB of Austin' Exceptions in ¶¶ 1 (on FOF ¶¶ 209-223 generally on the seventh statutory factor, with MB of Austin contending those findings are "outdated and stale" given the pandemic), and ¶ 53 (that portion of ¶ 213 MB of Austin challenges, that its operations are essentially "recession-proof").

⁷ See PFD, FOF ¶ 10. The information contained in the bullet points on this page and the next page were included in MBUSA's June 1, 2020 opposition to MB of Austin's second motion to reopen the record, or alternatively to reconsider motion to abate.

- MB of Austin has been allowed even under the initial shelter-in-place orders to continue its sales and service business
- All of MBUSA's experts already anticipated and opined on the effects of a recession occurring in 2020, including on Austin specifically, and Austin's likely quick recovery long before the new dealership could possibly open
- The Mercedes-Benz assembly plant in Alabama is open and running
- Mr. Hardeman, MB of Austin's owner and dealer principal, by his actions, has completely expressed his lack of concern in the current pandemic-related economic downturn by buying an Audi dealership on April 10, 2020 in San Juan.

MB of Austin has not even attempted to address any of these issues. While some are certainly suffering economically during the pandemic, MB of Austin is not among them; as MBUSA noted, and therefore among the reasons on which the ALJs relied:

- As of April 30, 2020, MB of Austin's new vehicle sales for January through April were up 14 units over the same period in 2019 (258 versus 244)
- New vehicle sales in April 2020 alone were higher than in April 2019 (74 versus 68 last year)
- MB of Austin sold just four fewer used vehicles this year through April 2020 than through April 2019 (440 versus 444)
- MB of Austin's net profit through April 30, 2020 is \$ 2,087,969, which is \$ 600,000 over its net profit through April 2019, and \$300,000 over its 2018 net profit for that same period, which puts it on track this year to realize about \$ 6,264,000 in net profit.

Dr. Steven Nivin, a PhD. economist, is an associate professor of economics at Saint Mary's University in San Antonio, and Chair of the Economics Department. He also has a consulting practice and runs a think-tank at the University that focuses on regional economic issues, among other credentials.⁸ Dr. Nivin opined at length at the hearing, none of which MB of Austin disputed, on the incredible growth in Austin in the

⁸ Tr. 11/12/19, 149:12-17.

last decade, surpassing almost all other Texas metros, in terms of overall population, in higher income households, in GDP and overall income and wages in the economy, with low unemployment, and in overall luxury vehicle sales, among other factors.⁹ This tremendous growth was fueled in large part by the diversification in Austin's economy from a sleepy college town with government and health administration as its main industries to now include natural resources, construction, professional services, and information segments (e.g., scientific and technical services, computer systems, and data processing hosting), among others, all in higher-paying jobs.¹⁰ As the ALJs noted, this diversification and economic strength "positions it to recover quickly from a recession," citing Dr. Nivin's testimony.¹¹

There simply is no reason to believe, as MB of Austin urges without evidence from the record, that the Austin area will fare worse, or take longer to recover, than it did in any of the previous recessions. In contrast, the record clearly supports the opposite—Dr. Nivin and Sharif Farhat, an automotive market analysis expert, opined in the 2019 hearing on this very situation, and Dr. Nivin on how Austin has historically suffered less and recovered more quickly than other Texas cities or elsewhere after previous

⁹ See, e.g., PFD, FOF, ¶¶ 209-210, 215-219, 223, and discussions at 25-26 and 77-78. Notably, MB of Austin has not filed any specific exceptions to the FOF on this seventh statutory factor other than the pandemic, at ¶¶ 209-223, with the exception that MB of Austin is "recession-proof," discussed below. See Exceptions, ¶ 53.

¹⁰ PFD at 24-25; Tr. 11/12/19, 173:1-176:19; Ex. I-71 at 20-21. MBUSA addresses in Section III.B and III.C below MB of Austin's contentions that MBUSA and Swickard had some obligation to produce evidence of when Swickard would be profitable. See Exceptions, ¶ 1 at 2. MB of Austin's additional contention that the pandemic will purportedly affect "younger, less affluent buyers" and thereby Swickard's strategy to sell entry-level Mercedes-Benz vehicles is a red herring. Those "less affluent buyers" Mr. Swickard so successfully targeted in his Wilsonville, Oregon dealership are young professionals, many in tech industries. See, e.g., 11/16/19, 1078:17-23. Due to their ability to work largely from home, it makes sense that these consumers are likely less impacted by the economic shutdowns.

¹¹ PFD at 78, with multiple transcript references to Dr. Nivin's testimony.

recessions, including the Great Recession in 2008.¹² Perhaps most important, this current economic downturn was caused by the shelter-in-place orders that temporarily closed mostly flourishing businesses before the shutdown. As businesses eventually fully reopen, whether late this year or even next year, unemployment will ease, people will spend money, and the economy should recover, as it has before. Consequently, the effects of the pandemic shutdowns will be in the rear-view mirror before Mr. Swickard is ready and able to open his new dealership.

While all area economies decreased during the 2008 recession, Austin's did not fall quite as much and bounced back stronger and more quickly, due largely to its diversification over the last 15 years.¹³ Undisputed are Dr. Nivin's opinions that not only has the Austin economy shown a strong ability in the past to absorb a recession and recover from it relatively quickly and strongly,¹⁴ but also should a recession occur in the next year or two (i.e., 2020 or 2021), Austin's economy will dip some, but not as much as other areas of the country, and will bounce back strongly, as it has in the past.¹⁵

As Dr. Nivin explained in his report: "Even if a recession does occur [in the U.S. and global economy], the upshot is that I see no substantial reason why the Austin economy will not continue to grow strongly over the next ten years, as it has over the past few decades. . . . [I]t is reasonable to expect that the economic conditions in the Austin metropolitan area will remain very strong over the next ten years, even taking

¹² See, e.g., Dr. Nivin's report, Ex. I-71 at 31-32.

¹³ Tr. 11/12/19, 169:22-171:2; Ex. I-71, Charts 10 and 11 at 15-16.

¹⁴ Ex. I-71 at 14.

¹⁵ Tr. 11/12/19, 183:21-184:13.

into account the possibility of a recession.”¹⁶ Importantly, Dr. Nivin gave these opinions fully expecting a recession this very year—in 2020.¹⁷ As alarming as this pandemic may feel, on a purely economic basis, there is nothing about an economic downturn that was not fully anticipated and accounted for in Dr. Nivin’s essentially un rebutted opinions about the strength of the Austin economy and reasonably foreseeable projections of economic conditions.

Even if Austin deals with a recession in the near term, Mr. Farhat testified it is misguided to focus on the next year or two.¹⁸ As Mr. Farhat explained, whether the market goes up, goes down, or stays stable may be interesting, but it is not critical to the decision as to whether it makes sense, or is reasonable, to add a Mercedes-Benz dealership in South Austin. The decision to add this additional dealership is a very long-term one—it is not a two-year, or even a five-year, situation.¹⁹ And as Fred Newcomb, MBUSA’s former Manager of Dealer Network, testified, the decision to add a dealership is a long-term decision, involving a long-term commitment and investment.²⁰

As Suzanne Heinemann, a forensic accounting expert testified, MB of Austin’s operational strengths are in more recession-proof areas, not reliant on new vehicle sales for its profitability—MB of Austin’s overall higher revenues, higher gross profit margins in the new and used vehicle departments, its higher number of used vehicles per new vehicle sold with higher gross profit per used unit it sells and, in particular, its

¹⁶ Ex. I-71 at 31-32 (“ . . . there is a good chance the U.S. and global economy will go into a recession in 2020”).

¹⁷ Ex. I-71 at 31.

¹⁸ Tr. 11/21/19, 1632:6-1633:12.

¹⁹ *Id.*

²⁰ *E.g.*, Tr. 11/13/19, 250:14-251:8.

high net profit in fixed operations (i.e., its service and parts business)—are all critically important.²¹ As she explained, fixed operations are more recession-proof, because consumers still have to have their vehicles serviced, a life blood for a dealer in a down market, even if consumers are buying fewer new cars.²² Through at least April 2020, though, MB of Austin has continued to sell new cars, even more than it did in the same period in 2019! In sum, the hearing evidence fully addressed the prospect of an economic downturn or recession in 2020 and 2021. It is still true, and it is still undisputed, that the reasonably foreseeable economic conditions in the Austin metropolitan area will remain very strong over the next ten years.

Again, the new dealership will not likely open until 2023 or 2024 at the earliest, once this matter concludes, and Mr. Swickard is able to begin installing the infrastructure for the new dealership and constructing the facilities on what is now raw land. This timeline fits with Dr. Nivin's assumption in his report that construction would start in 2022.²³ Dr. Nivin's report assumed a two-year ramp-up period and the dealership not reaching full operations until 2025.²⁴ It may be hard to keep perspective now, but MB of Austin submits nothing to say that the economic effect of the COVID-19 pandemic will not be long in the rear-view mirror by then.

Mr. Farhat's graph of the bounce back of the auto industry nationally after the Great Recession in 2008, for example, attests to the short-lived, albeit painful, economic

²¹ See MBUSA's post-hearing Opening Brief at 79-82.

²² Tr. 11/15/19, 761:12-23. Contrary to MB of Austin's Exception in ¶ 53, Ms. Heinemann's testimony, un rebutted by MB of Austin, and her underlying analysis, is the evidence on which the ALJs based their FOF ¶ 213.

²³ See Ex. I-71 at 32.

²⁴ Ex. I-71 at 36.

effects of that recession, relative to the time it will take here before a new dealership opens.²⁵ And as Dr. Nivin testified, which MB of Austin did not dispute, the Austin economy again will bounce back, and long before the new dealership could possibly open.

MB of Austin again seeks to cynically take advantage of current events as an excuse to reopen the record to delay this establishment that has been planned since 2014, as it did in its two motions to reopen the record. Far from being in free fall, MB of Austin is doing better than it did in 2019 as of the end of April 2020 (the last financial reporting period before MBUSA's opposition to MB of Austin's second motion), despite the effects of COVID-19 on the national economy. MB of Austin's request is unconscionable, particularly in light of Mr. Hardeman's purchase of an Audi dealership, getting licensed and opening in mid-April when the pandemic was raging and stay-at-home orders were in place. It is a hypocritical claim that an uncertain economic future should stop Swickard from receiving a license three to four years from now, while at the same time Mr. Hardeman trusts in the same future to decide that finalizing MB of Austin's own purchase and licensing of an Audi dealership in the midst of the pandemic is worthwhile. For all of the reasons MBUSA identified, and that the ALJs adopted in denying the second motion on this issue, MB of Austin simply seeks to further delay this establishment. That is patently unreasonable, unnecessary, and a waste of judicial resources.

Remanding this matter for a new hearing, with its additional discovery, new expert reports and testimony will not solve anything. The short-term state of the

²⁵ Tr. 11/21/19, 1632:6-1634:10; Ex. I-67 at 40.

economy will continue to be barely relevant to the opening of a dealership in South Austin three or more years after that. Even MB of Austin's own expert, Edward Stockton, stated in an affidavit in support of MB of Austin's second motion to reopen the record that "the COVID-19 outbreak . . . has created uncertainty with respect to the future prospects of the economy as a whole and the retail automotive industry," essentially admitting he has no idea what the economy will be like in six months or a year, when MB of Austin advocated for all discovery to be completed and a new hearing occur. That would clearly be a waste of judicial resources. In contrast, as Dr. Nivin testified, and without dispute, Austin and the Texas and U.S. economies will rebound from any recession in 2020 in less than one to two years.²⁶ That is long before the South Austin dealership would ever be ready to open.²⁷

Just as Mr. Hardeman admits by his Audi dealership purchase, and MBUSA's witnesses testified, the establishment of a new point in South Austin is about the future, five or ten years out and beyond, not about six months or even a year or two from now. For all of those reasons, MB of Austin's exceptions and requests to reopen virtually the entire record were properly rejected after thorough consideration.

III. THE ALJS ADOPTED THE APPROPRIATE ANALYSIS OF LOST SALES OPPORTUNITY

Lost sales and service opportunity are components of the fourth statutory factor, the extent of harm to MB of Austin if the new dealership opens. See PFD at 62-73, FOF ¶¶ 155-193. MBUSA is addressing this issue first before the remaining issues because

²⁶ Tr. 11/12/19, 183:21-184:13, 196:18-197:8.

²⁷ MB of Austin's argument that reopening the record will not prejudice the parties because of the years it will take to open the dealership is misleading. One key reason construction has not already begun is this ongoing legal process. Additional delay in the legal process will only delay the opening even longer, to the detriment of the public interest, but to the benefit of MB of Austin.

MB of Austin's challenge to the ALJs' findings of lost opportunity, and its contention that there must be evidence of Swickard's 'breakeven' profit point in relation to lost sales opportunity, permeates virtually every one of its 60 separate exceptions to the Proposal for Decision.²⁸ Lost service opportunity is addressed in Section IV below.

A. Gross Loss Plus All Insell Is the Appropriate Standard for Assessing Lost Sales Opportunity

1. Gross loss and insell have been approved and applied in numerous Board and Appellate decisions as the measure of lost sales opportunity

As a preliminary matter, MB of Austin's reliance on the *Landmark* Proposal for Decision for its mantra that there is no "reasonable" or "realistic" lost opportunity is simply wrong. The Third Court of Appeals, in the appeal of the *Landmark* Board decision, expressly approved of gross loss and all insell, as Mr. Farhat did here, as the appropriate standard of lost sales opportunity in a market. *Austin Chevrolet, Inc. v. Motor Vehicle Bd.*, 212 S.W.3d 425, 437 (Tex. App.—Austin 2006) (reh. overruled). The court in *Austin Chevrolet*, as the Board in *Landmark*, only disagreed with the benchmark by which gross loss was calculated for the Houston market (GM's expert's used Texas state average versus the Board's multi-point (metro) Texas markets, where 249 of the 259 Chevy Texas dealers were in rural, single-point markets, and with counting all insell in the unusual facts of that case where 80% of it was by a single dealer (what the court characterized as a "fringe" dealer) located at the very edge, literally, of the defined

²⁸ See Exceptions, ¶¶ 2-4, 19, 22, 24, 31, 32, 33, 36, 44, 45, 46, 48, 49, 51, 54, among others discussed below in other sections. Other aspects considered under the fourth factor, such as the potential financial impact, actually the lack thereof, to which the "breakeven" concept is intertwined, are discussed in Sections III.B. and VI. below.

Houston market. *Id.* Neither circumstance is present here.²⁹ Unlike in the *Landmark* PFD, using gross loss and all insell is not “pie-in-the-sky optimism” as the ALJ in that case stated in the unique facts of that case. Consequently, the “realistic” and “reasonable” calculation of lost opportunity is gross loss and insell under the appropriate comparative benchmark. MB of Austin did not challenge Mr. Farhat’s use of the national or Texas state benchmarks, nor his assessment of the reasonableness of those benchmarks to assess the Austin market for Mercedes-Benz vehicles.

MB of Austin also ignores the further facts found by the ALJs here that the lost sales opportunity model does not take into account future population and economic growth in the Austin AOR, which Dr. Nivin testified about without any dispute by MB of Austin. That is, the lost opportunity was calculated from a 2018 snapshot, and will grow with the growth of the Austin AOR. The Austin historical and prospective growth are in stark contrast to those in *Austin Chevrolet*, where the Third Court of Appeals noted that in 1993, the Houston market was “characterized by a ‘decade of sluggishness, a declining trend in automobile sales, stagnant wages, substantial layoffs, and only modest growth projections.’” 212 S.W.3d at 434.

Using gross loss and all insell has been adopted in a number of Board and appellate decisions. See, e.g., *RCJD Motors, Inc. v. Huffines Dodge Plano, L.P.*, SOAH Docket No. 608-10-5694.LIC, MVD Docket No. 10-0048.LIC, Final Order (Tex. DMV, MVD, July 12, 2012), adopting with minor modification, Proposal for Decision (Apr. 2, 2012), Final Order at 6 and PFD at ¶¶ 60 and 42 (ruling use of gross loss and insell methodology as appropriate means to determine amount of untapped opportunity in

²⁹ See Sections III.A.2. below for discussion of the flaws in Dr. Hatch and Mr. Stockton’s arguments against Mr. Farhat’s analysis.

market); *Graff Chevrolet Co. v. Tex. Motor Veh. Bd.*, 60 S.W.3d 154 158, n.4, 159-60 (Tex. App.—Austin 2001, no writ) (affirming Board's decision in *North Arlington Co. v. Graff Chevrolet*, Docket No, 97-777 (Sept. 1999), *adopting* Proposal for Decision (July 19, 1999), PFD at 18-21 (using gross loss and insell as measure of lost opportunity); *Burns Motors Ltd. v. Payne Edinburg*, SOAH Docket No. 608-17-1285.LIC, MVD Docket No. 16-0028.LIC (Tex. DMV, MVD, June 14, 2018), *adopting*, Proposal for Decision (Feb. 15, 2018), PFD at 71 (Board counted all insell as lost opportunity that the protestant could have captured but did not from outlying dealers, based on Mr. Farhat's analysis).

Again, overly and inappropriately relying on the *Landmark* PFD, MB of Austin faults MBUSA for not at least looking at gross loss or insell within a 20-mile radius, or, as it acknowledges several times, the 40-mile radius that Mr. Farhat's penetration profiles were based on, rather than the entire Austin AOR. Exception 2 at 5. Mr. Farhat selected the 40-mile radius because that was the general reach into the market of both MB of Austin and MB of Georgetown with respect to new vehicle sales, unlike the very GM dealer-crowded market in Houston in 1993.³⁰

Counting all gross loss and insell within that 40-mile radius of the South Austin dealership location actually includes virtually all of the vehicle registrations and insell in

³⁰ MB of Austin's attack on Mr. Farhat's penetration profile for the South Austin dealership (at 7 of the Exceptions, third bullet point) is simply wrong. Each of the several mile-rings of the penetration profiles around a given dealer are based on the existing dealers' sales effectiveness at those specific distances from their dealerships. Consequently, the location of the South Austin dealership is directly taken into account, specifically the demographics and registrations within each ZIP code in a given ring around the new dealership's location.

the Austin AOR. As the attached maps in the record demonstrate,³¹ only a very few registrations and insell fall outside of the 40-mile ring (each dot equaling one registration or one insell). More important, Mr. Farhat's analysis does not include the gross loss or insells in those ZIP codes inside the 40-mile ring, but outside of the Austin AOR. Those ZIP codes are primarily south of the boundary of the Austin AOR, on the way to Selma (the gray area in the ring but outside the Austin AOR), which is a more populous area, likely with more gross loss and insells than in the ZIP codes to the north and west outside the 40-mile radius but inside the AOR, reflected in the few random 'dots' on those respective maps.

Using Mr. Farhat's lost opportunity calculation of 755 units in his 2018 snapshot is neither "inflated" nor "unreasonable" or "unrealistic," as MB of Austin tiresomely argues in virtually every one of its exceptions. Lost sales and service opportunity is just that—opportunity. Sales opportunity is vehicle sales lost to competitors or to Mercedes-Benz dealers outside the AOR. Service opportunity is service lost to independent service shops that the existing Mercedes-Benz dealers could have captured, but did not. And, as the ALJs found, the 755 units from the 2018 snapshot, does not even take into account the enormous and undisputed growth projections for Austin. That growth will provide even more opportunity for the new dealership without "cannibalizing" MB of Austin's sales and service businesses, or making MB of Austin "subsidize" Swickard's sales years into the future.³² All of MB of Austin's exceptions and its proposed additional

³¹ The underlying maps are located in Mr. Farhat's report at Exhibit I-65 at 27, 33, 81, 82, 96, and 97. For demonstrative purposes, for this brief, the scale on each page was used to draw a circle with a 40-mile radius centered at the proposed location. The accuracy of this drawn circle is easily checked with a ruler.

³² This is also why it is unnecessary to reduce either the 2018 insell or gross loss, despite MB of Austin's argument, with which Mr. Farhat agrees, that every market has some of both.

“findings” (at 7-9) should be rejected on the basis of Mr. Farhat’s methodology that the Board and Third Court of Appeals have consistently followed.³³

2. The “expert” opinions on lost sales opportunity offered by Dr. Hatch is not based on accepted methodologies in the industry and have many other flaws

As MBUSA explained at length based on its experts’ testimony in its post-hearing briefing, the ALJs are correct—the methodologies Dr. Hatch used to arrive at greatly reduced lost sales opportunity are not accepted in the industry and are flawed. See Exception 43 regarding FOF 189.

As to his analysis of net loss and insell, Dr. Hatch’s contention that only 160 to 195 retail registrations is the sum total of the lost opportunity in the Austin AOR (compared to Mr. Farhat’s gross loss of 474, Ex. I-67 at 2), had the new dealership opened in 2018, is based on several flaws. First, Dr. Hatch’s netting the loss at such a high level as an AOR or AOI, as Dr. Hatch advocates, obscures specific areas of an AOI that are underperforming, like the South Austin area of the Austin AOI.³⁴

Second, his theory that registrations for a brand occur at “random” throughout an AOR based on his coin toss example does not reflect reality of the analysis of a market; Mr. Farhat’s calculating loss at the ZIP code level takes into account the unique demographic and location elements of each ZIP code, as the ALJs found. See FOF

³³ *E.g.*, FOF 143, 147, 153, 160, 161, 166, and others. MBUSA discusses in Section III.B. below why proof of Swickard’s “breakeven” point is not necessary in relation to the available lost sales opportunity.

³⁴ As just one example, calculating net loss at the AOI level obscures specific areas within the AOI that are underperforming. As Mr. Farhat’s example at 13 of his rebuttal report illustrates, if the north half of an AOI was above 100% RE (the green portion), but the south half was all below 100% RE (yellow portion), Dr. Hatch’s net loss calculation would cancel out the two areas and come up with zero loss for the AOI. That’s misleading, in that we can see there clearly is a large area of the market that is underperforming. See Tr. 11/21/19, 1591:16-1592:21; Ex. I-67 at 13. Taking Dr. Hatch’s net loss calculation to the extreme, if all markets in the U.S. with above 100% RE were netted against all below 100% per Dr. Hatch’s “net loss” theory, it will always sum to zero, and no opportunity would appear to ever exist anywhere in the U.S. Tr. 11/21/19, 1592:22-1593:4.

163. That's because the expectation (denominator) of the registration effectiveness equation per ZIP code is based on the competitive registrations unique to that specific ZIP code, as is the actual Mercedes-Benz registrations in the numerator. Interestingly, Dr. Hatch's own "net loss" opportunity calculation from his AOI level is surprisingly close to Mr. Farhat's at the ZIP code level—474 versus Dr. Hatch's 400 to 425. That's hardly an earth-shattering difference.³⁵ That these calculations are so close is not surprising, as the vast majority of ZIP codes throughout the metro are underperforming.³⁶ And the underperformance was increasing in 2019, as both Mr. Farhat's gross loss calculation reveals, and likely Dr. Hatch's net loss would too, because the majority of the Austin AOR continues to underperform, but increasingly so in the South Austin area.³⁷

Third, and perhaps more important, Dr. Hatch's contention that the degree of interbrand competition in one area somehow reduces the 100% expected registration effectiveness to something lower than that (that is how he got from his own 425 net loss to 160-195 lost opportunity), is wholly unsupported, and has not been advanced by any dealer or manufacturer expert who has analyzed any market for a new dealership or otherwise.

Fourth, Dr. Hatch ignores the existence of cross-sell throughout the Austin AOR by all dealers; both MB of Austin and MB of Georgetown sell new vehicles within 40

³⁵ Tr. 11/21/19, 1593:5-21, 1603:14-1604:6; Ex. I-65 at 96 and Ex. I-67 at 19; also of interest is Dr. Hatch's admission that his "net loss" calculation at the AOI level is really the result of summing up the gross loss in each AOI; that's exactly what Mr. Farhat did—he determines the loss in each ZIP code on a net loss basis, then sums those losses to get the gross loss in the market. See Dr. Hatch's admission, Tr. 11/20/19, 1221:9-1225:16.

MBUSA discusses below in this section Dr. Hatch's improper reduction of his net loss number for the degree of competition in each AOI.

³⁶ Ex. I-65 at 96 (yellow shaded ZIP codes and red dots throughout the metro).

³⁷ Tr. 11/21/19, 1594:12-1597:8; Ex. I-67 at 19-20 (increases from 474 in 2018 to 576, annualized, in 2019).

miles of their dealerships (40 miles of which covers almost the entire Austin AOR, per each of Mr. Farhat's maps in his reports, as graphically shown in the attached maps).

Further, Dr. Hatch's insell "opinion" is hardly one at all. Dr. Hatch admits that insell will be reduced with the addition of a new dealer into a market, and in particular it is the additional inventory that the dealer brings to the market and the added price competition for all dealers of that brand that will lower insell.³⁸ As Dr. Hatch admitted, increased inventory for customers to shop and better pricing are two of the primary reasons insell occurs in the first place.³⁹ While Dr. Hatch essentially guesses insell will be reduced by about 55 units of the actual insell of 281⁴⁰ in the AOR in 2018, he admitted he has never done a calculation of how much insell a new dealer will capture and in fact, has never studied that.⁴¹ While Dr. Hatch criticizes Mr. Farhat for including all insell in the Austin AOR as lost opportunity, nowhere does Dr. Hatch calculate how much insell will be captured by a new dealer. He admitted he never studied that before.⁴²

As Dr. Hatch acknowledged, he has no experience in evaluating auto dealer networks; his flawed analyses and methodologies make that abundantly clear.⁴³ As Mr. Farhat stated in his rebuttal report and testified, Dr. Hatch's methodology is "not well

³⁸ *Id.*

³⁹ Tr. 11/20/19, 1200:6-1204:5, 1240:20-1241:18.

⁴⁰ As to the 281 of insell in 2018, see Tr. 11/14/19, 504:19-25, 505:25-506:12, 578:18-579:5; Ex. I-65 at 42, 97-98. See also Gomez testimony: Tr. 11/19/19, 1090:22-1092:23 (through the half year of June 2019, insell, or "pump-ins," into the Austin AOI alone was 204, versus MB of Austin's sales outside the AOR of only 98).

⁴¹ Tr. 11/20/19, 1204:6-17, 1230:16-1231:4.

⁴² Tr. 11/20/19, 1230:16-1231:4.

⁴³ See MBUSA's Closing Brief at 65-73.

developed,” “novel,” “not utilized in automotive dealer network planning,” and something he has “never seen before” and has not been accepted in the industry.⁴⁴

Regardless of how Dr. Hatch came up with this novel methodology to reduce the lost sales from his own net loss of 400 or 425 units to 155 and insell to 55 units, it does not pan out at all in the real world. To test Dr. Hatch’s theory, Mr. Farhat applied it to what actually happened with the BMW brand in the Austin AOR before and after the new dealer in South Austin was added in mid-2018, so same market, same approximate area of a new dealership.⁴⁵ What Mr. Farhat found is that Dr. Hatch’s methodology of using historic performance in the market of existing dealers to the new dealer, or the South Austin AOI, would have resulted in an increase from 82% RE in 2017 (before the addition) to only about 90% in 2018 and 2019 (after the new dealer went in), when in fact the BMW brand achieved 102.1% RE in the South Austin AOI in 2018 and 116.4% in 2019, annualized, so way above what Dr. Hatch’s method would have predicted and with a much higher number of corresponding registrations.⁴⁶ The same is true for the balance of the Austin AOR—Dr. Hatch’s model would have predicted only an increase to about 95% in 2018 and 2019 from actual in 2017 of 90% RE, when in fact BMW’s registration effectiveness rose to 108% and 102.2%, respectively, in 2018 and 2019.⁴⁷ And as Mr. Gomez testified, as of October 2019, the existing BMW dealer in the market before the establishment only lost on average two sales per month, or 20 sales through October, from the same period the prior year before the establishment and had already

⁴⁴ Tr. 11/21/19, 1608:6-12; Ex. I-67 at 3, ¶ 5.

⁴⁵ Tr. 11/21/19, 1608:13-1611:8.

⁴⁶ *Id.*; Ex. I-68 at 14.

⁴⁷ *Id.*; Ex. I-68 at 15.

made 1,440 new vehicle sales through October 2019; more interesting, the new South Austin BMW achieved 760 new vehicle sales through October 2019, up 400 vehicles from 2018.⁴⁸ No “fixed pie,” no “cannibalization” of the existing dealer; clearly any 2018 lost sales opportunity is just a threshold and not the ceiling.

Mr. Farhat’s analysis of the lost opportunity in the market based on gross loss and insell is appropriate and, as noted above, has been adopted in many Board decisions and the Third Court of Appeals decision in *Austin Chevrolet*. All of MB of Austin’s challenges to his analysis throughout its exceptions, both specifically and generally in relation to other specific issues, should be rejected.⁴⁹

B. Evidence of Swickard’s “Breakeven” Sales Number is Neither Required nor Necessary to Assess Lost Sales Opportunity⁵⁰

While MB of Austin correctly notes that the Board must consider all the statutory factors, it tries to define an entirely new factor that it deems must be proven and is determinative—proof of Swickard’s “breakeven” profit point. That lost opportunity must be greater than the “number of new vehicles a proposed new dealership must sell to breakeven,” or it will “cannibalize” existing dealers’ sales is by far the most consistent, and erroneous, theme throughout MB of Austin’s exceptions. It is fatally flawed in many respects.

⁴⁸ Tr. 11/19/19, 1082:19-1084:25.

⁴⁹ MBUSA does agree that the ALJs misspoke, in their statement on page 62 of the PFD, that MB of Austin calls out. It is BMW’s brand performance in Austin, based on registration effectiveness, not the new dealer’s sales effectiveness, that increased after BMW’s establishment in South Austin. See Section IX below.

⁵⁰ See Exceptions, ¶¶ 2-4, 18, 23, 26, among others, including the purported import of MBUSA’s and Swickard’s failure to provide sales projections, financial information, business plans and the like, discussed in Section III.C. immediately below.

First, the “breakeven” concept is simply a repackaging of a previously rejected “economic viability” argument that Protestant’s counsel unsuccessfully urged in the relocation case of *Gene Hamon Ford, Inc. v. David McDavid Nissan, Inc.*, 997 S.W. 2d 298, 308 (Tex. App.—Austin 1999, pet. denied). (“McDavid also argues: “Without knowing Hamon’s break-even point at the proposed League City site, there is no rational way of knowing whether there is enough ‘lost opportunity’ available to Hamon at League City without seriously harming McDavid.”) As the Third Court of Appeals stated in *Gene Hamon*, “Section 4.06(c) [predecessor to Tex. Occupations Code 2301.652] does not require an applicant to supply this information, and we reject McDavid’s argument that harm to the protestant cannot be calculated in its absence.” *Id.*⁵¹

The *Landmark* PFD, on which MB of Austin relies exclusively for the breakeven concept, did not hold it is a requirement that an applicant prove its breakeven point, as MB of Austin asserts throughout its Brief. While the *Landmark* PFD notes that the registration shortfall in 1992 was “well under the number of units [the Applicant] needs to break even,” (PFD at 35), there is no analysis of “breakeven,” no indication of what evidence was in the record regarding it, other than simply the number of new units the applicant suggested it might sell and GM’s planning volume. See PFD at 31-35. Beyond one or two references to “breakeven,” the entirety of this section of the *Landmark* PFD deals with the profitability of the existing dealer, which is not a problem in this case. See *also Landmark*, Findings of Fact, PFD at 47, ¶ 37, at 68, ¶ 247, and at 71, ¶ 278

⁵¹ McDavid even challenged that a breakeven analysis was required to be submitted to the agency under other sections of the former statute. The Third Court disagreed stating, “[t]he Board does not read section 4.02(a) to permit a protestant to challenge the adequacy of the economic information provided by a dealer seeking relocation.” *Gene Hamon*, 997 S.W. 2d at 305.

(mentioning only applicant's anticipated sales and GM's planning potential, as compared to the lost sales opportunity, discussed immediately below).

The facts in *Landmark* are very different, which may explain the PFD's reference to a breakeven point. Under the benchmark the Board adopted to assess lost opportunity in the Houston market,⁵² there was little lost opportunity, 336 units, when the applicant apparently said it needed 1200 to 1500 new vehicle sales to breakeven, and GM's planning volume was 2296, in a rapidly declining market for GM vehicles.⁵³ Second, the protesting Landmark dealership had very low profitability across all departments and its gross profit per new unit sale was lower than the average for Houston or national dealers.⁵⁴ Neither is true as to MB of Austin, which is highly profitable, particularly in its used, service, parts and body shop departments, and has a higher gross profit per new vehicle sold than the composite groups.⁵⁵

Notably, the Third Court of Appeals in the *Landmark* case merely mentioned "breakeven" once, and only in summarizing the Board's findings; that concept did not form any part of its analysis on appeal. *Austin Chevrolet*, 212 S.W.3d at 437.

Consequently, there is no precedent, or even persuasive authority, that requires an

⁵² The Board and the Third Court of Appeals in *Austin Chevrolet* held the Texas benchmark inappropriate to evaluate lost opportunity in Houston, by far the largest multi-point market in the state, where 249 of Chevrolet's 259 dealers in Texas at the time were single point markets. *Austin Chevrolet*, 212 S.W.3d at 436. In contrast, more than half of Mercedes dealers in Texas are in metro multi-point markets. See Ex. I-65 at 27-31 (17 of the 30 Texas Mercedes dealers are in multi-point markets of Austin, Dallas, Houston and San Antonio). More important, MB of Austin has not at all questioned the national or Texas state benchmarks Mr. Farhat used in his analysis.

⁵³ See *Landmark* PFD that MB of Austin quotes at 36 of its Exceptions, and Findings 37 and 208-209; *Austin Chevrolet*, 212 S.W.3d at 433.

⁵⁴ *Landmark Chevrolet v. General Motors Corp.*, Docket No. 02-0002 LIC (Tex, DMV, MVD, Dec. 9, 2004), *adopting* Proposal for Decision (Sept. 16, 2004) at 28, 32.

⁵⁵ See summary of Heinemann testimony, MBUSA's Opening Brief at 77-78 (general profitability and balance sheet indicators) and 79-82 (profitability of departments other than new vehicle and higher average gross profit per new vehicle sold).

applicant to provide evidence of what its breakeven point would be, and in particular, no support for the assertion that to prevail in a protest the applicant must provide evidence of its profits and expenses, pro formas, and the like. Given that *Landmark* is the only decision that even references “breakeven,” Swickard and MBUSA have provided the information that case noted (on potential sales), even assuming it were required. The ALJs correctly found MB Austin did not show why Swickard’s “breakeven number” is necessary to show that MB Austin will not be harmed, particularly when the evidence established that sufficient opportunity exists in the market to sustain the proposed dealership. See PFD at 59, 62-64, and 74; FOF 142.

Second, the concept that lost opportunity must cover an applicant’s projected sales or else “cannibalize” existing dealers’ sales incorrectly assumes a “fixed pie” of sales for a brand in a given market, frozen in time by the evaluation year. Here the latest evaluation year was using 2018 data. The undisputed data in this case from other markets demonstrates that a fixed pie is not reality. Registration effectiveness from the evaluation year (the “fixed pie” number) and absolute sales in various markets have increased after the addition of a new dealer, not only for markets where Mercedes Benz dealers have been added in Texas, but also for BMW in the Austin metro.⁵⁶ Even Mr. Stockton estimated that there will be a 5% or so increase in registrations likely with the addition of a new dealer based on his review of similar data in other markets.⁵⁷ The fixed pie concept also assumes, erroneously, that additional opportunity will not result from the undisputed continued anticipated growth in the Austin metro population and

⁵⁶ See Farhat analysis and testimony at 72-74 of MBUSA’s Opening Brief and Section VII.C.1 of its Closing Brief.

⁵⁷ Stockton: Tr. 11/19/19, 993:20-25.

economy, which is unlike the decade-long declining circumstances in the Houston market that was present in *Austin Chevrolet*, noted above.⁵⁸ Cf. *Grubbs Nissan*, 2007 WL 1518115 at *7; PFD at 22,. MB of Austin's reliance on either "breakeven" and "fixed pie" concepts have no place in the Board's analysis in this case.

Third, that the 1984 decision in *Lee Trevino* suggested the Board must make sure that both the existing and additional dealers will be profitable after an establishment does not provide any support for MB of Austin's argument that MBUSA and Swickard must actually prove Swickard's sales, revenues, debt and the like, particularly with his intent to focus on entry-level vehicle sales. In any event, *Lee Trevino* is distinguishable and not dispositive.⁵⁹

There is absolutely no question that MB of Austin will remain profitable, even if it lost a significant number of new vehicles sales, which it will not.⁶⁰ Also, the sales projections MB of Austin complains exceed the 2018 lost opportunity are not inconsistent with the 500 to 700 sales Mr. Farhat estimated the Swickard dealership likely would have achieved, had it opened in 2018. That range of likely 2018 sales were based on the sales profiles of both MB of Austin and MB of Georgetown, as the ALJs expressly stated in Finding of Fact 165. The estimate Mr. Swickard's organization

⁵⁸ Even Mr. Stockton agreed that among bigger cities, Austin is the fastest growing city in the country. Tr. 11/19/19, 1010:19-24 (looking at 2017-2018 data). Cite to Ex. P-1 at 67?

⁵⁹ See Exceptions, ¶3 and throughout the brief citing *Lee Trevino Ford v. Payton Ford Sales, Inc.*, Docket No. 302, Proposal for Decision at 29 and 74 (Jan. 30, 1984). In *Lee Trevino*, Ford's market share in the relevant market and in Fort Worth was consistently way above Ford's national share for over ten years, even though declining (PFD at 15 and 30); in the prior five years, the whole car industry suffered "severe declines" in the throes of national recession (at 18 and 29); in the 1982-evaluation year, Ford would only have needed 9 cars and 12 light trucks to meet national benchmark (at 22); the closest Ford dealer had not been profitable at all for three to four years (at 33); and increased convenience would be minimal, as the three closest Ford dealers were within 12- and 15-minute drives of the proposed site (at 34).

⁶⁰ See Section VI below, on MB of Austin's highly profitable dealership, and in particular the fact it is not reliant on its new vehicle sales volume for its profitability.

identified in its Preliminary Projections (Ex. A-2) of 775 new vehicles in its first year of operations is three to four years down the road, not what it would have done in 2018, per Mr. Farhat's analysis. Even assuming it were relevant, the planning volume MB of Austin points to (in Ex. I-42) of 916 new vehicle sales on its face is for five years from 2019, when that analysis was prepared, to 2023, the "Planning Year."⁶¹ The incredible growth trajectory Austin was on in population, high paying jobs, high income households, and other factors that Dr. Nivin opined about, without dispute, will continue by 2023 or 2025, after the economic downturn recovers.⁶² Consequently, both Mr. Swickard's estimates and MBUSA's planning volume are not at all unreasonable that far down the road, or inconsistent with the 2018 snapshot of then available lost opportunity.

The fact that Mr. Swickard intends to focus on generating new business from entry-level vehicle customers also is not a barrier to Mr. Swickard's profitability, as MB of Austin contends due to its perception of their lack of profitable margins or that a large volume of entry-level vehicle sales "are not realistically available to the proposed dealership."⁶³ Both of these assumptions are flawed, based on Mr. Swickard's own success with that business model recently in Wilsonville, a suburb of Portland, and the actual registrations in the entry-level segments in Austin by MBUSA's competitors. Mr. Swickard testified at length on how he turned around a failing dealership in Wilsonville, focusing on entry-level sales. Mr. Swickard bought his first dealership—Mercedes-Benz of Wilsonville—in 2014, after a successful career as an entrepreneur.⁶⁴ Mr. Swickard

⁶¹ See also Mr. Newcomb's testimony at Tr. 291:12-293:15.

⁶² See testimony and findings on the effect of any recession in 2020 and Austin's likely ability to rebound quicker than other areas of Texas and the nation, in Section II above.

⁶³ See, e.g., Exception 23.

⁶⁴ Tr. 11/12/19, 52:25-54:21.

was able to quickly turn around not just that poor performing dealership, but the entire Portland metro market to the benefit of the other two Mercedes-Benz dealerships and the Mercedes-Benz brand.⁶⁵ Mr. Swickard attributes his dealership's and the market's success to a number of factors, which he intends to apply to his dealership in South Austin, including aggressively marketing to and attracting entry-level luxury customers who never bought Mercedes-Benz vehicles before, among other factors that propelled his success.⁶⁶ Many dealers build successful dealerships on high volume, low margin vehicle sales, which MB of Austin apparently disdains and instead chooses to sell fewer, but higher gross profit vehicles. Mr. Swickard's success in Wilsonville is not an anomaly, but a business model he can repeat in Austin.

Despite MB of Austin's argument that it sold 20% of its total new vehicle sales in the entry-level vehicle segments in 2018 and 17% in 2017, there is still a very substantial portion of entry-level vehicles that its competitors are selling in the Austin AOR and, more important, that Mercedes-Benz dealers outside the AOR are selling to AOR residents, i.e., insell or "pump-ins." Considering that MBUSA sells scores of vehicle models,⁶⁷ 204 lost to competitors in the entry-level segment in just the first six months of 2019 is significant. And it is rising; 114 lost through May 2019 translates into 276 for the year. Insell of Mercedes-Benz entry-level vehicles by dealers outside the AOR is even more significant—as Mr. Gomez testified, the #1 'pump-in,' or insell, model into the Austin AOI is the GLC, the entry-level SUV, and #2 is C-Class, entry-level sedans, demonstrating that there is much additional appetite for entry-level vehicles in

⁶⁵ Tr. 11/12/19, 61:5-18, 102:1-103:20.

⁶⁶ Tr. 11/19/19, 1090:22-1092:23.

⁶⁷ Ex. I-65 at 38.

the Austin AOR.⁶⁸ Competitor sales and insell of vehicles in these segments are certainly opportunity Mr. Swickard can capture by implementing his already successful business model in Austin. That is yet another reason that Swickard's new dealership will not "cannibalize" MB of Austin's new vehicle sales because Mr. Swickard will focus on sales that Mr. Hardeman testified he has no interest in making, without regard to what the 2018 lost opportunity was.⁶⁹

The ALJs also correctly found (in FOF 142) that detailed operating expenses, revenue projections and other financial projections from Swickard were not necessary, whether to MBUSA or on the purported "breakeven" issue. Again, MB of Austin's only authority for arguing the Board needs this information is the *Landmark* PFD, and in particular cites it for the proposition that without that evidence "the Board rightly assumes that cannibalization of sales will ensue if the applicant is licensed." Exceptions at 28. Again, all the *Landmark* PFD referred to was the applicant's anticipated sales and in one spot GM's planning volume, which was so disproportionate, and many multiples above what the ALJ there found the lost opportunity to be; it referenced no other evidence on the issue.

Finally, and perhaps most telling, MB of Austin's expert for possible harm to MB of Austin, Edward Stockton, did not opine that he could not fully assess potential harm to MB of Austin without knowing Swickard's breakeven point. When assessing harm to MB of Austin, Mr. Stockton apparently did not care how many sales Mr. Swickard needs

⁶⁸ Gomez: Tr. 11/20/19, 1078:2-23.

⁶⁹ See, e.g., PFD at 7 (MBUSA is being undersold by all competitors in particular in entry-level luxury vehicles, like the C-class and GLC); 11 (Hardeman prefers to sell high-end vehicles rather than entry-level due to higher margins); 51 and 61 (since BMW of South Austin opened in mid-2018, MB of Austin registered only 330 entry-level vehicles versus 925 by BMW, 912 by Lexus, and 665 by Audi) and FOF 30, 31, 72, 97, 107, 149, and 160.

to breakeven, or even how many sales Mr. Stockton claims he will make. The “breakeven” concept is something MB of Austin concocted from its reading of the *Landmark* PFD, but which it failed to note any analysis in that case of the concept, or the complete lack of mention of breakeven evidence or required proof in the appellate decision of that case, *Austin Chevrolet*, in its discussion of harm to the existing dealer under the fourth factor, or any other factor. Any purported proof of “breakeven” is therefore irrelevant, and every single exception that relies on it should be rejected.

C. The ALJs Correctly Found Testimony About Swickard’s Plans and Past Business Model Successes Sufficient to Rebut the Contention that Proof of “Breakeven” Evidence or Otherwise was Required⁷⁰

The ALJs made 15 separate factual findings concerning Mr. Swickard’s background, his success in turning around both the Wilsonville dealership and the Portland market as a whole, and his intent to use that model in South Austin. See FOF 87-101. Those findings are amply supported by the undisputed testimony by both Mr. Swickard and Fred Newcomb, MBUSA’s former Manager of Dealer Network, about Mr. Swickard’s dealership successes.⁷¹ MB of Austin does not submit any exceptions to any of those findings.

Mr. Swickard testified even more extensively to his business plan that led to his Wilsonville success than are captured in the ALJs’ findings: marketing to and attracting entry-level luxury customers who never bought Mercedes-Benz vehicles before;⁷²

⁷⁰ See Exceptions, ¶¶ 6, 18, 23 (discussed in the preceding section), and 50 and simply referenced throughout without further analysis or argument.

⁷¹ See, generally Tr. 11/12/19, 54:18-21, 59-72, 101-103, 112-114, and 11/13/19, 284-288.

⁷² Tr. 11/12/19, 59:4-23, 62:10-15 (noting that 70% of vehicle trade-ins of new customers are of non-Mercedes-Benz brands).

marketing nearly new ex-service loaner cars to similar entry-level luxury consumers;⁷³ growth in the service department based on customer loyalty;⁷⁴ providing a superior customer experience, what Mr. Swickard described as “ceremonial,” “comfortable,” and a “place of joy” for customers;⁷⁵ and which he attributes to his hiring staff outside of the auto industry and his unique employee training (e.g., through Ritz-Carlton Hotel hospitality consultants) that first makes his dealership his “employees’ favorite” place to work.⁷⁶ Mr. Swickard also attributes his success in Wilsonville, and that of the other Mercedes-Benz dealers in that market, to the “harmonious relationship” he has with those dealers.⁷⁷ It likely was his and his team’s harmonious relationship with the surrounding Mercedes-Benz dealers that led to their and other regional Mercedes-Benz dealers’ nomination of Mr. Swickard to represent them on the MBUSA National Dealer Board two years ago, and his more recent election by his national dealer peers to be the Chair of the Board.⁷⁸

It is precisely because of Mr. Swickard’s phenomenal turnaround success in Wilsonville, his appointment by his dealer peers to the MBUSA’s National Dealer Board (and recent election to national chair), and the then very recent application in connection with his purchase of another Mercedes-Benz dealership in Atlanta that MBUSA did not need an application, business plan, construction plans, or any of the other items MB of Austin complains are not in the record at the time MBUSA offered Mr.

⁷³ Tr. 11/12/19, 59:24-60:17, 129:7-130:11.

⁷⁴ Tr. 11/12/19, 61:19-62:6.

⁷⁵ Tr. 11/12/19, 68:19-69:13.

⁷⁶ Tr. 11/12/19, 68:14-69:13, 93:1-94:13.

⁷⁷ Tr. 11/12/19, 102:1-103:20.

⁷⁸ Tr. 11/12/19, 104:13-105:22; Tr. 11/13/19, 286:25-288:21 (Newcomb on description and importance of Dealer Board).

Swickard the South Austin dealership opportunity, in addition to this pending protest.⁷⁹ Again, MBUSA proved why these items were not necessary; MB of Austin failed to rebut it, which is why the ALJs correctly stated (PFD at 62) MB of Austin did not show the contrary and properly found MBUSA did not need these items (FOF 142).⁸⁰

MB of Austin's contention that the "Code also directs the Board to consider the 'financial expectations' of the proposed new dealership" also does not support its position. Exception 6 at 15. The only place "financial expectations" appears in the Occupations Code is in the middle of the seventh statutory factor, without more. No previous Board or appellate cases discuss this portion of the seventh factor separate and apart from the economic and other market growth projections on which Dr. Nivin opined. To the extent it does mean the financial expectations of the establishing dealer, Mr. Swickard testified he "can't imagine running a Mercedes-Benz franchise in Austin, Texas and not being extraordinarily profitable," although profitability is not his primary motivation.⁸¹ In his view, based on his firsthand knowledge of living in the city, Austin is "hungry" for luxury vehicles, and if "you get the other formula right in the business of treating customers well, . . . profit just seems to follow."⁸² His informed expectation is that he will own a profitable Mercedes-Benz dealership in South Austin, similar to the other Mercedes-Benz dealerships he owns, and has no financial concerns.⁸³ His

⁷⁹ Tr. 11/13/19, 284:10-285:10, 330:18-331:17, 400:14-401:19.

⁸⁰ MBUSA discussed Exception 23 regarding FOF 149 in Section II.B. above, concerning Swickard's marketing to entry-level customers, which MB of Austin's competitors are outselling Mercedes-Benz in the Austin market.

⁸¹ Tr. 11/12/19, 96:4-14.

⁸² Tr. 11/12/19, 96:15-97:18.

⁸³ *Id.*

successful business model, discussed in Section III.B. above, should put this issue to bed.⁸⁴

Finally, MB of Austin's attack on Dr. Nivin's analysis of the economic benefits of a new dealership, directly in terms of new dealership employment, local and state sales taxes from vehicle and parts sales, and construction-related employment and supplier opportunities, as well as the downstream benefits to local businesses from the new dealership, is not "speculative." Exception 50, attacking FOF 195, 199, and 201. As noted above, Dr. Nivin is a PhD economist, an associate professor of economics at Saint Mary's University in San Antonio, and Chair of its Economics Department. He also has a consulting practice and runs a think-tank at the University that focuses on regional economic issues.⁸⁵ Dr. Niven previously worked for two corporations as a political economist, and for many years with the City of San Antonio in economic development and became its Chief Economist.⁸⁶ Among his other experience, Dr. Nivin performed over 150 economic impact studies of all shapes and sizes, both as Chief Economist for the City of San Antonio and in his current consulting practice, ranging from the impact of conventions, various private development and public projects, new businesses, including the impact of a new Toyota manufacturing facility which assisted city policy

⁸⁴ MBUSA takes issue with MB of Austin's characterization of the appellate decision in *Austin Chevrolet*. See Exception 18 at 29. Nowhere did the Third Court of Appeals say, or imply, that destructive competition would result if the lost opportunity is "insufficient for [the new dealer] to be profitable." *Id.* Rather, the court reinforced the Board's ruling, and that of two 1981 cases of the standard MBUSA reiterated, and that the ALJs also adopted, that it would not be in the public interest if the establishment would result in "the failure of an existing dealer or the reduction of [its] service to the public." *Austin Chevrolet*, 212 S.W.3d at 434.

⁸⁵ Tr. 11/12/19, 149:12-17.

⁸⁶ Tr. 11/12/19, 150:13-23; Ex. I-71 at pp. 49-70.

makers to devise appropriate incentive packages to attract Toyota and other businesses to San Antonio.⁸⁷

Just as in virtually all of the many other economic impact analyses he has performed, Dr. Nivin looked at the impact of a new dealership regarding the construction of the facilities and then the economic impact of its operations on an annual basis, using a well-regarded and widely-used software package to model the impacts, to arrive at the direct impact and multiplier ripple effects through the local economy.⁸⁸ For the dealership operations component, he used a composite of the dealer financial statements of six Mercedes-Benz dealerships in Texas with annual new vehicle sales of 500 to 700 vehicles in 2018, provided by Ms. Heinemann (a subset of all dealers in her geographic Area D Texas dealer composite that had annual new vehicle sales in 2018 of 500 to 700).⁸⁹ Dr. Nivin's use of financial information of dealers with that range of new vehicle sales was based on Mr. Farhat's range of what a new South Austin dealer's new vehicle sales would have been if it had performed like MB of Georgetown and MB of Austin, respectively, in 2018.⁹⁰ His estimates of the number of employees and the like were premised on that composite data and his sophisticated software analytics. There was absolutely nothing "speculative" about his analysis.

MB of Austin's exceptions on all of these issues should be rejected, as well as each of its proposed bullet-point alternative findings in ¶ 6 of its Exceptions.

⁸⁷ Tr. 11/12/19, 151:23-152:22, 190:4-191:10.

⁸⁸ Tr. 11/12/19, 152:23-154:11.

⁸⁹ Tr. 11/12/19, 191:25-192:21; Tr. 11/15/19, 727:9-730:8; Heinemann report, Ex. I-69 at 109-110.

⁹⁰ Tr. 11/14/19, 506:13-509:17; Ex. I-65 at pp. 98-99. Had Dr. Nivin used the Swickard organization's higher anticipated new sales volumes (Ex. A-2), his analyses in this section would have reflected much higher dollar impacts. Tr. 11/12/19, 206:14-207:6, 218:3-18.

IV. THE ALJs CORRECTLY FOUND LOST SERVICE OPPORTUNITY EXISTS FOR SWICKARD TO CAPTURE⁹¹

A. The SOI Reports Reflect Significant Lost Service Opportunity in the Austin AOI

Service opportunity is reflected in the Service Opportunity Index (“SOI”) reports in evidence, which reveal the large volume of Un-Serviced VINs of the Mercedes-Benz vehicle owners residing in the AOI of MB of Austin, and the expected revenue from those Un-Serviced VINs that MB of Austin and other Mercedes-Benz dealers are leaving on the table. Those Un-Serviced VINs constitute the untapped service opportunity in the Austin AOI—opportunity that a new dealer can capture without harming MB of Austin’s robust and already overcapacity service department, or that MB of Austin can capture to continue its extraordinary service profitability. As the ALJs found, there is a large number of Un-Serviced VINs, and millions of dollars of revenue opportunity reflected in each of those reports.

MB of Austin primarily complains that the ALJs’ findings based only on the December 2018 SOI Report, rather than the 2019 reports in evidence, is “stale” and “outdated.”⁹² While the Austin AOI did improve some in the 2019 reports cited, this lagging behind trend still continued through April in the most comparable categories—Area D, Market 12 and Market Tier (metro AOIs).⁹³ MB of Austin’s argument also belies the very significant fact that even when the September 2019 report showed increased

⁹¹ Exceptions, ¶¶ 2 (at 6), 8, 9, 13, 14, 27-30.

⁹² MB of Austin complains throughout that the ALJs’ refusal to consider SOI reports after the December 2018 report is “unexplained” and “mystifying.” *E.g.*, Exception ¶2 at 6. It is not. The ALJs in fact discussed the trends from the 2019 reports (PFD at 16). The fact that they also chose to discuss the December 2018 report, which had similar dollar amounts on lost service value, does not change the fact that this market has plenty of service opportunity for MB of Austin, MB of Georgetown, and MB of South Austin.

⁹³ See MB of Austin’s table at 23 of its Brief.

percent scores compared to the different geographical averages over the prior reports, the number of Un-Serviced VINs in the AOI actually increased— from 3,939 in June 2019 to 4,039 in September 2019 and a value of \$5.5 million in service business lost to independents⁹⁴—and showed little improvement from December 2018, when the Un-Serviced VINs were 4,615, at a lost service value of \$5.7 million.⁹⁵

As Mr. Hoefl explained, and the ALJs found,⁹⁶ the effect of this lost service opportunity goes far beyond just the numbers of Un-Serviced VINs; it is the opportunity dealers have to develop long-term relationships with Mercedes-Benz vehicle purchasers through routinely servicing their vehicles. Perhaps most important is a dealer's developing a service relationship with buyers of entry-level luxury vehicles, like the C, GLC and GLK model vehicles, who are usually first-time buyers of Mercedes-Benz cars and SUVs. As Mr. Hoefl explained, entry-level luxury customers typically are younger, at the start of their careers, and the exact customers that MBUSA wants, through servicing their vehicles, to experience the brand and grow with it to more expensive vehicles as they grow in their careers.⁹⁷ Further, MB of Austin's proposed finding (Exception 2 at 9) that younger owners of entry-level models often "prefer" to take their vehicles to independents is wholly unsupported by any evidence, including the testimony cited. All

⁹⁴ Ex. P-29 (June 2019 Un-Serviced VINs=3939), Ex. P-61 (September Un-Serviced VINs=4039).

⁹⁵ Ex. I-26.

⁹⁶ See PFD, FOF 39-41 and discussion at 13-14.

⁹⁷ See also 11/20/19, 1372:14-1373:4 (Hardeman testifying that MB of Austin does not sell many entry-level luxury vehicles because of the low margins, but acknowledged both that there is profit to be made in their service work and that the hope is to catch younger buyers for Mercedes-Benz and move them up as their income increases); Tr. 11/21/19, 1517:24-1518:2 (Mr. Opinker testifying that he is more likely to get service business from people who have owned several Mercedes-Benz vehicles than younger, entry-level luxury customers).

Mr. Hoefl testified is that younger owners are going to independents⁹⁸—an indictment on MB of Austin’s failure to adequately serve the market as to service. Importantly, Mr. Hoefl also testified that to get those entry-level owners into MB of Austin or other Mercedes dealers takes advertising and a targeted marketing campaign, which he also testified, and the ALJs found, MB of Austin refuses to do at all for its service operations.⁹⁹

Also throughout its exceptions, MB of Austin contends that it is enough to note that by the September 2019 SOI report, Mercedes dealers are meeting the average coverage in the Austin AOI against the various geographical benchmarks of about 70%, and therefore there is zero lost opportunity. As with lost sales opportunity, just meeting the average does not demonstrate there is no opportunity available. This 70% is just the average of all AOIs in the geography to which it is compared at that moment in time, much like 100% registration effectiveness is just a “C” average; it is a threshold, not a ceiling, and many AOIs had to have achieved substantially above 70% Serviced VINs such that the average would be that 70%, much like Mr. Farhat demonstrated many Texas AOIs perform above 100% RE, just as BMW has in 2018 and 2019 after it opened BMW of South Austin.¹⁰⁰ What distinguishes lost service opportunity from lost sales opportunity, however, is the incredible number of Un-Serviced VINs and dollar

⁹⁸ See Tr. 11/15/19, 855:9-22 and 859:1-860:4. There could be any number of reasons, than they “prefer” to—long wait times for dealer service, inconvenient brand dealer locations, poor customer service, among any number of other dealer-specific reasons. Further, MB of Austin’s slams of Mr. Hoefl’s credibility and oral testimony as purportedly “without support” are completely unwarranted. First, oral testimony is evidence, and which MB of Austin did not rebut. Second, the ALJs are in the best position to judge every witnesses’ credibility, and they clearly deemed Mr. Hoefl as credible given their reliance on Mr. Hoefl’s testimony in the PFD.

⁹⁹ See Tr. 11/15/19, 855:9-22, 859:1-861:7, part of which MB of Austin cites, and PFD, FOF 41. See also Tr. 11/15/19, 862:3-13.

¹⁰⁰ See Farhat Reports, Ex. I-65 at 42; Ex. I-67 at 14-15.

values that we know is being lost to independent shops and that indicates there is significant lost service opportunity in the Austin AOI, whether its 4,039 VINs in September 2019 and a value of \$5.5 million in service business lost or 4,615 at a lost service value of \$5.7 million in December 2018.

MB of Austin also ignores the fact that with additional sales by the Swickard dealership, additional VINs will be added to the current Austin AOI. Those additional vehicle sales necessarily will increase the service opportunities.

Finally, MB of Austin also refers to Mr. Hardeman's speculation that, over time, his service business will be lost to the new dealer, based only on his anecdotal testimony about what happened when MB of Georgetown moved to its current site 16 years ago, and notably in the midst of a recession in 2004. There are two issues with that testimony. First, it directly contradicts his deposition testimony, with which he was impeached during the hearing, where he admitted he would not lose any service when the new dealer opens.¹⁰¹ Mr. Hardeman also admitted he's not afraid of competition from the South Austin dealership in service.¹⁰² And even more telling was Mr. Hardeman's testimony that he thinks he will capture more service business if South Austin opens from owners that buy a car from the new dealer but live closer to MB of Austin.¹⁰³ In fact, Mr. Hardeman admitted his dealership's inadequate service representation, and that there is more service opportunity in the AOI when he told his expert witness, Edward Stockton, that he desired to open a service satellite facility in

¹⁰¹ Tr. 11/20/19, 1389:14-1390:6, 1393:11-1394:8.

¹⁰² Tr. 11/20/19, 1393:20-1394:6, 1394:13-1395:13.

¹⁰³ Tr. 11/20/19, 1384:3-20.

southwest Austin, that it would be beneficial to him.¹⁰⁴ Obviously, Mr. Hardeman's admissions belie all of MB of Austin's arguments throughout its exceptions that no lost service opportunity exists. All of MB of Austin's exceptions regarding lost service opportunity should be rejected.¹⁰⁵

B. MB of Austin's Remaining Service-Related Arguments Go to the Adequacy of Service in the Austin AOI

In the paragraphs of its exceptions (listed in footnote 91 above), MB of Austin also argues against the ALJs' findings regarding its construction of additional service bays, intent to hire more technicians, Mercedes-Benz product issues, and MBUSA's parts delays. These issues go more to the adequacy of MB of Austin's service and are discussed in Section V.B. below.

V. THE ALJs CORRECTLY FOUND THE AUSTIN AOR IS NOT ADEQUATELY REPRESENTED IN TERMS OF SALES, SERVICE CAPACITY, AND FACILITIES

A. The Mercedes-Benz Brand Has Not Been Adequately Represented as to New Vehicle Sales in the Austin AOR or Austin AOI for Years¹⁰⁶

The performance of a brand, like Mercedes-Benz, in an individual AOI or in a metro AOR is measured by registration effectiveness, which is the percent of the actual number of Mercedes-Benz vehicles registered in a given geography (regardless of what dealer sold those resident consumers their vehicles) against an expected number under a given standard or benchmark of a larger geography. PFD at 27. Registration effectiveness is a nationally recognized standard in the industry for evaluating the

¹⁰⁴ Tr. 11/19/19, 1012:11-1013:21.

¹⁰⁵ There are portions of Finding of Fact 38 (Exceptions, ¶ 9) and 122 (Exceptions, ¶ 13) that should be revised, the first regarding the calculation of how many vehicles MB of Austin, versus other Mercedes-Benz dealers serviced per Ex. I-26, the December 2018 SOI Report, and the second that simply refers to MB of Austin instead of Mercedes-Benz dealers, both of which are addressed in Section IX of this reply.

¹⁰⁶ See Exceptions, ¶ 17.

adequacy of a brand's performance. *Id.* Achieving 100% registration effectiveness is merely average; anything under 100% reflects inadequate representation in a market.

Id.

As the ALJs found, in 2018 alone, the Austin AOR achieved only 78.8% against the national average benchmark, or 1581 actual registrations divided by 2006 new vehicle registrations expected. *Id.* As Mr. Farhat testified, since at least 2014, the proposed South Austin AOI, the Austin AOI, and the entire Austin AOR have been consistently below 100% registration effectiveness against both the national and Texas benchmarks. Between 2014 and 2016, against the national benchmark, the South Austin AOI, had it been carved out of the Austin AOI in those years, was in the mid-70% registration effectiveness, jumped a bit in 2017 to 84% registration effectiveness, and then declined below 70% in 2018 to 69% registration effectiveness.¹⁰⁷ In its current geography (without carving out South Austin AOI), the Austin AOI was at 76.5% registration effectiveness in 2014, and 75.6% registration effectiveness in 2018.¹⁰⁸ The entire Austin AOR (including Georgetown) performed a bit better, buoyed by the Georgetown AOI's consistently better registration effectiveness performance,¹⁰⁹ at 82.3% registration effectiveness in 2014, increasing to 93.2% registration effectiveness in 2017, but then dropping more than 14 points to 78.8% in 2018.¹¹⁰ As the ALJs also

¹⁰⁷ Tr. 11/14/19, 458:14-460:6; Ex. I-65 at 45.

¹⁰⁸ Tr. 11/14/19, 463:9-465:6; Ex. I-66 at 215, 219. The Austin AOI (MB of Austin's AOI with South Austin carved out) performed only slightly better, in the higher 70s registration effectiveness% for 2014 and 2015, in the mid 80% registration effectiveness in 2016 and 2017, but then a sharp decline to 79% in 2018. Tr. 11/14/19, 462:6-463:8; Ex. I-65 at 46.

¹⁰⁹ Tr. 11/14/19, 470:5-471:18; Ex. I-65 at 53 (Georgetown AOI – exceeded 100% RE in four of the five years at Texas and Southern Region benchmarks, and three of those years at national, but below 100% in 2018).

¹¹⁰ Tr. 11/14/19, 466:7-22; Ex. I-65 at 47.

found, in 2018, the Austin AOI ranked 10th out of 10 in registration effectiveness among the ten dealers in Market 12. See PFD, FOF 104. And it is only getting worse since BMW opened its South Austin dealership in 2018. See PFD, FOF 105 and 117.¹¹¹ That's consistently inadequate representation going back several years no matter how it is sliced.

Neither Mr. Stockton nor Mr. Hatch disputed the efficacy of the registration effectiveness measure, Mr. Farhat's use of a national or Texas average as the benchmark to compare the Austin market's performance, or that 100% registration effectiveness is merely average performance in a given market.

Nor does MB of Austin challenge any of the findings of fact related to the adequacy of sales representation in the Austin market. See PFD, FOF 102-120. All they challenge is the ultimate finding (in FOF 130) that the Mercedes-Benz brand is not adequately represented as to sales.¹¹² To get there, MB of Austin improperly conflates adequacy of representation in the first statutory factor, discussed here, with the wholly separate issue under the fourth factor of lost opportunity, discussed in Section III above. See Exceptions, ¶ 17 at 26-27. The undisputed evidence, particularly the analysis

¹¹¹ As Mr. Farhat explained, competitive retail luxury vehicle registrations in the South Austin AOI increased in 2018, and at a higher percentage than in the Austin AOR. That competitive retail registrations in the South Austin AOI increased in 2018, and at a higher percentage than in the Austin AOR, at the same time the Mercedes-Benz brand's registration effectiveness fell sharply between 2017 and 2018. That disconnect is largely due to the opening of the new BMW dealership up the road from the Swickard's proposed site and its increased registration effectiveness from the mid-80% in 2017 to 102% in 2018. Tr. 11/14/19, 484:7-485:7; Ex. I-65 at 59-61.

¹¹² The one exception is Finding of Fact 121 regarding Farhat's "share of franchise" analysis, which is one component of his "likely causes" opinions that explain a given market's consistent sales underperformance. See Exception 12. MB of Austin, however, apparently misunderstands that analysis. The purpose of the analysis is not to compare how many dealers Mercedes-Benz has in a market to any other single luxury brand, like BMW or Audi. Rather, it demonstrates how many Mercedes-Benz dealers are appropriate and needed to meet the total number of competitive dealers in that market, consistent with its share of franchises both nationally and in Texas. Mr. Farhat's analysis found, as did the ALJs, that there should be three Mercedes-Benz dealers in the Austin AOR to meet the average in all Texas and national markets. See MBUSA's Opening Brief at 36-37.

performed by Mr. Farhat, wholly supports that the Mercedes-Benz brand is not adequately represented anywhere in the Austin metro area.

B. MB of Austin's Lack of Service Capacity Renders its Service Representation Inadequate¹¹³

MBUSA has already discussed above in Section IV the lost service opportunity in the Austin AOI, as measured largely by the SOI Reports in evidence. It is against that backdrop that it addresses here why MB of Austin, along with other Mercedes-Benz dealers, are not capturing more of the service opportunity that clearly exists in the Austin AOI.

Contrary to its contentions, every finding MB of Austin challenges on this topic—Findings of Fact 41 (MB of Austin's failure to do service advertising), 44 (service area's lack of air conditioning), 125 (long wait times as evidence it is over-capacity) and 126 (new service bays being constructed will not solve capacity issues)—are supported by the evidence.

Wait times for service impacts the adequacy of service, for both warranty and non-warranty work. Wait times at MB of Austin are as long as ten days or more, per Mr. Hoefl; per MB of Austin's service director Mr. Opinker, wait times are up to seven to nine days.¹¹⁴ Having customers wait longer than a week is unacceptable.¹¹⁵

¹¹³ See Exceptions, ¶¶10, 11, end of 13, and 14. MBUSA also notes that Exception 11 is based on what MB of Austin terms "the unreliable testimony of MBUSA employee, Fred [sic] Hoefl." Not only was Mr. Ed Hoefl a credible and reliable witness, there is a certain irony of MB of Austin unreliably identifying a witness it claims, without basis, to be unreliable.

¹¹⁴ Tr. 11/15/19, 862:14-864:6; Tr. 11/21/19, 1454:20-1454:24. See also Hatch testimony, Tr. 11/20/19, 1234:22-1236:5 (where consumers have long wait times for service, customers may buy a different brand on their next vehicle purchase).

¹¹⁵ Tr. 11/15/19, 862:14-25.

It is precisely because of those long wait times that MB of Austin's service management refuses to advertise. As Mr. Hoefl testified, MBUSA has several marketing and advertising tools available to its dealers to increase their service business, on which Mr. Hoefl counsels his dealers. MB of Austin has resisted Mr. Hoefl's counseling, even though it knows there is significant service opportunity it is not capturing in its own AOI; and, alarmingly, one reason MB of Austin's management has given for resisting Mr. Hoefl's suggestions is that their service department is already at full capacity, and any additional customers would further increase customer wait times for repair of their vehicles.¹¹⁶ That is, it cannot handle the available service business actually coming to its facility.

Factors contributing to those long wait times include MB of Austin's inability to retain enough technicians, having lost, for example, about 20% in the summer of 2019.¹¹⁷ Mr. Opinker, MB of Austin's Service Director, admitted that if MB of Austin had six to eight more technicians, it could perform better service to its service customers and take in more service work.¹¹⁸ Losing technicians is perhaps due to the lack of air conditioning in MB of Austin's service department, which all but two of Mr. Hoefl's ten dealers have (the other being MB of San Juan, that Mr. Hardeman recently purchased). MB of Austin admits that the service shop gets to 85 or more degrees in the summer, as the ALJs found.¹¹⁹ Whether or not the lack of air conditioning is why MB of Austin lost so many technicians last summer, the fact remains its shop does not have that basic

¹¹⁶ Tr. 11/15/19, 861:8-862:13; 892:21-893:22.

¹¹⁷ Tr. 11/15/19, 864:18-865:6.

¹¹⁸ Tr. 11/21/19, 1501:25-1502:7.

¹¹⁹ Tr. 11/15/19, 866:16-24, 897:21-898:11; Tr. 11/21/19, 1515:22-1516:6.

amenity as the vast majority of other dealerships do, and it, in fact, lost 20% of its technicians last summer.

The record evidence also supports the ALJs' finding that the construction of the parking garage structure with a few additional service bays may not solve the wait time problem. See FOF 126. Mr. Hardeman admitted that the only benefit the new construction will have on his service business is eliminate the need for service porters who now shuttle customer vehicles waiting for service by opening from a remote lot.¹²⁰

Factors MB of Austin does raise to explain its long wait times and the apparent high numbers of customers who must be bringing their vehicles to independent service providers are readily explained away. If in fact there are Mercedes-Benz Alabama assembly plant product problems and parts shortages, then independent repair shops would have the same issues; it is not a reason for customers to shun dealers and go to independents. It also does not explain long wait times; when those issues arise, dealers simply keep the customer's vehicle until a fix or parts are obtained and give them loaner vehicles. If anything, that should shorten wait times.

In short, the ALJs' Findings of Fact 41, 44, 125, and 126, as well as its general Finding 122 are supported by the evidence, and MB of Austin's exceptions should be denied.

C. The ALJs Correctly Found that MB of Austin's Facilities Are Not Adequate Compared to Those of its Competitors in the Market¹²¹

The undisputed testimony and extensive documentary photo evidence presented by MBUSA Facilities Project Manager Jason Andersen is reflected in the ALJs' Findings

¹²⁰ Tr. 11/20/19, 1278:12-1279:1.

¹²¹ See Exceptions, ¶¶ 7, 15, 16.

of Fact that MB of Austin challenges. FOF 34, 127 and 129. Mr. Andersen testified extensively to the shortfalls in MB of Austin's facilities, particularly its failure to provide the luxury experience Mercedes-Benz and other luxury brand buyers and owners have come to expect in their sales and service contacts with a dealership, summarized at 48-54 of MBUSA's Opening Brief.¹²² Adequate representation has everything to do with the customer experience, the way customers experience the brand, and making sure everything the customer comes in contact with at the dealership represents the Mercedes-Benz brand in the very best possible way. As Mr. Andersen explained, the goal of any brand, especially high-end luxury vehicle brands, is to create a sense of joy, happiness and comfort through the design, aesthetics, amenities, finishes, and flow of the facilities, for both customers and employees.¹²³ In retail, and particularly in the auto business, all manufacturers want to create a lasting impression of the vehicles they sell, to create customers for life, and the physical space in which the product is sold is critical to that experience.¹²⁴

As just a few examples, MBUSA dealership design elements include those giving customers: (1) a sense of transparency, through beautiful ground to high-ceiling glass in the front façade, so that customers can see into the dealership when they drive up and the natural light spotlights, for example, on the new vehicle models in the showroom; ceilings with exposed mechanicals; windows into the service shop areas so customers can see their cars being repaired; (2) a natural and ease of flow through the dealership,

¹²² See, e.g., Tr. 11/14/19, 611-684; see photos at Ex. I-49 and 50 (MB of Austin), Ex. I-51 (MB of Georgetown), Ex. I-52 (BMW of South Austin). See also the table at 50-52 of MBUSA's Opening Brief, comparing aspects of MB of Austin's facilities that fall far short of the state-of-the-art facilities of its competitors, MB of Georgetown and BMW of South Austin.

¹²³ Tr. 11/14/19, 608:2-612:19.

¹²⁴ Tr. 11/14/19, 608:10-14, 610:10-20, 611:21-613:14; 622:6-13 (re employees).

from the parking lot to the sales experience and service experience by, for example, having a well-defined entry portal with a direct sight-line to the reception desk as well as easy and comfortable movement to the customer lounge and service area; and (3) high-end finishes—furniture, floor tile and wall materials and color palettes—to give customers the luxury brand experience they expect. MB of Austin provides very little of these design and material elements, especially as compared to the state-of-the-art facilities of its immediate competitors, MB of Georgetown and BMW of South Austin, as captured in the extensive photos of the three facilities about which Mr. Anderson testified.

MBUSA's "brand standards" which MB of Austin relies on for the basis for these exceptions are the absolute minimum facilities requirements, requirements that MBUSA established largely for its incentive program, not for purposes of the Code. As witnesses testified, MBUSA sets a very low bar for each element of its incentive program with the intent that virtually all dealers can meet that bar, and thereby earn the incentives, which as MB of Austin notes, it has met and earned in the last several years on the brand standards component.¹²⁵

Adequacy of a dealer's facilities under the first statutory factor is a completely different issue from the minimums a manufacturer sets to allow dealers to achieve bonus money. To be statutorily adequate, a dealer's facilities should be competitive, both in capacity, style, and the providing of the exceptional customer experience luxury brand purchasers expect with others in the market, both intra- and inter-brand.

¹²⁵ See, e.g., Tr. 11/22/19, 1679:24-1681:9 (MBUSA incentives are targets that are intentionally set as a low bar, designed to be attained by virtually all dealers, so that they receive their incentive bonus payouts).

Enhancing healthy competition is the essence of the seven statutory factors, including the adequacy of representation. In a highly competitive luxury vehicle marketplace like the Austin metro, the ALJs correctly found that adequacy of facilities under the first factor is assessed by the competitive nature of the facilities in a given market. Adequacy is not merely meeting the most minimal branding standards MBUSA sets to allow their dealers to earn incentives, noted above. As Mr. Andersen testified at length, MB of Austin falls far short of the appropriate standard. The ALJs in fact noted several significant deficiencies, all supported by Mr. Andersen's testimony and photo evidence, at pages 12-13 of the Proposal for Decision.

MB of Austin does not address any of Mr. Andersen's testimony, or any of the deficiencies he described relative to MB of Georgetown or the new BMW dealership in South Austin. Instead, MB of Austin argues that if MBUSA wants its dealers to have facilities that are the same aesthetically, or that are comparable with, or superior to, those of competing brands, then MBUSA has the "power to mandate the facility standards necessary to achieve those goals." Exceptions at bottom of 17. Given MB of Austin's long history as a Texas dealer of multiple brands, it is surprising that it would make such a contention. Such a suggestion flies in the face of the statutory prohibition on any manufacturer or distributor "requiring," let alone mandating, dealer facility renovations, with very limited exceptions likely not applicable here, a statutory provision enacted a decade or more ago.¹²⁶

¹²⁶ See Tex. Occ. Code § 2301.467(b) ("Notwithstanding the terms of any franchise, a manufacturer, distributor, or representative may not unreasonably require a franchised dealer to relocate, or to replace or substantially change, alter, or remodel the dealer's facilities," with certain exceptions).

Contrary to MB of Austin's further exception (in ¶ 16, FOF 129), the ALJs' finding that the dealership's location "is no longer a desirable part of town for a luxury car dealership" was also based on the undisputed testimony of Mr. Andersen. While it may be conceivable it could have been an attractive area in the 1980s when MB of Austin relocated there, it now is not in the best area of the market. It is across from train tracks amid lower-end businesses, not in a high-end retail area where Mercedes-Benz customers shop for new vehicles.¹²⁷ It's also landlocked on its site, with nowhere to expand as the market for luxury vehicles continues to grow, despite its building up with its new parking garage.¹²⁸ That it might be a convenient location in terms of distance for Mercedes-Benz customers to have their vehicles serviced does not prove the adequacy of the facilities or its location in its ability to offer luxury car buyers the experience they have come to expect. The ALJs correctly found in favor of MBUSA and Swickard on this issue as well.

VI. THE ALJs CORRECTLY FOUND MB OF AUSTIN WILL NOT BE HARMED FINANCIALLY UNDER THE CORRECT STANDARD FOR THE FOURTH STATUTORY FACTOR

A. The Standard the Board has Repeatedly Relied on Is Not "Any Harm" to Existing Dealers' Sales or Profits, as MB of Austin Urges Throughout the Exceptions¹²⁹

MB of Austin recites throughout its exceptions its erroneous mantra—if the opportunity in the relevant market is less than the new dealer's breakeven sales number, the protesting dealer should not have to sacrifice its profits.¹³⁰ That is not the

¹²⁷ Tr. 11/14/19, 623:23-624:20.

¹²⁸ Tr. 11/14/19, 624:18-625:14.

¹²⁹ See Exceptions, ¶¶ 37-39, 45, 46, 49, and others discussed in the following subsections.

¹³⁰ See Section III above.

standard. The only standard that the Board has consistently, and for decades, applied is “whether the establishment will cause so much harm . . . ‘as to cause the failure of the [existing] dealership or at least reduce the existing dealer’s profitability to such extent that it could not properly serve the public.’” *RCJD*, Final Order at 7, ¶ 70; PFD at 41 (quoting *Rockwall Imports v. The Allee Corp.*, *SOAH Docket No. 601-09-1276.LIC*, *MVD Docket No. 09-0014.LIC* (Tex. DMV, MVD, Jan. 23, 2012), adopting, *Proposal for Decision* (Apr. 20, 2011), PFD at 60, fns. 249 and 250); see also *A.C. Collins Ford v. Charlie Thomas Ford*, *Docket No. 87-206* (Tex. MVC, Sept. 6, 1989), adopting as modified, *Proposal for Decision* (July 14, 1989) PFD at 22, on which MB of Austin relies (“To sustain losses of the magnitude predicted by [protestant’s expert] would result in a reduction of the ability of the dealership to provide service to the public and ultimately go out of business”).

Contrary to MB of Austin’s characterization, the *Lee Trevino* case (quoted extensively at 10-11 of the exceptions) is consistent with this standard. The quoted passages speak to enough opportunity to maintain the profitability of the dealers, i.e. that they not operate at a loss, not that any harm is too much.

More important, MB of Austin’s constant citing to the *Landmark* PFD here and throughout its exceptions is misleading. On appeal of the Board’s decision in that case, the Third Court of Appeals said that in a market with opportunity, as here, “an existing dealer is not necessarily harmed because it must share the market with a new dealer, even if it means that the existing dealer will profit less after the dealer network expands.” *Austin Chevrolet, Inc.*, 212 S.W.2d at 434 (emphasis added). In that situation,

the Board would expect the existing dealer to “adjust its business strategy to capture untapped opportunity in the market.” *Id.*¹³¹

That MB of Austin totally ignores the appropriate standard of harm to the existing dealer is evident in the manner in which it asks the ALJs to revise their Findings of Fact in ¶¶ 37, 39, 45, 46 and 49, among others. In those exceptions, it contends MBUSA and Swickard must show that the establishment will occur “without taking profits” from MB of Austin (FOF 167) or “without harming the existing MB dealers” (FOF 194 and 200), that MB of Austin is “not required to sacrifice [any] business” (FOF 179 and 191) or “will suffer little or no harm” (FOF 192). The ALJs roundly rejected these arguments, and rightly so. See PFD at 63-64.

Again, only a total loss in profitability that causes the dealer to shutter its doors or to fail to be able serve the public would weigh in MB of Austin’s favor on this factor. As the ALJs found, based on the extensive affirmative and rebuttal testimony of Ms. Heinemann, MB of Austin is at zero risk of losing enough of its profitability to even approach this standard.

B. There Is No Question MB of Austin Is Highly Profitable and Able to Effectively Compete With an Additional Dealer in South Austin¹³²

MB of Austin first challenges only two of 13 separate findings on its incredible profitability, profitability far above all the composite dealer groups it was compared to,

¹³¹ The circumstances in *Landmark*, as noted in the appellate decision were completely different from this case, where it found the protesting dealer was not profitable and where there was no additional sales opportunity at all in the 1993 Houston market at issue, which at the time was “characterized by a ‘decade of sluggishness, a declining trend in automobile sales, stagnant wages, substantial layoffs, and only modest growth projections’”. See *Austin Chevrolet*, 212 S.W.3d at 434. *Lee Trevino*, which MB of Austin also relies on throughout, alludes to the proper standard, stating that it is not in the public interest if “the market is not sufficient to enable the dealers to operate profitably,” where the closest dealer was not profitable at all in the prior three to four years. *Lee Trevino*, PFD at 29 and 33.

¹³² See Exceptions, ¶¶ 37, 39, 45, 46, 49.

and the diversity in its operation that will allow it to comfortably compete with a new dealer (FOF 167 and 179), even if it loses some new vehicle sales if the lost opportunity were actually lower than it was in 2018, which it is not.¹³³ Notably, MB of Austin does not challenge any of the straight-up financial facts of its high profitability and the reasons for that profitability in Findings of Fact 168-178.

Those straight-up financial facts are set out by the ALJs in their discussion on the fourth factor, and each was amply supported by the extensive testimony of MBUSA's forensic accountant Suzanne Heinemann that the ALJs cited (at 71-73 of the PFD):

- Every year since 2015, MB Austin's net profit has exceeded the benchmark composite groups (FOF 168), with net profit of \$ 5,247,335 in 2015, \$ 4,989,833 in 2016, \$ 4,734,182 in 2017 and \$ 5,616,638 in 2018.¹³⁴
- As of 2018, MB Austin had no long-term debt; a cash position of \$4.6 million, a net cash position of nearly 600 percent, and working capital of 200 percent of what MBUSA requires for a healthy dealership; its net profit for 2018 exceeded its total net fixed assets after depreciation (\$5.6 million versus a little under \$4 million); and MB Austin's return on equity is very high and far exceeds the average of the composite groups (FOF 169).
- MB Austin's profitability is not dependent on its new-vehicle sales volume. Specifically, in 2018, MB Austin's profit increased from \$4.7 million to \$5.6 million, despite selling 16 percent fewer new vehicles than in 2017 (FOF 170).
- MB Austin generates a higher amount of revenues from its fixed operations (service, parts, and body shop departments) than the benchmark groups, and the profit margins in fixed operations are much higher than those in the new or used vehicle departments (FOF 171).
- MB Austin's net profit in its fixed operations exceeds all of its fixed expenses by 1.72 times, which is more than the composite groups (FOF 172).

¹³³ MB of Austin does also challenge Finding of Fact 170 in its Exception ¶ 38 on the issue of incentives it receives from MBUSA, discussed in the next section. Finding 170, however, is a simple statement of financial fact—MB of Austin's net profit increased in 2018 from \$4.7 million to \$5.6 million, despite selling 16% fewer cars in 2018.

¹³⁴ See Exs. I-8, I-9, I-11, and I-14, respectively, at 1, bottom right summary box.

- MB Austin is in a better financial position than most dealerships because fixed operations are more recession-proof than vehicles sales: if customers are not buying new cars, then they will need to have their old cars serviced (FOF 173).
- Because its net profit from fixed operations fully covers its fixed expenses, MB Austin has more flexibility in its new and used vehicle departments (FOF 174).
- MB Austin has a large used vehicle department with higher profit per vehicle than the benchmark groups (FOF 175).
- In 2018, MB Austin increased its gross profit on finance, insurance, and service contract products sold with new vehicles, and made a higher profit than previous years on the sale of those items while maintaining its higher-than-average gross profits on new vehicles (FOF 176 and 178).
- MB of Austin has had higher than average gross profit on sales of new vehicles, charging more for vehicles than its peers on an average per unit basis (FOF 177).

These are the very financial facts—that MB of Austin is “so profitable and financially successful [to] withstand competition from an additional dealer” —that will allow MB of Austin to “easily adjust its business strategy [to meet] additional competition,” and that “will allow it to compete effectively with a new dealership.” as the ALJs found in Findings of Fact 167, 178 and 191, respectively, contrary to Exceptions ¶¶ 37, 39 and 46. It is also these facts that lead to the ultimate fact that the ALJs also found (FOF 192), under the appropriate legal standard above, that MB of Austin will suffer little or no harm from the establishment, thereby ruling in MBUSA and Swickard’s favor on the fourth statutory factor.

In particular, it is MB of Austin’s higher than average gross profits per unit of new and used vehicles and the fact that its fixed operations cover all of its overhead expenses of the dealership, that the ALJs found above, that will provide MB of Austin a “cushion” to allow it to compete better on pricing to the benefit of consumers under the

fifth public interest factor, under Findings of Fact 192, 194 and 200, contrary to MB of Austin's Exceptions ¶¶ 46 and 49.

C. MB of Austin Will Not Lose Any MBUSA Incentives, And Possibly Earn More¹³⁵

In its exceptions (at ¶ 38), MB of Austin challenges Finding 170, that simply states the fact that it made almost an additional \$1 million more in net profit in 2018 than 2017 even though it sold 16% fewer new vehicles in 2018. MB of Austin's argument is that much of that profit, presumably in both years, was due to incentives it, and almost every other Mercedes-Benz dealer, earns from MBUSA for hitting certain specified performance targets, and that MBUSA did not show that MB of Austin will not lose the bulk of its incentives, if its sales drop. *Id.*

The incentives issue is a red herring. First, MB of Austin injected this issue into this matter in its post-hearing brief, stating that neither Ms. Heinemann, nor its own expert Edward Stockton, looked at the impact of lost sales on its ability to earn MBUSA incentives. See PFD at 70. But the evidence presented, that the ALJs summarized (at 70-71 of the PFD) actually demonstrates to the contrary, that MB of Austin will probably earn more incentive money than it has in the past, even with fewer new vehicle sales.

First, MBUSA pays incentives to all of its dealers, the qualifiers for which are intentionally "low bars" so that all dealers can meet them, like the Brand Standards qualifier discussed above in Section V.C.¹³⁶ In reality, the bonuses are generally earned by many activities other than new vehicle sales. Exhibit P-19 is an example of the scorecard from the Dealer Performance Bonus Program, from which the incentive

¹³⁵ See Exception ¶ 38.

¹³⁶ See, e.g., Tr. 11/22/19, 1679:24-1681:9 (MBUSA incentives are targets that are intentionally set as a low bar, designed to be attained by virtually all dealers, so that to receive their incentive bonus payouts).

payments are derived. The categories for earning the incentives that MB of Austin worries about relate to things like customer experience survey results for both sales and service, whether the dealership collects email addresses and sends email to its customers, whether dealership employees are trained, whether the dealership meets the facilities Brand Standards, and whether the dealership sells certified pre-owned vehicles in its mix of used vehicle sales.¹³⁷ There is one aspect related to new vehicle sales; it is not raw volume, but rather scores such as achieving just 80% of its sales effectiveness (not even the average score of 100%).¹³⁸ And despite MB of Austin's fretting about the future of new vehicles sales, all the sales-related performance metrics only represented 14% of the incentives in 2017, and MB of Austin already did consistently poorly on this particular sales effectiveness score.¹³⁹ In fact, MB of Austin made about \$500,000 more in incentives in 2018 over 2017, even though it sold 14% fewer new vehicles in 2018.¹⁴⁰

Perhaps more important, MB of Austin will likely actually do better on the 80% sales effective bonus target once the geography of the new AOI for the South Austin territory is carved out of its current Austin AOI, and thereby consistently earn that incentive payout. A smaller geography from which the 'expected' denominator

¹³⁷ Ex. P-19.

¹³⁸ *Id.* at "New Vehicle Sales" section.

¹³⁹ *See id.* (0.75, the value of the New Vehicle Sales Section, is 14% of the 5.5% total earnable bonus and despite scoring poorly in this section, MB of Austin was still paid the entire 5.5% and MB of Austin missed the SE% target of 80%). The other two targets in the New Vehicle Sales section, of "AOI" and "DMA" refer to the percent of a dealer's total sales that are purchased by consumers residing in the dealer's AOI or the greater DMA. Those are super easy targets; if a dealer just sells 2 vehicles in a calendar quarter, and both of those sales are to residents of its AOI and DMA, even though it needs to sell 100 to be sales effective, it would still meet those AOI and DMA low bar targets, as MB of Austin almost always did.

¹⁴⁰ Total of 2018 incentive payments, lines 45 and 63-71 on page of Ex. I-14 compared to total in 2017 of lines 44 and 62-70 on page 2 of Ex. I-11.

component is calculated means a smaller expected number, so even a reduction in the dealer's actual sales will likely yield a higher sales effectiveness percent, thereby making it easier for MB of Austin to receive that component of the incentive program going forward. Mr. Farhat actually did that calculation and it proved true for MB of Austin.¹⁴¹

Based on MBUSA's evidence, including the above, the ALJs did "not find MB Austin's argument regarding incentive payments to be persuasive." PFD at 71. MB of Austin presents no additional evidence in the record for the ALJs to come to any different finding than that in Finding of Fact 170.

D. The ALJs Correctly Found Fault with Mr. Stockton's Opinions¹⁴²

MB of Austin complains in its Exception 40 that the ALJs provide no evidentiary support for the finding that Mr. Stockton's profit loss analysis did not account for economic and population growth in Austin. Therefore, MB of Austin argues, that finding and corresponding discussion on page 68 of the PFD should be withdrawn. This finding is inherent to Mr. Stockton's analysis and fully supported by the record. First, Mr. Stockton did not hide the fact that his models were tied solely to 2017 and 2018 data.¹⁴³ By pinning MB of Austin's claimed loss of 20% to 30% to 2017 and 2018 inherently does not account for the economic and population growth in Austin since 2018. Additionally, although Mr. Stockton obscures his analysis and results in his own report, Ms. Heinemann's reconstruction of Mr. Stockton's loss calculations are clearly limited to

¹⁴¹ See, e.g., Ex. I-65 at 55 (showing that MB of Austin's sales effectiveness varied from 65.9 to 71.6 between 2014 and 2017, but with smaller geophagy due to the establishment carved out for South Austin, its sales effectiveness for the same time period would have ranged from 95.7% to 107.4%).

¹⁴² See Exceptions, ¶¶ 40-43.

¹⁴³ Tr. 11/19/19, 1009:21-23 ("Q You built your models around 2017 and 2018 information? A Yes.").

2017 and 2018, therefore not accounting for any growth that has or will occur after 2018.¹⁴⁴

Exception 41 challenges the finding that Mr. Stockton's gravity model exaggerates predicted impact on existing dealers when applied to real world examples. MB of Austin complains this finding mischaracterizes Mr. Stockton's testimony. MB of Austin's criticism fails to acknowledge this finding is based on the analysis of Mr. Farhat, which the ALJs credit.¹⁴⁵ MB of Austin's complaints notwithstanding, the gravity model underpins much of Mr. Stockton's analysis,¹⁴⁶ and even he admits that it does not always work in the real world.¹⁴⁷ In support of its argument, MB of Austin asserts that Mr. Stockton claimed that MB of Austin would only lose two-thirds of the sales loss implied by the territory losses. As demonstrated by Mr. Farhat, and as credited by the ALJs, this is still exaggerated when compared to the real world. For example, the first establishment listed on page 26 of Exhibit I-67—MB of The Woodlands—shows that Mr. Stockton's gravity model predicted that MB Houston North would lose 29.3% of its sales; the measured impact was only 12.5%.¹⁴⁸ Mr. Farhat showed that Mr. Stockton's model overstates impact by an average of 30% to 40%.¹⁴⁹ That the ALJs credited Mr. Farhat's rigorous analysis over Mr. Stockton's generalized claims does not support a

¹⁴⁴ Tr. 11/22/19, 1744:13-1745:22; Ex. I-70 at 47-48.

¹⁴⁵ See PFD at 68 ("Additionally, Mr. Farhat demonstrated that Mr. Stockton's gravity model exaggerates . . ."); Tr. 11/21/19, 1625-26; Ex. I-67 at 26.

¹⁴⁶ See, e.g., discussion beginning at Tr. 11/19/19, 976, during Mr. Stockton's direct examination. "Gravity model" appears approximately 23 times in the questions and answers of Mr. Stockton's testimony.

¹⁴⁷ Tr. 11/19/19, 1019:2-5 (admitting MB of Austin does better in its fixed operations than would be implied by gravity model).

¹⁴⁸ *Id.*

¹⁴⁹ Tr. 11/21/19, 1625:2-1626:2; Ex. I-67 at 26.

valid exception. Finding of Fact No. 185, and the related discussion, is supported by the record, and Exception 41 should be rejected.

In Exception 42, MB of Austin tries to unsay what Mr. Stockton actually said. MB of Austin takes exception to the finding that admitted his gravity model did not accurately capture MB of Austin's performance in fixed operations. MB of Austin seeks to create uncertainty by citing the word "probably" used in a related follow-up question. However, this does not change Mr. Stockton's admission in cross-examination:

Q Mercedes-Benz of Austin is doing better in their fixed operations than would be implied by their regression-based proximity advantage?

A ··They are.

Tr. 11/19/19, 1019:2-5. That is, contrary to MB of Austin's statement in Exception 42 that "[t]he gravity model is a useful predictive model," MB of Austin should not be able to escape the clear admission of its own expert. Finding of Fact 186, and its corresponding discussion, is supported by the record, and Exception 42 should be rejected.

In Exception 43, MB of Austin tries to bring Mr. Stockton along for the ride in its attempted rehabilitation of the analysis and methodologies of Dr. Hatch.¹⁵⁰ Startlingly, the only citation to anything related to Mr. Stockton in Exception 43 is page 241 of Mr. Stockton's report. No testimony is cited. The one Stockton-related page that is cited in Exception 43 was only touched on in passing during Mr. Stockton's testimony. Notably, page 241 of Mr. Stockton's report can only have so much importance given that it is not cited or discussed in the 17-page narrative of Mr. Stockton's report. That is, nothing discussed in Exception 43 actually connects to the ALJs' reasonable conclusion to reject Mr. Stockton's methodologies. Rather, as reflected in Findings of Fact 187 and

¹⁵⁰ The real problems with Dr. Hatch's methodologies is discussed in detail in prior sections.

188, the ALJs reasonably rejected Mr. Stockton's methodologies because he does not explain or support his opinions, makes estimates not supported by calculations, and in one example, focused on a statistically non-significant result that he doubled from 12.37 percent to 25 percent. As to Mr. Stockton, Exception 43 also should be rejected.

VII. MB OF AUSTIN'S ATTACKS ON THE ALJs' GENERAL FINDINGS OF HEALTHY COMPETITION, CUSTOMER CONVENIENCE, AND PUBLIC INTEREST ARE UNWARRANTED GIVEN THE LOST OPPORTUNITY IN THE MARKET¹⁵¹

MB of Austin essentially agrees with the ALJs' general statements of how an additional dealership will create a desirable competitive marketplace and be beneficial to the consuming public—increased inter- and intrabrand competition, more competitive pricing, enhanced customer convenience to shop for cars and have them serviced, increased customer choice through increased inventory, more locations and the like, and increased brand awareness through additional advertising and visibility by the new dealership. See FOF 144, 146, 147, 150 and 153. MB of Austin argues, however, that none of these benefits will occur because, again, of the purported lack of lost opportunity sufficient for Swickard to be profitable (the “breakeven” argument again) will cause destructive competition and will outweigh any of these consumer benefits.

There is more than enough lost sales opportunity in the Austin AOI and AOR, based on what the ALJs correctly found was the only credible evidence, offered by Mr. Farhat. See Section III above. The only additional substantive issue MB of Austin raises in its exceptions to the Findings of Fact above is that the Austin AOR is already a highly competitive market in terms of vehicle pricing; any further competition will just harm it. *E.g.*, Exception ¶ 20. While that may be true as to interbrand competition from BMW,

¹⁵¹ See Exceptions, ¶¶ 20, 21, 22 and 24, among other attacks on general findings like these.

Audi and Lexus, it definitely is not true with regard to intrabrand competition among Mercedes-Benz dealers. Gross profit per unit of new vehicles sold is a prime indicator of the level of price competition at the intrabrand level. As Ms. Heinemann's detailed analysis demonstrated, on its gross profit on the sale of new vehicles, or PNUR, MB of Austin has always made more money, charging more for new vehicles than its peers in the multiple composites of Mercedes-Benz dealers in Texas and of like-size in the Southern Region on an average per unit basis. That higher PNUR shot up substantially in 2018 in terms of overall gross profit on new vehicle sales when MB of Austin made a much higher profit on the finance, insurance, and service contract products it sells with its new car sales (F&I) than in the past. MB of Austin's higher gross profit on its new vehicles sales plainly indicates its pricing is not competitive, and has not been for years.

MB of Austin's exceptions on this issue should also be rejected.

VIII. THE ALJs' CONCLUSIONS OF LAW ARE AMPLY SUPPORTED BY THE RECORD EVIDENCE¹⁵²

In their Proposal for Decision, the ALJs made 223 separate evidentiary findings, after thoroughly addressing the evidence and providing their analysis of the parties' arguments in 78 pages of discussion and citations to the record. There simply is no basis to reject any of the ALJs' summary, ultimate factual findings on each statutory factor, or any of the Conclusions of Law on each of those factors. MB of Austin's reliance on the *Charter Medical* case is misplaced.¹⁵³ The Texas Supreme Court in that case was only addressing the agency's conclusory decision as a whole, not where, as

¹⁵² See Exceptions, ¶¶ 25, 47, 51, 54-60.

¹⁵³ See *Texas Health Facilities Comm'n v. Charter Medical-Dallas*, 665 S.W.2d 446 (Tex. 1984), cited in Exceptions 35, 47 and 51.

here, the ALJs made 223 separate fact findings, all amply supported by the record evidence, that support their conclusions.

These Exceptions should be denied, as well as the Findings of Fact MB of Austin has challenged.

IX. MBUSA AGREES ON THREE MINOR POINTS MB OF AUSTIN RAISES AND REQUESTS CORRECTION OF ONE ADDITIONAL MINOR MISTAKE

The three points with which MBUSA agrees in part are with regard to Finding of Fact 38 (Hoefl's testimony that MB of Austin only serviced 43% of the vehicles serviced), Finding of Fact 122 (on who is not capturing lost service opportunity in the Austin AOI), and a statement on page 62 of the Proposal for Decision (sales effective performance of BMW of South Austin).¹⁵⁴

Looking at Exhibit I-26, the December 2018 SOI report, what Mr. Hoefl intended was exactly what the ALJs noted at page 53 of the Proposal for Decision. There were 7,921 Mercedes-Benz vehicles in the AOI out of the total UIOs in the AOI of 12,397, or 63.9%, that were actually serviced by a Mercedes-Benz dealer (the Serviced VINs). As the ALJs properly noted, of those Serviced VINs, MB of Austin only serviced 43% of the 63.9% serviced, with the remaining 20.9% of that 63.9% having been serviced by other Mercedes dealers. So, MB of Austin essentially serviced approximately two-thirds of the Serviced VINs, or about 5,300 of the 7,921. The error in Finding of Fact 38, however, is that the total number of Un-Serviced VINs, which is the amount of opportunity, remained 4,615, which is higher than the 3,900 noted in Finding of Fact 38.¹⁵⁵

¹⁵⁴ See Exceptions, ¶ 9, bottom of page 19, and ¶¶ 13 and 34.

¹⁵⁵ See Ex. I-26, top line, middle box.

Finding of Fact 122, that “MB Austin” is not adequately capturing the lost service opportunity in its AOI, should read “Mercedes-Benz dealers” instead of MB of Austin, as the SOI reports reflect customer VINs registered in the Austin AOI that are serviced by any Mercedes-Benz dealer.

The statement on page 62 of the Proposal for Decision (which actually is not in Finding of Fact 164 about which Exception ¶ 34 takes issue), regarding BMW of South Austin, is a simple misstatement. As the ALJs correctly stated in detail at page 29, Mr. Farhat testified that the registration effectiveness of the BMW brand in South Austin, not the sales effectiveness of the new BMW of South Austin, exceeded 100%.¹⁵⁶ The statement on page 62 to the contrary should be revised.

The one misstatement MBUSA noticed in the Proposal for Decision is at page 37, where it states “[a]s of 2018, MBUSA’s total inventories, including new cars and parts inventory, was \$30 million.” “MBUSA” should be “MB of Austin.” MBUSA requests this simple typographical error be revised.

X. CONCLUSION

The thrust of the establishment provision of the Occupations Code is the “strong public interest in a vigorously competitive marketplace.” *Grubbs Nissan*, PFD at 22 (ruling in favor of the establishment despite the findings of adequacy of sales or service and little lost opportunity in the Grapevine market, noting that is only one factor of seven). This is particularly true where, as here, there is overwhelming evidence of the

¹⁵⁶ See PFD at 29 (“BMW’s registration effectiveness in South Austin increased from 82 percent in 2017 to 102.1 percent by the end of 2018 and to 116.4 percent through May 2019. In the rest of the Austin AOR (where the pre-existing BMW dealership is located), BMW’s registration effectiveness rose from 90 percent in 2017 to 108 percent in 2018 and was still above national average at 102.2 percent through May 2019.”)

long history of underperformance in sales and service in the Austin market for the Mercedes-Benz brand, significant lost sales and service opportunity, and nowhere near the level of financial harm MB of Austin would have to experience to weigh in its favor. This is particularly true, given the undisputed testimony of the long-standing demographic and economic growth in Austin, which, once the effects of COVID-19 are behind us, will continue apace, and sooner than the new dealership could possibly open.

For these reasons, and those in MBUSA's post-hearing briefing, MB of Austin's exceptions should be overruled.

Respectfully submitted,

s/ Lloyd E. Ferguson

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CERTIFICATE OF SERVICE

I hereby certify that on this the 10th day of August, 2020, I will serve the above and foregoing on all counsel of record via the Texas e-filing system.

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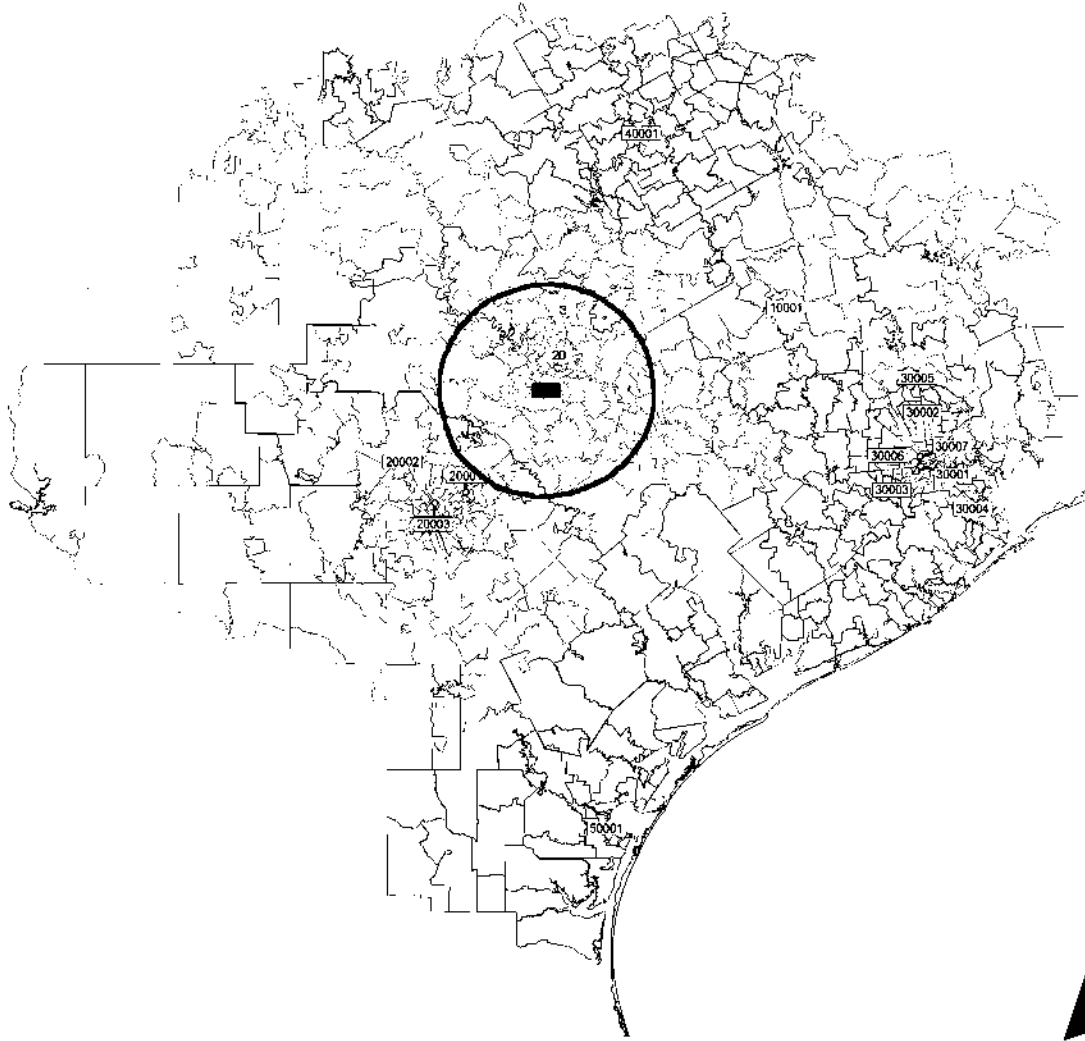
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s/ Lloyd E. Ferguson

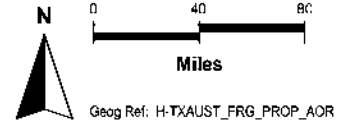
Lloyd E. Ferguson

MERCEDES-BENZ USA, LLC

Austin Fringe Proposed AOR Map



- 1 PROP M-B South Austin
- 3 M-B GEORGETOWN Georgetown
- 20 M-B AUSTIN Austin
- 10001 FUT M-B COLLEGE College Station
- 20001 FUT M-B SELMA Selma
- 20002 M-B BOERNE Boerne
- 20003 M-B SAN ANTONIO San Antonio
- 30001 M-B HOUSTON GRN Houston (Greenway)
- 30002 M-B HOUSTON NOR Houston (North)
- 30003 M-B SUGAR LAND Sugar Land
- 30004 M-B CLEAR LAKE League City
- 30005 M-B WOODLANDS The Woodlands
- 30006 M-B W HOUSTON West Houston
- 30007 STAR MOTOR CARS Houston
- 40001 M-B WACO Waco
- 50001 ED HICKS IMPORT Corpus Christi



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Exhibit I-65 - 027

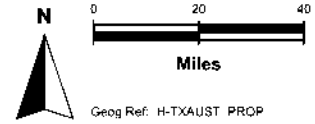
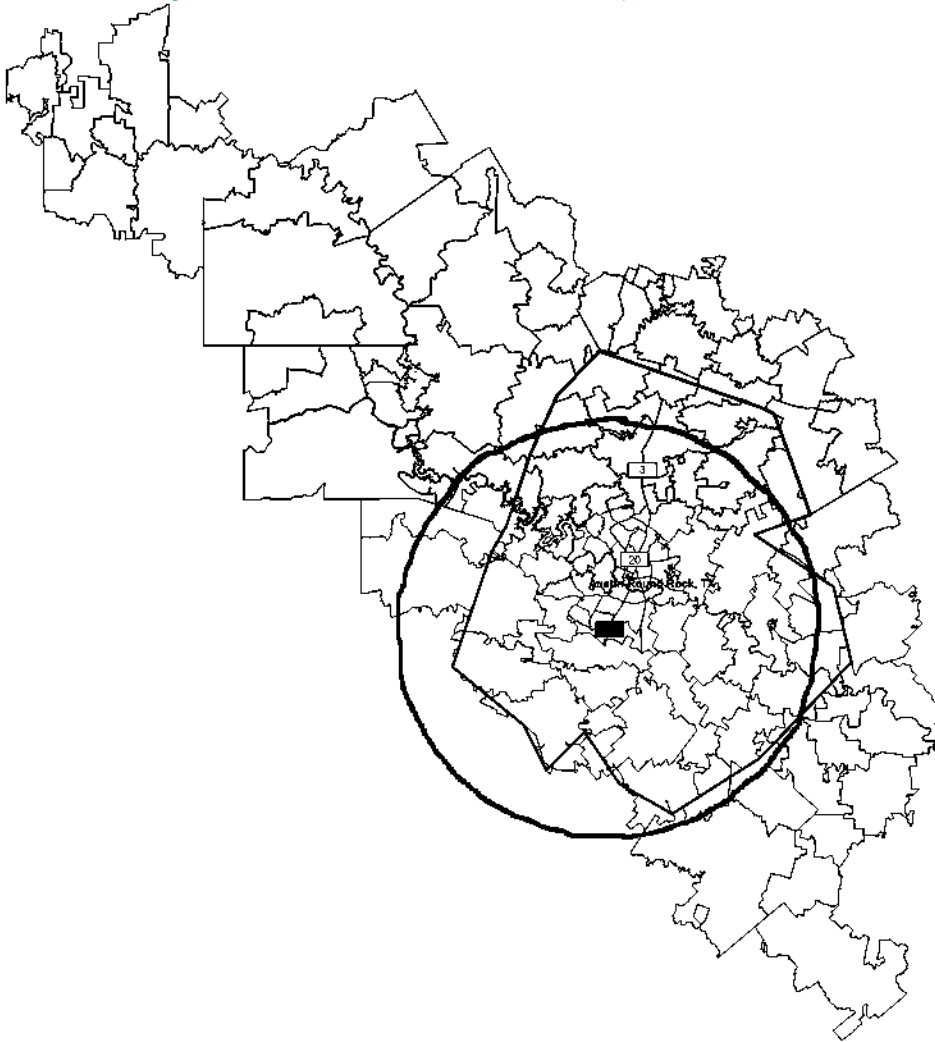
A-3

MERCEDES-BENZ USA, LLC

Austin AOR Proposed AOI Map

- 1 PROP M-B South Austin
- 3 M-B GEORGETOWN Georgetown
- 20 M-B AUSTIN Austin

— Austin-Round Rock MSA



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Exhibit I-65 - 033

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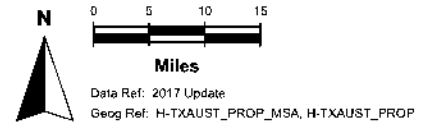
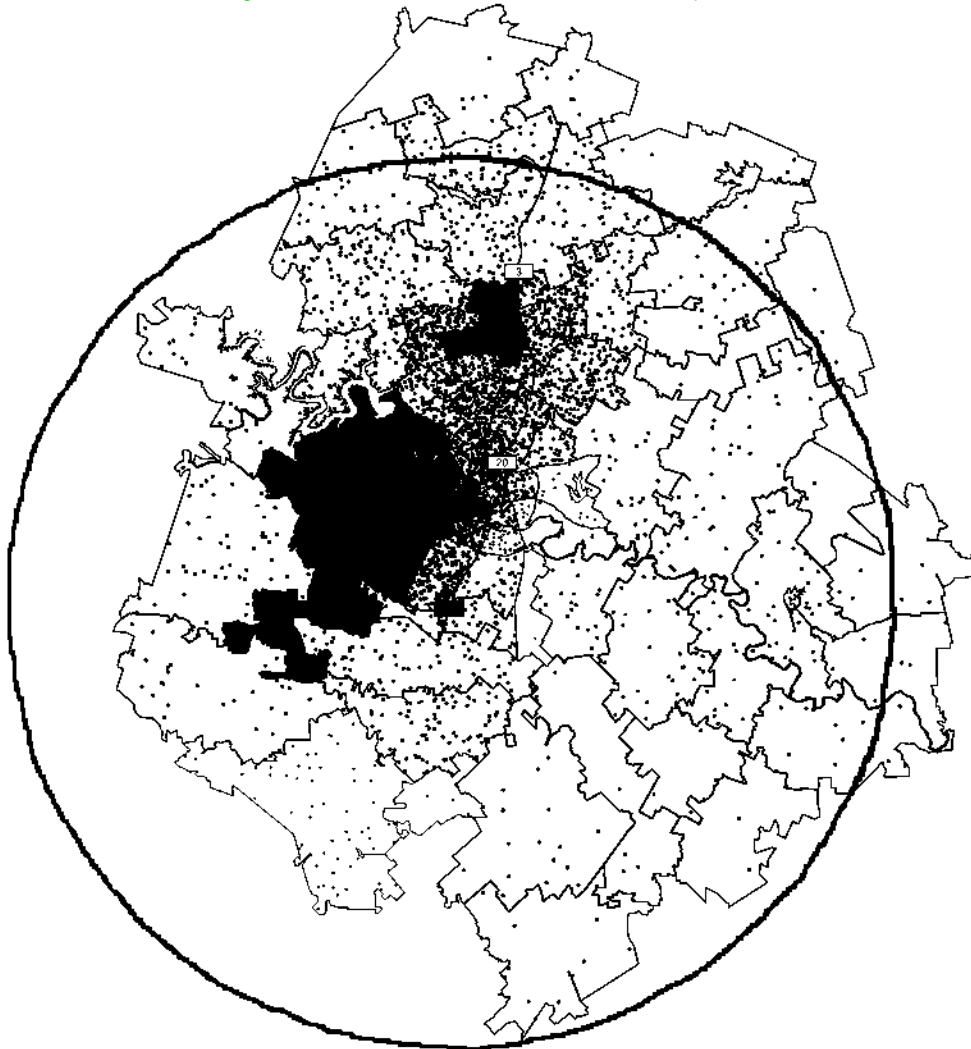
**Austin-Round Rock MSA
2017 Median
Household Income
Greater than \$100,000**

1 Dot = 60 Household(s)
Total 2017 HH Inc > 100K = 293,302
Data by Environics Analytics, Inc

- \$100001 AND ABOVE
- \$50000 - \$100000
- \$50000 AND BELOW
- NO DATA

- 1 PROP M-B South Austin
- 3 M-B GEORGETOWN Georgetown
- 20 M-B AUSTIN Austin

Austin AOR:
Total 2017 HH Inc > 100k = 328,964



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Exhibit I-65 - 081

MERCEDES-BENZ USA, LLC

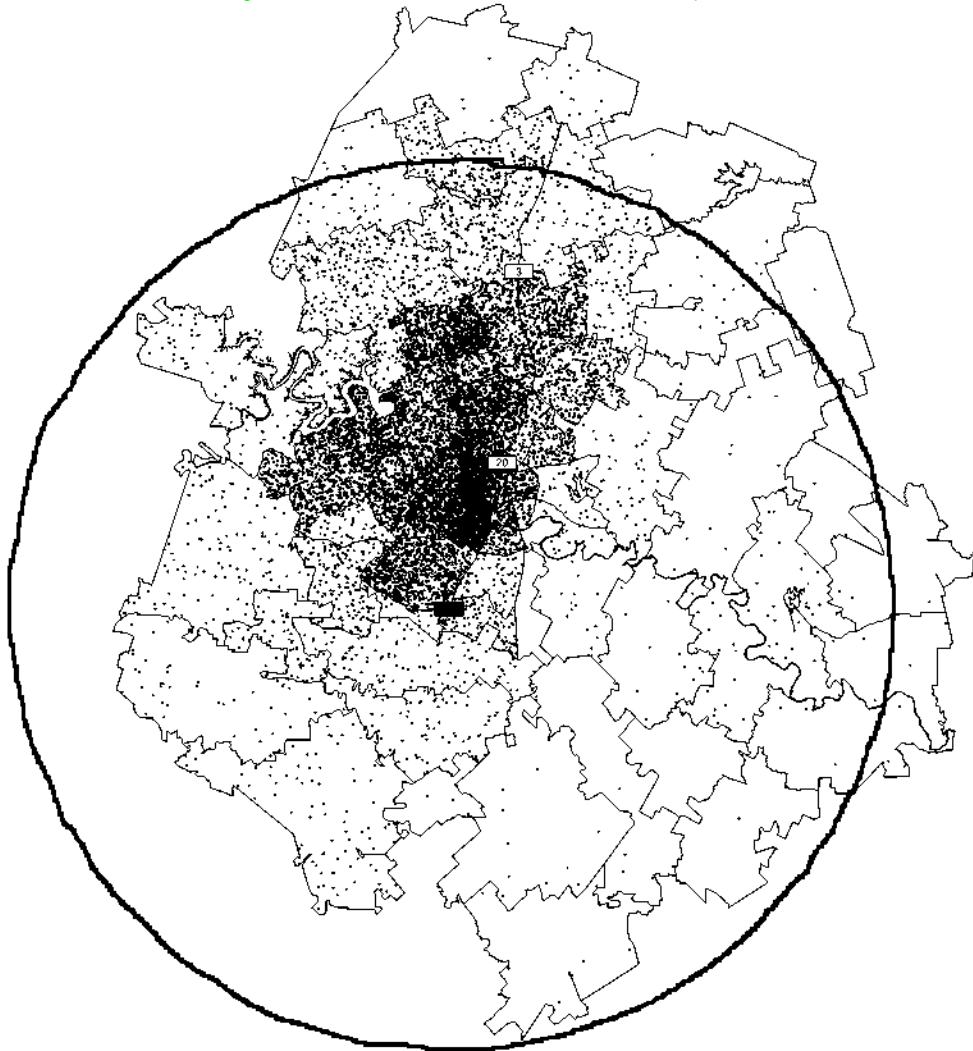
**Austin-Round Rock MSA
Dec 2018 CYTD
Competitive Group
Luxury Car and SUV
Retail Registrations**

1 Dot = 1 Registration(s)
Data By: Experian

Total Registrations = 12,155

- 1 PROP M-B South Austin
- 3 M-B GEORGETOWN Georgetown
- 20 M-B AUSTIN Austin

Austin AOR:
Total Registrations =13,295



Data Ref: Dec 2018 CYTD
Geog Ref: H-TXAUST_PROP_MSA, H-TXAUST_PROP

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Exhibit I-65 - 082

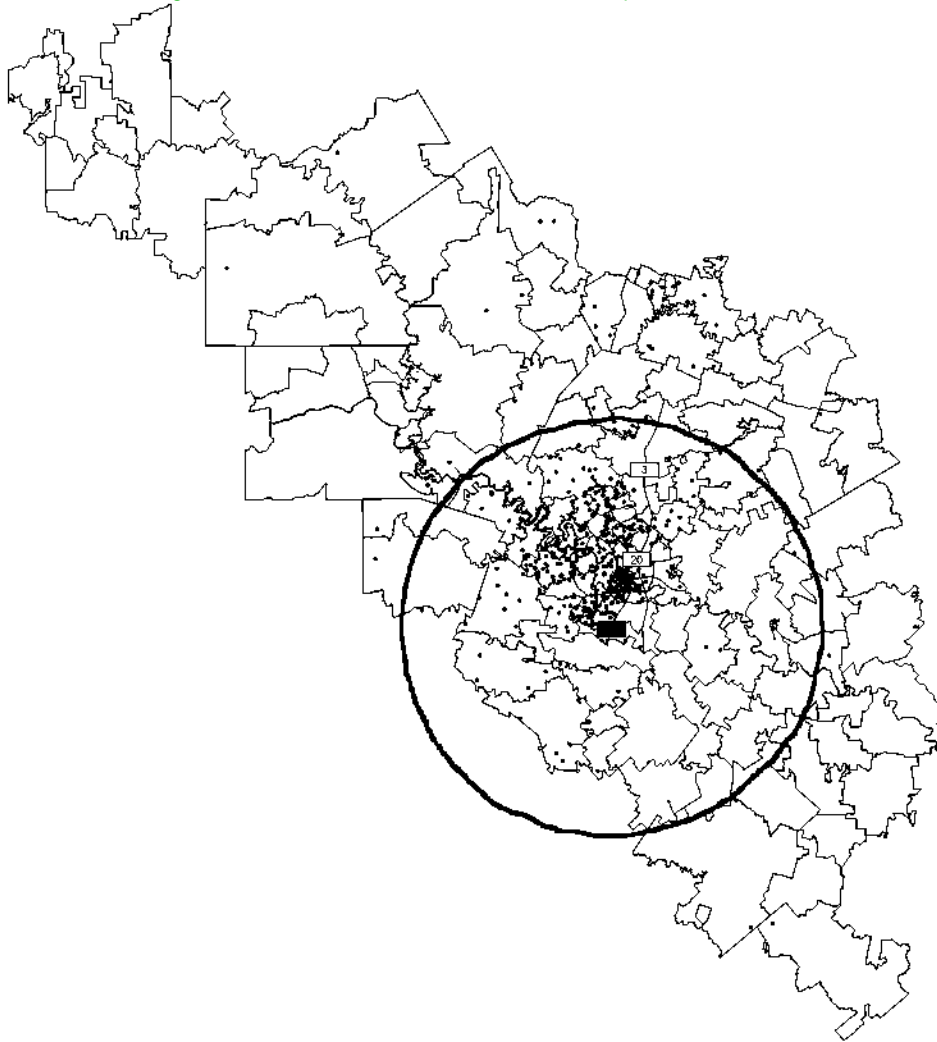
MERCEDES-BENZ USA, LLC

**Austin AOR
Retail Mercedes-Benz
Luxury Car and SUV
Areas that Fall Below
National***

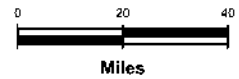
1 Dot = 1 Registration(s)
Data By Experian

LOSS: 474

- 1 PROP M-B South Austin
- 3 M-B GEORGETOWN Georgetown
- 20 M-B AUSTIN Austin



*National Market Share Adjusted for ZIP Code Segment Popularity



Data Ref: Dec 2018 CYTD
Geog Ref: H-TXAUST PROP

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Exhibit I-65 - 096

A - 72

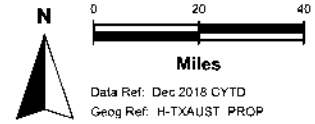
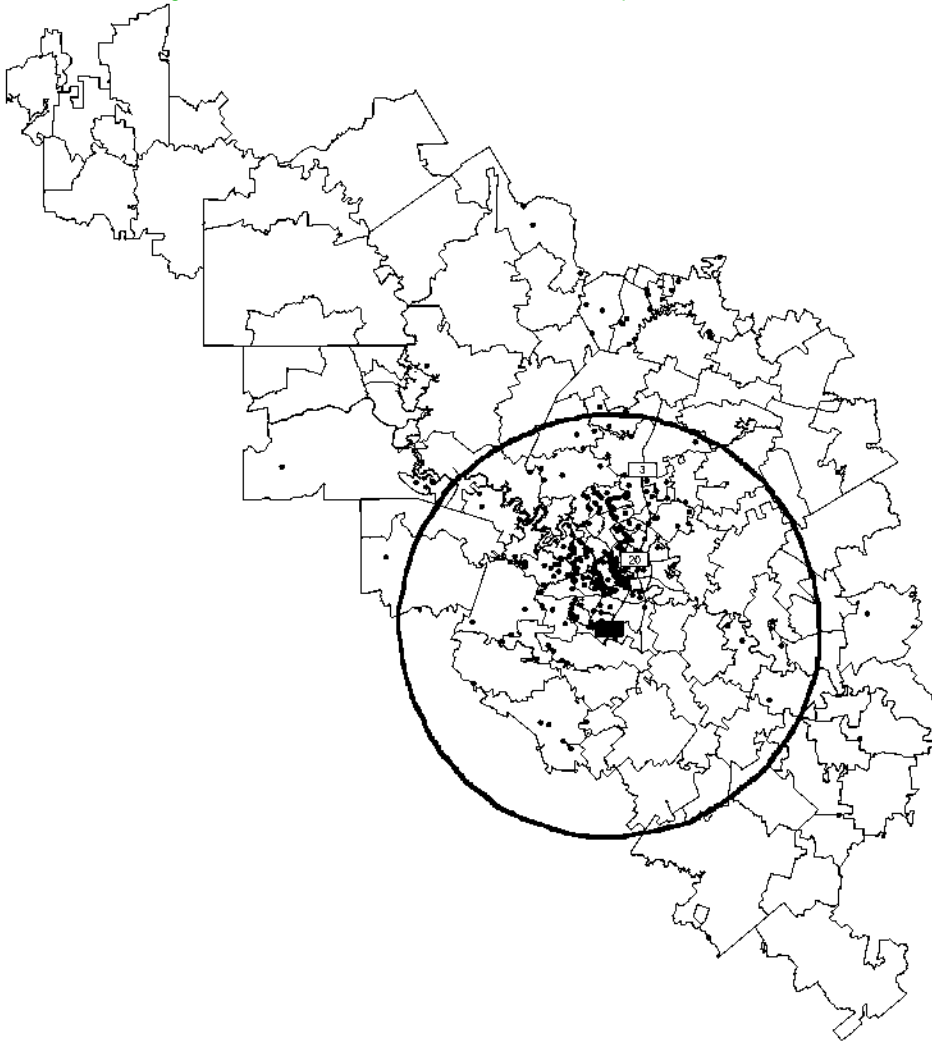
MERCEDES-BENZ USA, LLC

**Austin AOR
Insell
Retail Mercedes-Benz
Luxury Car and SUV
Registrations**

1 Dot = 1 Sale(s)
Data By: Experian and MBUSA

Total Insell Registrations = 281

- 1 PROP M-B South Austin
- 3 M-B GEORGETOWN Georgetown
- 20 M-B AUSTIN Austin



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Exhibit I-65 - 097 A - 73

license application and so that the Applicant can begin the process of developing and opening the new dealership to the benefit of all.

Dated this 10th day of August, 2020.

Respectfully submitted,

BASS SOX MERCER

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-and-

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CERTIFICATE OF SERVICE

I certify that a true and correct copy of this foregoing document has been forwarded to all counsel of record via e-mail on this 10th day of August, 2020 as follows:

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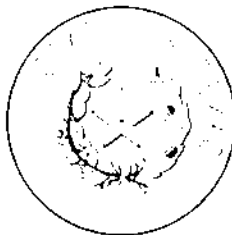
Attorneys for Intervenor

/s/ Nicholas A. Bader
Nicholas A. Bader

FILED
608-19-2065 Board Meeting eBook
8/21/2020 4:04 PM
STATE OFFICE OF
ADMINISTRATIVE HEARINGS
Jessie Harbin, CLERK

April 1, 2021

State Office of Administrative Hearings

Kristofer Monson
Chief Administrative Law Judge

August 21, 2020

Daniel Avitia, Director
Motor Vehicle Division
Texas Department of Motor Vehicles
4000 Jackson Avenue
Austin, TX 78731VIA EFILE TEXASRE: **Docket No. 608-19-2065.LIC; MVD Docket No. 19-0005.LIC; Continental Imports, Inc. d/b/a Mercedes-Benz of Austin v. Swickard Austin, LLC d/b/a Mercedes-Benz of South Austin, Applicant, Mercedes-Benz USA, LLC, Intervenor.**

Dear Mr. Avitia:

After the Proposal for Decision (PFD) was issued, Continental Imports, Inc. d/b/a Mercedes-Benz of Austin (MB Austin) filed exceptions. Intervenor Mercedes-Benz USA, LLC, (MBUSA) filed a reply to those exceptions. The applicant, Swickard Austin, LLC d/b/a Mercedes-Benz of South Austin (Swickard), filed a pleading stating it was joining in MBUSA's reply. MB Austin excepts to most of the holdings in the PFD. MBUSA does not except to the PFD, but recommends four revisions, which are detailed below.

I have reviewed the exceptions filed to the PFD in this case and the replies to the exceptions. After review, I recommend the following minor changes to two Findings of Fact, and note corresponding misstatements or errors on pages 13, 37, 53, and 62 of the PFD, but otherwise do not recommend any changes to the PFD, the Findings of Fact, or the Conclusions of Law. The revisions to the findings are as follows:

38. Of the 7,900 serviced vehicles, MB Austin ~~only~~ serviced ~~43~~ 67 percent, or 5,300 of those vehicles. ~~leaving 3,900 un-serviced vehicles in the Austin AOI.~~¹
122. Mercedes-Benz dealers are ~~MB Austin~~ is not adequately capturing the lost service opportunity in its AOI.

¹ There are corresponding misstatements on pages 13 and 53 of the PFD.

SOAH Docket No. 608-19-2065.LIC
Exceptions Letter
Page 2 of 2

On page 37 of the PFD, at the top of the page, we wrote that "... MBUSA's total inventories, including new cars and parts inventory, was \$30 million." This was in error. We should have referred to MB Austin in this sentence rather than to MBUSA.

Finally, MBUSA noted that, on page 62 of the PFD, we referred to the sales effectiveness of the new BMW dealership in south Austin as being over 100 percent sales effective. We should have stated that the BMW brand, not the new BMW dealership, was experiencing over 100 percent sales effectiveness.

The remainder of MB Austin's exceptions appear to be disagreements with the PFD's evaluation of the evidentiary record. I stand by our initial analysis of the record. MBUSA adequately explained in its reply² to exceptions the reasons why we did not abate the proceedings or reopen in the evidentiary record post-hearing because of the Covid-19 pandemic. We reviewed the issue and accepted MBUSA's arguments, as stated in Order No. 15 and referenced in Finding of Fact No. 10. Those reasons will not be restated here.

In sum, other than the changes recommended above, I do not recommend any other changes to the PFD or the Findings and Conclusions included therein. The PFD is ready for consideration.

Sincerely,



Beth Bierman
Administrative Law Judge

BB/db
Enclosure

cc: All Parties of Record – VIA EFILE TEXAS

² See MBUSA Reply to Exceptions, pp. 5-12.

CONTINENTAL IMPORTS, INC. d/b/a	§	
MERCEDES-BENZ OF AUSTIN,	§	
Protestant	§	
v.	§	
	§	MVD DOCKET NO. 19-0005.LIC
SWICKARD AUSTIN, LLC d/b/a	§	
MERCEDES BENZ OF SOUTH AUSTIN,	§	SOAH DOCKET NO. 608-19-2065.LIC
Applicant,	§	
	§	
MERCEDES-BENZ USA, LLC,	§	
Intervenor.	§	

PROTESTANT’S WRITTEN MATERIALS

Summary of Reasons to Remand this Case to SOAH

Continental Imports, Inc. d/b/a Mercedes-Benz of Austin (“Protestant”) asks the Board to vacate the Proposal for Decision (“PFD”) and to remand this contested case to the State Office of Administrative Hearings (“SOAH”) for further proceedings for two reasons.

First, the Administrative Law Judges (“ALJs”) misinterpreted and misapplied the law applicable to a license application to add a new franchised dealership to a hypercompetitive market where multiple existing franchised dealerships already represent the manufacturer’s brand. In such an extremely competitive market, the Board’s decisions in *Landmark Chevrolet v. General Motors*, Docket No. 02-0002 (Dec. 9, 2004) (final order) and *Lee Trevino Ford v. Payton Wright Ford*, Proceeding 302 (March 7, 1984) (final order) require the applicant to provide reliable, factual evidence showing the estimated new vehicle sales *realistically* available for capture from competing brands but not being captured by the brand’s existing dealers, and the proposed dealership’s estimated break-even point.¹ The ALJs violated the Board’s *Landmark* and *Trevino* precedent by excusing Swickard and MB’s total failure to provide such evidence. Without it, the

¹ Excerpts from *Landmark* are behind Tab 1 of the Appendix to Protestant’s Exceptions to the PFD. Excerpts from *Trevino* are behind Tab 2 of that Appendix. “Tr.” refers to the transcript of the SOAH evidentiary hearing. “Ex.” refers to an exhibit admitted at the SOAH hearing “FF” refers to a fact finding made by the ALJs and set forth in the PFD.

Board cannot rationally assess, weigh, and make legally-sustainable findings on the good cause issues of §§ 2301.652(a)(1), (3), (4), (5), and (7) of the Texas Occ. Code (“the Code”).

Second, the COVID-19 pandemic has made the economic, financial, and market data on which the PFD is based outdated and unreliable, requiring the taking and consideration of new evidence on five of the seven statutory good cause issues. The SOAH evidentiary hearing ended in November 2019. (PFD at p. 2). Before the ALJs issued the PFD on July 2, 2020, the COVID pandemic erupted, causing widely-reported disruptions in the auto industry. Protestant asked the ALJs to reopen the record to take evidence of the pandemic’s impact on current and foreseeable economic, financial, and market conditions. (*Id.* at 3). The ALJs erred in refusing to do so.

The Board lacks reliable evidence to assess and weigh five good cause issues

This case concerns the Austin luxury market (“the Austin market”), which the ALJs found is already “extremely competitive” (PFD at p. 90), and which Mercedes-Benz USA (“MB”) admits is “hypercompetitive.” (*Id.* at p. 59). MB has two existing dealerships in the Austin market as does each of its top competitors, BMW, Audi, and Lexus. (Tr. 565:8-19, 1296:10-17). *None* of MB’s competitors has three dealerships in the Austin market. MB wants a third Austin dealer and recruited Swickard to build a facility in South Austin. (Tr. 83:9-10, 84:18-20). The Code places on Swickard the burden to prove good cause exists to establish its proposed dealership. The ALJs recommend granting Swickard’s application despite its total failure to offer any evidence showing (1) the estimated number of new vehicles the proposed dealership must sell in the hypercompetitive Austin market to exceed break-even and be profitable (Tr. 119:17-23), and (2) that the estimated untapped or lost opportunity realistically available for capture by the MB brand in this hypercompetitive market is large enough for the proposed dealership to operate profitably without unduly taking sales and service business from MB’s existing dealers, primarily Protestant.

In the absence of reliable, factual evidence concerning these two critical facts, neither the ALJs nor the Board can rationally analyze, weigh, and make proper basic findings and legal conclusions on five good cause issues, namely, whether MB is being adequately represented in the Austin market by its existing dealers, the degree of harm Protestant will suffer if the proposed dealership is licensed, the proposed dealership's financial expectations, *i.e.*, whether it will be profitable or unprofitable, and whether licensing the proposed dealership will promote healthy competition and be in the public interest. Code §§ 2301.652(a)(1), (3), (4), (5), and (7).

The Board may take any action conducive to the issuance of a final order, which includes remanding the case to SOAH for additional analysis of issues and for the taking of additional evidence. Code § 2301.709(c). The Board should vacate the PFD and remand the case to SOAH so proper findings can be made on the five good cause issues, and the Board can then assess and weigh those issues to decide if good cause exists to establish the proposed dealership.

The ALJs' misinterpreted and misapplied applicable law and precedent

The Legislature directs the Board to consider seven specific issues in deciding whether good cause exists and to make a finding on each such issue. Tex. Occ. Code §§ 2301.652(a), 2301.711(b)(1) ("Code"). In making the ultimate decision on whether good cause exists, the Board has discretion to give greater significance and weight to some statutory issues than it does to others.

In add-point cases in which the relevant market is already extremely competitive and where the manufacturer already has dealership representation, the Board gives greater significance and weight to the statutory issues of adequacy of representation, harm to the protesting dealer, and to the public interest. *See, e.g., Landmark and Trevino*. Those three issues are of greater importance in such add-point cases because allowing a manufacturer to oversaturate an already

hypercompetitive market with too many dealers greatly increases the risk of *destructive* competition, which harms both the public and the manufacturer's existing dealers in that market.

The Legislature gives the Board power to regulate and control the entry of a new franchised dealer into the market of existing dealers of the same brand to protect those dealers and the public from the destructive competition that will ensue if a new, but unneeded, dealership is added to a market already well-served by the brand's existing dealers. Franchised dealers are the manufacturer's customers. A manufacturer has an incentive to establish a new dealership, regardless of whether the market needs it, because doing so creates a new customer obligated to buy inventory from the manufacturer. (Tr. 36:13-37:2). Letting a manufacturer put a new dealership in a highly competitive market where its existing dealers already capture most of the sales and service business available for the brand is harmful to the existing dealers. It allows a new, unneeded dealer to live off the fruits and profits of the existing dealers' efforts. The Board has a statutory duty to protect existing dealers from a new intra-brand competitor unless the evidence reliably shows that the market can support both the new and existing dealers profitably.

Furthermore, motor vehicles distribution and sales "vitaly" affect the public interest and welfare of Texas citizens. Code § 2301.001. The public suffers from destructive intra-brand competition by establishing an unneeded dealership in an already extremely competitive market. Destructive competition ensues because too many dealers of the same brand in the same market chase too few sales. The overzealous competition resulting from the oversaturation of dealers in a market precludes the dealers from being able to provide a full range of customer services. The Code authorizes the Board to protect the public from unprofitable, financially unsound dealerships.

A determination whether the proposed new dealership will be in the public interest requires the Board to have reliable proof of likely profitability—not mere aspirational speculation. In

Landmark and *Trevino*, the Board established the standards for analyzing and weighing the good cause issues in add-point cases, when, as here, the manufacturer already has multi-dealer representation in an extremely competitive market. Those standards are:

- Unprofitable dealerships are not in the public interest. (*Landmark*, PFD at p. 35; *Trevino*, PFD at pp. 29, 33).
- The added convenience of a proposed dealership to the public is outweighed if the consequences of adding the dealership are likely to be more detrimental than beneficial. (*Trevino*, PFD at p. 28).
- An existing dealer's loss of sales and service business to a proposed dealership is harmful when the lost opportunity, realistically available for capture in the market, is *not* large enough to support both the proposed and existing dealerships. A lack of lost opportunity realistically available for capture prevents the existing dealer from recouping sales and profits lost to the new dealer by capturing available, but untapped opportunity in the market. (*Landmark*, PFD at p. 35; *Trevino*, PFD at p. 34).
- Destructive competition occurs if the applicant and manufacturer fail to prove that the sales and service opportunity that is realistically available for capture in a market by the brand is large enough to profitably support the proposed new dealer and the brand's existing dealers. (*Landmark*, PFD at p. 32; *Trevino*, PFD at pp. 22-23, 29, 34)
- A dealership is profitable when it exceeds its "breakeven point." Breakeven is the estimated new vehicle sales the dealership must make to reach zero operating profit. Operating profit is total sales less total cost of sales and total expenses. (Ex. P-66).
- If the sales opportunity realistically available for capture in the market by the brand, but not being captured by the brand's existing dealers, falls *below* the proposed dealership's estimated break-even point, then licensing the proposed dealership will cause destructive competition, harm to existing dealers, and will not be in the public interest. Insufficient opportunity to support the brand's proposed and existing dealers profitably also shows adequacy of representation of the brand by the existing dealers. (*Landmark*, PFD at pp. 30-31, 32, 35).

The Board's *Landmark* and *Trevino* decisions show that whether the brand's existing dealer network is adequately representing the brand, whether the proposed dealership will harm the protesting dealer or dealers, and whether licensing the proposed dealership will further healthy competition and be in the public interest hinge on the answers to three questions:

1. How many new vehicles must the proposed dealership sell to exceed its breakeven point and become profitable?
2. How many new vehicle sales realistically are available for capture for the brand in the market area, but are not being captured by the brand's existing dealers?
3. Does the number of new vehicle sales realistically available for capture by the brand, but not being captured by the brand's existing dealers, exceed the number of new vehicles the proposed dealership must sell to be profitable?

Because the ALJs' misinterpreted and misapplied the decisions in *Trevino* and *Landmark*, the ALJs excused Swickard and MB's complete failure to provide the credible, factual evidence needed to answer these questions and to provide the basis for a proper analysis of several good cause issues, especially in the context of this hypercompetitive Austin market.

Trying to show the proposed dealership will be profitable, the ALJs relied on Mr. Swickard's generalized puffery about MB dealerships he bought in the Seattle, Washington, and Portland, Oregon markets. (PFD at p. 78). Mr. Swickard said he "can't imagine running a Mercedes-Benz franchise in Austin . . . and not being extraordinarily profitable," although it is said he is "not just primarily motivated by profitability." (Tr. 96:8-12). Based on living in Austin previously, Mr. Swickard said the city is "hungry" for luxury vehicles, and he expects to own a profitable South Austin dealership "similar to the other Mercedes franchises that I own." (Tr. 96:16-25). Yet, Swickard produced *no evidence* of the revenues, expenses, and profits of his other "similar" dealerships or of the estimated revenues, expenses, and profits (or losses) of the proposed dealership – although such evidence was readily accessible to Swickard. Without evidence of the proposed dealership's breakeven point, the Board cannot rationally assess the consequences of adding the dealership to the already hypercompetitive Austin market.

The ALJs finding that "sufficient opportunity exists in the market" (PFD at p. 94 [FF 190]) is based on opportunity "hypothetically" or "theoretically" available for capture in the market by

the MB brand instead of opportunity “*realistically available*” for capture, as required by *Landmark*. The ALJs wrongly accepted MB’s market expert’s “hypothetical” lost sales opportunity—measured by the concepts of “gross loss” and “insell”—instead of lost sales opportunity realistically available for capture. (PFD at p. 92 [FF 161]). The expert did not exclude from the lost opportunity calculation the amounts of “gross loss” and “insell” he admitted would remain in the market even if the proposed dealership were established and the MB brand exceed 100% registration effectiveness. (Tr. 570:22-571:19, 578:24-579:5, 604:2-3, 1163:18-22, 1205:20-1206:5, 1602:10-11; Exs. I-65@096, I-66@033; P-1@241). The resulting lost opportunity calculation of 755 units not only is inflated, but *less* than the new vehicle sales projected by Swickard (775 units) and MB (916 units). (Tr. 1207:22-1209:1; Exs. I-42, I-65@098, A-2).

Because of their misinterpretation of Board decisions and applicable law, Swickard offered no evidence and the ALJs made no findings concerning:

- The estimated operating costs and expenses from which the proposed dealership’s breakeven point could be determined.
- The estimated new vehicles the proposed dealership must sell to breakeven.
- The new vehicle sales and service business that are realistically available for capture for the MB brand in this hypercompetitive market, but not being captured by the existing MB dealers.

Because no such evidence was offered and no such findings made, the fact findings and conclusions of law the ALJs did make in their PFD on five of the good cause issues are arbitrary, capricious, and unsupported by substantial evidence. Fact findings and legal conclusions produced by the ALJs’ their legal misunderstandings and violations of prior decisions do not bind the Board. The Legislature allows the Board to vacate a PFD or to reject fact findings and legal conclusions when the ALJs misinterpret or misapply applicable law and prior decisions. Tex. Gov’t Code § 2001.058(e)(1). The ALJs’ misinterpretation and misapplication of applicable law and of

Landmark and *Trevino* invalidate their analysis of the good cause issues in §§ 2301.652(a)(1), (3), (4), (5), and (7), the findings and conclusions they made concerning those issues, and the ultimate finding of good cause. Adopting the PFD would nullify the protections the Legislature gives the public and existing dealers from the harmful consequences of destructive competition caused by adding an unneeded dealership to an already hypercompetitive market.

The Impact of the COVID-19 Pandemic Requires Updated Data

Whether good cause exists to establish the proposed dealership includes consideration of “current and reasonably foreseeable projections of economic conditions, financial expectations, and the market for new motor vehicles in the relevant market area.” Code § 2301.652(a)(7). Such data also impacts the good cause issue of adequacy of representation, harm to the protesting dealer, a competitive marketplace, and the public interest. Code §§ 2301.652(a)(1), (3), (4), and (5).

The expert opinions on which most of the ALJs’ good cause findings and conclusions rest are based largely on 2018 and 2019 economic, financial, and market conditions. The COVID-19 pandemic has created a dramatic, abnormal, and unforeseen shift in the societal and economic foundations of this nation and this state. The financial, economic, and market reports issued since March 2020, which Protestant sought to put in evidence, show the expert opinions expressed on the good cause issues are based on outdated data from a vastly different economic era. *See* Affidavits attached to Protestant’s Motion to Take Official Notice of COVID-19 Pandemic and to Abate this Case, filed April 13, 2020, and Protestant’s Motion to Reopen the Record, or Alternatively, to Reconsider Motion to Abate, filed May 29, 2020. The pandemic has created a radically different reality than existed then, with potentially decisive impacts on five of the good cause issues, namely, Code §§ 2301.652(a)(1), (3), (4), (5), and (7). Updated expert opinions based on an analysis of post-COVID vehicle sales and on other market, financial, and economic data are

necessary to enable trustworthy findings and conclusions to be made regarding the consequences of establishing the proposed dealership. The ALJs took “official notice” of the general existence of the COVID-19 pandemic, but they unreasonably refused to consider its economic consequences and to reopen the record to take the necessary evidence concerning those consequences. (PFD at pp. 3, 80). The Board should remand this case to SOAH so that such evidence may be taken, properly analyzed, and new findings made.

Conclusion

The Board should vacate the PFD and remand the case to SOAH for further proceedings consistent with applicable law and the Board’s prior decisions. A proposed interim order of remand is attached. Alternatively, the Board should deny Swickard’s application.

Respectfully submitted,

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 E-mail: lvk@cardwellhartbennett.com
 E-mail: jbb.chblaw@me.com

By: /s/ Leon V. Komkov
 Leon V. Komkov

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CERTIFICATE OF SERVICE

I certify that a true copy of the foregoing document has been delivered by via e-mail on March 2, 2021, to all counsel of record in this proceeding.

/s/ J. Bruce Bennett
 J. Bruce Bennett

CONTINENTAL IMPORTS, INC. d/b/a §
 MERCEDES-BENZ OF AUSTIN, §
 §
 Protestant §
 §
 v. §
 §
 SWICKARD AUSTIN, LLC d/b/a §
 MERCEDES BENZ OF SOUTH AUSTIN, §
 §
 Applicant, §
 §
 MERCEDES-BENZ USA, LLC, §
 §
 Intervenor. §

MVD DOCKET NO. 19-0005.LIC
SOAH DOCKET NO. 608-19-2065.LIC

**INTERIM ORDER VACATING PROPOSAL FOR DECISION
 AND REMANDING THE CASE TO THE STATE OFFICE OF ADMINISTRATIVE
 HEARINGS FOR FURTHER PROCEEDINGS**

On April 1, 2021, the above-referenced matter came before the Board of the Texas Department of Motor Vehicles in the form of a Proposal for Decision from the State Office of Administrative Hearings. The Board, having considered the evidence, arguments, findings of fact, and conclusions of law presented in the Proposal for Decision as well as the arguments and written materials submitted to the Board by the parties to this contested case proceeding, renders this Interim Order:

Pursuant to § 2001.058(e)(1) of the Texas Government Code and § 2301.709(c) of the Texas Occupations Code, it is ORDERED that the Proposal for Decision is VACATED and the case is REMANDED to the State Office of Administrative Hearings for further proceedings to consider the following matters and to receive admissible evidence the parties may offer concerning those matters:

1. The impact of the COVID-19 pandemic on:
 - Whether the Mercedes-Benz line-make is being adequately represented as to sales and service in the Austin Area of Responsibility (“AOR”) by its

existing dealer network;

- Whether licensing the proposed Mercedes-Benz of South Austin dealership (“the proposed dealership”) will promote healthy competition in the Austin AOR;
- Whether licensing the proposed dealership will harm Mercedes-Benz of Austin;
- Whether licensing the proposed dealership will be in the public interest; and
- The current and reasonably foreseeable projections of economic conditions, financial expectations, and the market for new motor vehicles in the Austin AOR.

2. The estimated number of new motor vehicles the proposed dealership must sell to exceed its breakeven point and become profitable.

3. The estimated number of new motor vehicle sales which are realistically available for capture in the Austin AOR by the Mercedes-Benz line-make from competing line-makes, but which are not being captured by its existing dealer network.

4. Whether the estimated number of new motor vehicle sales which are realistically available for capture in the Austin AOR by the Mercedes-Benz line-make from competing line-makes, but which are not being captured by the existing Mercedes-Benz dealer network, is greater or lesser than the estimated number of new motor vehicles the proposed dealership must sell to exceed its breakeven point and become profitable.

5. The estimated dollar amount of service opportunity that is realistically available for capture in the Austin AOR by the existing Mercedes-Benz dealerships, but which is not being captured by them.

A remand is necessary and conducive to the issuance of a final order in this contested case because the Board is concerned that the COVID-19 pandemic, which began in March 2020, has rendered stale and unreliable the pre-pandemic economic, financial, and market data on which the

Proposal for Decision and many of its findings and conclusions are based.

Vacating the Proposal for Decision is necessary, and also conducive to the issuance of a final order in this contested case, because the Administrative Law Judges (“ALJs”) misinterpreted and misapplied applicable law and the Board’s prior administrative decisions interpreting and applying applicable law, principally those in *Landmark Chevrolet v. General Motors Corp.*, Docket No. 02-0002 (Dec. 9, 2004) (final order) and *Lee Trevino Ford v. Payton Wright Ford*, Proceeding 302 (March 7, 1984) (final order). The ALJs’ misinterpretation and misapplication of applicable law render erroneous their analysis of the “good cause” factors of § 2301.652(a)(1), (3), (4), (5), and (7) of the Texas Occupations Code and the findings and conclusions they made regarding those factors. The absence of proper findings on these statutory good cause factors prevents the Board from analyzing and weighing them in determining whether good cause exists to establish the proposed dealership in the Austin AOR, which the ALJs found to be already extremely competitive and the parties agree is hypercompetitive.

In *Trevino*, the Board recognized that unprofitable dealerships are not in the public interest. (*Trevino*, PFD at p. 29). The ALJs misinterpreted *Trevino* by stating that the Board’s discussion of dealership profitability applied solely to the profitability of existing dealerships rather than to the profitability of a proposed dealership, and that proof of a proposed dealership’s estimated revenues and expenses is not required. (Proposal for Decision at p. 74). The Board’s decisions in *Trevino* and *Landmark* were concerned with the profitability of the proposed dealership as well as the protesting dealership. (*Trevino*, PFD at pp. 29, 33; *Landmark*, PFD at p. 35). The decision in *Landmark* shows the importance of determining the proposed dealership’s breakeven point in a market that already is extremely competitive. (*Landmark*, PFD at pp. 35, 71 [Finding of Fact No. 278]). A breakeven point cannot be determined without reliable estimates of the proposed

dealership's operating revenues and expenses. Because the ALJs misinterpreted those decisions, the ALJs misapplied them to excuse Applicant's failure to provide evidence of its proposed dealership's estimated operating costs and revenues from which the proposed dealership's breakeven point could be determined. In the absence of such evidence, the Board is unable to determine how many new vehicles the proposed dealership must sell to exceed its breakeven point and become profitable.

In *Landmark*, the Board also held that the standard for measuring the untapped sales potential or "lost opportunity" of a line-make in the relevant market is the amount of opportunity realistically available for capture from competing line-makes in the market, but that is not being captured by the line-make's existing dealer network. The ALJs misinterpreted and misapplied applicable law, as interpreted and applied by the Board in *Landmark*, by measuring the lost opportunity that is theoretically or hypothetically available for capture rather than that the lost opportunity which is realistically available for capture. (Proposal for Decision at p. 66; Finding of Fact No. 161). The lost sales opportunity calculation presented by Intervenor and accepted by the ALJs consisted of total "gross registration loss" in the Austin AOR and total "in-sell" in Austin AOR.¹ (Proposal for Decision at p. 28; Tr. 1198:4-7, 1206:3-1). It is undisputed that "gross registration loss" and "in-sell" would remain in the Austin AOR if the proposed dealership were established and the Mercedes-Benz line-make's penetration rate exceeded 100% of its expected share of the luxury vehicle registrations in the Austin AOR. (Exs. I-65 @096, I-66 @033, P-1 @ 241; Tr. 570:22-571:6, 578:24-579:5, 1160:22-1161:7, 1199:1-20, 1205:20-1206:5, 1602:10-11).

¹ Intervenor calculated gross registration loss by comparing the actual Mercedes-Benz registrations in each ZIP code within the Austin AOR in 2018 to the expected Mercedes-Benz registrations in that ZIP code at the national benchmark if the Mercedes-Benz brand were achieving 100 percent registration effectiveness in that ZIP code, then adding up the individual deficiencies. Intervenor calculated "in-sell" by counting the new motor vehicles sold into the Austin AOR in 2018 by Mercedes-Benz dealers located outside the Austin AOR. (Proposal for Decision at p. 28).

It is further undisputed that neither Intervenor nor the ALJs made a downward adjustment to the lost sales opportunity calculation to account for the “gross registration loss” and “in-sell” that would remain in the Austin AOR if the proposed dealership were established and the Mercedes-Benz line-make’s penetration rate exceeded 100% of its expected share of the luxury vehicle registrations in the Austin AOR. (Tr. 1163:18-22). As pointed out in *Landmark*, such opportunity is not realistically available for capture. (*Landmark*, PFD at pp. 25, 26, 27, 61). Because of the ALJs’ misinterpretation and misapplication of *Landmark*, the Board is unable to make a proper estimate of the amount of sales opportunity in the Austin AOR that is realistically available for capture by the Mercedes-Benz line-make, but which is not being captured by Mercedes-Benz’s existing dealer network.

The ALJs also applied the improper “hypothetical” or “theoretical” lost opportunity standard to measure lost service opportunity in the Austin AOR. (Proposal for Decision at p. 13; Finding of Fact Nos. 37, 38; Ex. I-26). The Board also is concerned over the ALJs’ unexplained decision to rely on the Service Opportunity Index Report of December 2018 for Protestant’s Area of Influence (Ex. I-26) to estimate lost service opportunity and to disregard the more recent Service Opportunity Index Reports for 2019. (Exs. I-25, P-26, P-27, P-28, P-29, P-61, P-62). Because the ALJs misinterpreted and misapplied *Landmark*, the Board is unable to make a proper estimate of the dollar amount of service opportunity in the Austin AOR that is realistically available for capture by the existing Mercedes-Benz dealers but which is not being captured by them.

Vacating the Proposal for Decision is further necessary and conducive to the issuance of a final order in this contested case because the ALJs misinterpreted and misapplied § 2301.652(a)(1) of the Texas Occupations Code concerning whether the Mercedes-Benz line-make is being adequately represented as to sales and service. It is undisputed that Mercedes-Benz of Austin

satisfies all of Mercedes-Benz USA, LLC's dealership brand standards. (Proposal for Decision at p. 55). However, the ALJs determined that Mercedes-Benz of Austin was providing inadequate representation because its dealership facility is not as attractive or as well located as those of other luxury dealerships in the Austin AOR. (Proposal for Decision at pp. 54-55; Finding of Fact Nos. 34, 127). The statutory standard is whether the manufacturer or distributor is being adequately represented as to sales and service. It is not whether the dealership of the protesting dealer is less attractive or less well situated than those of competing dealerships.

For the foregoing reasons, the Proposal for Decision is vacated and this case is remanded to the State Office of Administrative Hearings so that the parties may offer additional, admissible evidence on the matters referenced above and for the preparation of a new proposal for decision, supported by recommended findings of fact and conclusions of law, based on a proper interpretation and application of applicable law and the Board's decisions interpreting and applying applicable law.

Date: _____

Guillermo "Memo" Treviño, Chair
Board of the Texas Department of Motor Vehicles

**SOAH DKT. NO. 608-19-2065.LIC
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PROTESTANT,	§	
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VS.	§	OF
	§	
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MERCEDES-BENZ OF SOUTH AUSTIN,	§	
	§	
APPLICANT,	§	
	§	ADMINISTRATIVE HEARINGS
MERCEDES-BENZ USA, LLC,	§	
	§	
INTERVENOR.	§	

APPLICANT WRITTEN MATERIALS

Applicant Swickard-Austin, LLC d/b/a/ Mercedes-Benz of South Austin hereby submits written materials in accordance with 43 Texas Admin. Code, Rule §215.60 (2021). Footnotes are from the original source.

Respectfully submitted,

By: /s/ Nicholas A. Bader

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ATTORNEYS FOR APPLICANT

Proposal for Decision at 21-23

Mr. Swickard was nominated by other MB dealers to represent them on the MBUSA National Dealer Board in 2017 and has been elected by his national dealer peers to be the Chair of the Board.¹³⁹

Mr. Swickard's MB Wilsonville facility is, in MBUSA's view, above and beyond brand requirements in terms of high-end amenities, fixtures, and finishes.¹⁴¹ MBUSA's witness Mr. Andersen, a facilities project manager for MBUSA, testified that such a facility in South Austin would improve the brand image of MB in the Austin AOR.¹⁴² Mr. Swickard's Wilsonville dealership turned the Portland metro market around from underperforming to number one in terms of registration effectiveness, exceeding sales performance expectations, and ranking 28th of 384 dealers on key metrics measured by MBUSA in its Dealer Performance Ranking.¹⁴³

Mr. Swickard testified that his MB dealerships focus on attracting entry-level customers in order to grow business and gain new customers.¹⁴⁴ He took efforts to make MB vehicles more affordable by selling . . . loaner vehicles and other nearly-new vehicles that can be sold for less than brand-new vehicles.¹⁴⁵ He testified that his goal is to take the pretension and judgment out of luxury car buying and to make it comfortable and achievable for everyone.¹⁴⁸

He stated that he intends to be personally involved in the dealership and to spend as much time as he can in Austin.¹⁵⁰ Mr. Swickard intends for the South Austin facility to be as well-designed as the competing BMW dealership located nearby.¹⁵²

¹³⁹ Tr. at 104-05, 286-88.

¹⁴¹ Tr. at 679-80.

¹⁴² Tr. at 679-80.

¹⁴³ Tr. at 61, 102-03, 284, 286-89; Exs. I-33, I-40.

¹⁴⁴ Tr. at 59.

¹⁴⁵ Tr. at 59-60.

¹⁴⁸ Tr. at 69.

¹⁵⁰ Tr. at 78.

¹⁵² Tr. at 92.

Exhibit I-71 – 013, 023, 029**Table 5. Employment by Metropolitan Area
(Seasonally adjusted)**

	Employment (thousands)		Total Employment Growth	Average Annual Employment Growth
	Jan. 1990	Feb. 2019	Jan. 1990-Feb. 2019	Jan. 1991-Feb. 2019
Austin	387.1	1,080.5	179%	3.63%
Houston	1,734.2	3,130.1	80%	2.00%
Fort Worth	605.1	1,066.4	76%	2.00%
Dallas	1,400.4	2,676.7	91%	2.26%
San Antonio	547.1	1,068.8	95%	2.39%
El Paso	209.1	319.3	53%	1.49%
Texas	7,023.9	12,666.3	80%	2.04%
U.S.	109,197.0	150,606.0	38%	1.12%

Source: U.S. BLS; Federal Reserve Bank of Dallas; author's calculations

Table 7. Average Annual Wage Growth by Metropolitan Area: 1991-2017

Industry	Dallas-				
	Austin	Fort Worth	El Paso	Houston	San Antonio
Construction	3.71%	3.65%	3.49%	3.52%	3.96%
Education and Health Services	3.55%	3.05%	2.60%	3.12%	3.04%
Financial Activities	4.81%	4.29%	3.53%	4.53%	4.25%
Information	4.27%	4.14%	2.95%	3.55%	4.06%
Leisure and Hospitality	3.47%	2.81%	2.62%	2.48%	2.98%
Manufacturing	4.58%	3.64%	3.98%	3.52%	3.88%
Natural Resources and Mining	6.91%	4.16%	5.59%	4.80%	5.45%
Other Services	3.56%	3.26%	3.37%	3.53%	3.30%
Professional and Business Services	4.36%	3.99%	2.48%	4.19%	3.89%
Public Administration	3.41%	3.29%	3.24%	3.27%	3.05%
Trade, Transportation and Utilities	4.18%	2.80%	2.56%	3.32%	3.04%
Unclassified	4.70%	3.80%	15.02%	1.78%	5.55%
Total, All Industries	3.84%	3.28%	2.85%	3.45%	3.32%

Source: TWC QCEW; author's calculations

Table 10. Household Income by Strata in Austin MSA: 2009 and 2017

<i>Household Income</i>	2009		2017	
	<i># Households</i>	<i>Share of All Households</i>	<i># Households</i>	<i>Share of All Households</i>
Less than \$10,000	37,393	6.42%	37,516	5.18%
\$10,000 to \$14,999	23,665	4.06%	22,466	3.10%
\$15,000 to \$19,999	23,953	4.11%	23,302	3.22%
\$20,000 to \$24,999	27,207	4.67%	28,702	3.96%
\$25,000 to \$29,999	28,903	4.96%	28,109	3.88%
\$30,000 to \$34,999	30,301	5.20%	29,090	4.01%
\$35,000 to \$39,999	28,968	4.97%	29,608	4.09%
\$40,000 to \$44,999	30,547	5.24%	30,840	4.26%
\$45,000 to \$49,999	24,387	4.19%	27,983	3.86%
\$50,000 to \$59,999	48,829	8.38%	54,213	7.48%
\$60,000 to \$74,999	60,551	10.39%	76,697	10.59%
\$75,000 to \$99,999	76,882	13.20%	96,918	13.38%
\$100,000 to \$124,999	52,140	8.95%	75,476	10.42%
\$125,000 to \$149,999	30,260	5.19%	47,317	6.53%
\$150,000 to \$199,999	29,652	5.09%	53,796	7.42%
\$200,000 or more	28,894	4.96%	62,533	8.63%
Total	582,532		724,566	

Note: Household income is over the past 12 months in inflation-adjusted 2009 and 2017 dollars.

Source: U.S. Census 2005-2009 and 2013-2017 American Community Surveys

CERTIFICATE OF SERVICE

I hereby certify that on this 11th day of March, 2021, I will serve the above and foregoing on all counsel of record via eFileTex.gov or email.

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INTERVENOR.	§	

INTERVENOR MERCEDES-BENZ USA, LLC’S WRITTEN MATERIALS

These materials reproduce excerpts from the SOAH administrative record. Footnotes are the footnotes in the original source; added record citations are contained in brackets and italicized.

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Certificate of Service: I certify on 3/11/21, I will cause service of these materials on all parties.

/s/ Lloyd E. Ferguson

I. PFD at 69, 94 (FOF 189) (rejecting MB of Austin’s experts’ analyses)

“The ALJs are also not persuaded by Mr. Stockton’s and Dr. Hatch’s projections and analyses. Mr. Stockton’s projections are based on non-statistically significant results that are doubled, though he says he merely rounded up.⁴⁵⁰ Neither Mr. Stockton nor Dr. Hatch used

⁴⁵⁰ Tr. 1039-42; Ex. P-1 at 244.

methodologies that have been accepted by the automotive industry or the Board, and their chosen methodologies are not improvements upon the accepted methodologies used by Ms. Heinemann and Mr. Farhat. Rather, the methodologies employed by Mr. Stockton and Dr. Hatch do not hold up when tested in real-world examples of new dealership establishments.”

II. MBUSA’s Reply to Exceptions at 3-4 (discussing Protestant’s Misuse of Board Decisions in *Landmark Chevrolet* and *Lee Trevino*)

“The applicant and intervenor have the burden of proving good cause to establish the new dealership. Tex. Occ. Code §2301.652(a). While the Board must consider all the statutory factors, ‘the statute does not place any emphasis on one factor over another’; the ‘question of how best to resolve the issue, including the weight to be given to each statutory factor, is a matter committed to the [Board]’s discretion,’ as is ‘whether in light of these factors there is “good cause” for licensing a new dealership.’ *Grubbs Nissan Mid-Cities, LTD v. Nissan N. Am., Inc.*, 2007 Tex. App. LEXIS 4154, *13 and *20 (Tex. App.-Austin May 23, 2007, pet. denied) (“*Grubbs Nissan*”) (affirming Director of the MVD of the TDOT’s decision dismissing existing dealer’s protest against establishment of new dealership in Grapevine, despite absence of any then current lost opportunity in the market).^[1] As the Third Court of Appeals stated in *Grubbs Nissan* (decided, by the way, years after the *Landmark* Proposal for Decision), decisions are made regarding ‘specific proposals at specific geographic points in specific markets at specific times.’ *Grubbs Nissan*, 2007 WL 1518115 at *6.”

“In contrast, MB of Austin misuses old cases to try to create standards that do not actually exist. Just as the facts and circumstances in *Grubbs Nissan* were vastly different from those in *Landmark*, discussed in *Austin Chevrolet*,² and on which MB of Austin almost

² As examples, the Third Court of Appeals in *Grubbs Nissan* noted that (1) potential for future growth in the Grapevine market was more than sufficient to sustain a new Nissan dealership, with both experts agreeing the future of Tarrant County was “optimistic,” . . . ; (2) automotive

exclusively relies, the circumstances here are dramatically different from those in *Landmark/Austin Chevrolet* and the now 36-year old Board decision in *Lee Trevino Ford*, on which MB of Austin also relies throughout its exceptions.³

* * *

“As is demonstrated in their 98-page Proposal for Decision, the ALJs carefully considered and weighed all of the evidence, including the credibility of the witnesses and the experts’ competing analyses, to arrive at their 223 separate findings of fact, all of which supported their conclusions that led them to recommend that the establishment should be allowed to move forward.”

III. *Id.* at 2 (discussing non-existent “requirement” to prove breakeven point)

“• The Board has never adopted a requirement that an applicant or manufacturer prove what the new dealer’s ‘breakeven’ point is, with the exception of some references in the 2004 *Landmark* Proposal for Decision, which the Third Court of Appeals in that case (in *Austin Chevrolet*, discussed below) neither adopted nor addressed, and which the Third Court of Appeals previously, in *Gene Hamon*, roundly rejected.”

IV. *Id.* at 22-25, 28-29 (discussing non-existent “requirement” to prove breakeven point)

“First, the ‘breakeven’ concept is simply a repackaging of a previously rejected

retail sales go through up and down fluctuations, but expected 2004 to be the start of an “up” period, expecting the retail automotive market to grow more rapidly in Dallas/Fort Worth than in Texas or the U.S.; (3) Grubbs was financially healthy, and improving, . . . which, given the flourishing market conditions, would expect Grubbs to continue to adjust its business strategy to capture the benefits of the projected economic growth . . . (4) by Grubbs’s own actions in applying for [this] dealership, it recognized the economic growth potential for the new dealership. *Grubbs Nissan*, 2007 WL 1518115 at *5-*7. Again, *Grubbs Nissan* was decided years after the *Landmark* PFD, as well as its appellate decision in *Austin Chevrolet* in the appeal of the *Landmark* Board Order.

³ *Austin Chevrolet, Inc. v Motor Veh. Bd*, 212 S.W.3d 425 (Tex. App.—Austin, 2006, pet. denied); *Landmark Chevrolet v. General Motors Corp.*, Docket No. 02-0002 LIC (Tex, DMV, MVD, Dec. 9, 2004), adopting Proposal for Decision (Sept. 16, 2004); *Lee Trevino Ford v. Payton Wright Ford*, Proceeding 302 (Tex. MVC, March 7, 1984), adopting Proposal for Decision (Jan. 30, 1984).

‘economic viability’ argument that Protestant’s counsel unsuccessfully urged in the relocation case of *Gene Hamon Ford, Inc. v. David McDavid Nissan, Inc.*, 997 S.W. 2d 298, 308 (Tex. App.—Austin 1999, pet. denied). (‘McDavid also argues: ‘Without knowing Hamon's break-even point at the proposed League City site, there is no rational way of knowing whether there is enough “lost opportunity” available to Hamon at League City without seriously harming McDavid.’) As the Third Court of Appeals stated in *Gene Hamon*, ‘Section 4.06(c) [predecessor to Tex. Occupations Code 2301.652] does not require an applicant to supply this information, and we reject McDavid's argument that harm to the protestant cannot be calculated in its absence.’ *Id.*⁵¹”

“The *Landmark* PFD, on which MB of Austin relies exclusively for the breakeven concept, did not hold it is a requirement that an applicant prove its breakeven point, as MB of Austin asserts throughout its Brief. While the *Landmark* PFD notes that the registration shortfall in 1992 was ‘well under the number of units [the Applicant] needs to break even,’ (PFD at 35), there is no analysis of ‘breakeven,’ no indication of what evidence was in the record regarding it, other than simply the number of new units the applicant suggested it might sell and GM’s planning volume. See PFD at 31-35. Beyond one or two references to ‘breakeven,’ the entirety of this section of the *Landmark* PFD deals with the profitability of the existing dealer, which is not a problem in this case. See also *Landmark*, Findings of Fact, PFD at 47, ¶ 37, at 68, ¶ 247, and at 71, ¶ 278 (mentioning only applicant’s anticipated sales and GM’s planning potential, as compared to the lost sales opportunity, discussed immediately below).”

* * *

⁵¹ McDavid even challenged that a breakeven analysis was required to be submitted to the agency under other sections of the former statute. The Third Court disagreed stating, “[t]he Board does not read section 4.02(a) to permit a protestant to challenge the adequacy of the economic information provided by a dealer seeking relocation.” *Gene Hamon*, 997 S.W. 2d at 305.

“Notably, the Third Court of Appeals in the *Landmark* case merely mentioned ‘breakeven’ once, and only in summarizing the Board’s findings; that concept did not form any part of its analysis on appeal. *Austin Chevrolet*, 212 S.W.3d at 437. Consequently, there is no precedent, or even persuasive authority, that requires an applicant to provide evidence of what its breakeven point would be, and in particular, no support for the assertion that to prevail in a protest the applicant must provide evidence of its profits and expenses, pro formas, and the like. . . . The ALJs correctly found MB Austin did not show why Swickard’s ‘breakeven number’ is necessary to show that MB Austin will not be harmed, particularly when the evidence established that sufficient opportunity exists in the market to sustain the proposed dealership. *See* PFD at 59, 62-64, and 74; [PFD] FOF 142.”

* * *

“Third, that the 1984 decision in *Lee Trevino* suggested the Board must make sure that both the existing and additional dealers will be profitable after an establishment does not provide any support for MB of Austin’s argument that MBUSA and Swickard must actually prove Swickard’s sales, revenues, debt and the like, particularly with his intent to focus on entry-level vehicle sales. In any event, *Lee Trevino* is distinguishable and not dispositive.⁵⁹”

* * *

“Finally, and perhaps most telling, MB of Austin’s expert for possible harm to MB of Austin, Edward Stockton, did not opine that he could not fully assess potential harm to MB of Austin without knowing Swickard’s breakeven point. When assessing harm to MB of Austin,

⁵⁹ *See* Exceptions, ¶3 and throughout the brief citing *Lee Trevino Ford* . . . In *Lee Trevino*, Ford’s market share in the relevant market and in Fort Worth was consistently way above Ford’s national share for over ten years, even though declining (PFD at 15 and 30); in the prior five years, the whole car industry suffered “severe declines” in the throes of national recession (at 18 and 29); in the 1982-evaluation year, Ford would only have needed 9 cars and 12 light trucks to meet national benchmark (at 22); the closest Ford dealer had not been profitable at all for three to four years (at 33); and increased convenience would be minimal, as the three closest Ford dealers were within 12- and 15-minute drives of the proposed site (at 34).

Mr. Stockton apparently did not care how many sales Mr. Swickard needs to breakeven, or even how many sales Mr. Stockton claims he will make. The ‘breakeven’ concept is something MB of Austin concocted from its reading of the *Landmark* PFD, but which it failed to note any analysis in that case of the concept, or the complete lack of mention of breakeven evidence or required proof in the appellate decision of that case, *Austin Chevrolet*, in its discussion of harm to the existing dealer under the fourth factor, or any other factor. Any purported proof of ‘breakeven’ is therefore irrelevant, and every single exception that relies on it should be rejected.”

V. PFD at 64, 74 (rejecting MB of Austin’s prior decision analysis and purported “requirement” to prove breakeven point)

“The ALJs find that MB Austin did not show why Applicant’s ‘breakeven number’ is necessary to show that MB Austin will not be harmed when the evidence established that sufficient opportunity exists in the market to sustain the proposed dealership.”

* * *

“The ALJs agree with MBUSA’s reading of *Lee Trevino*. That PFD did not discuss requiring proof of the proposed dealership’s estimated revenues and expenses; rather, it discussed the profitability of the existing dealerships.⁴⁸⁰”

VI. MBUSA’s Reply to Exceptions at 13-15, 28-29 (discussing failure of Protestant’s lost opportunity argument and appropriateness of MBUSA’s asserted standard)

“ . . . MB of Austin’s reliance on the *Landmark* Proposal for Decision for its mantra that there is no ‘reasonable’ or ‘realistic’ lost opportunity is simply wrong. The Third Court of Appeals, in the appeal of the *Landmark* Board decision, expressly approved of gross loss and all insell, as Mr. Farhat did here, as the appropriate standard of lost sales opportunity in a market. *Austin Chevrolet*, 212 S.W.3d 425, 437 (Tex. App.—Austin 2006) (reh. overruled). . . . Unlike in

⁴⁸⁰ *Lee Trevino*, PFD at 29.

the *Landmark* PFD, using gross loss and all insell is not ‘pie-in-the-sky optimism’ as the ALJ in that case stated in the unique facts of that case. Consequently, the ‘realistic’ and ‘reasonable’ calculation of lost opportunity is gross loss and insell under the appropriate comparative benchmark. MB of Austin did not challenge Mr. Farhat’s use of the national or Texas state benchmarks, nor his assessment of the reasonableness of those benchmarks to assess the Austin market for Mercedes-Benz vehicles.”

“MB of Austin also ignores the further facts found by the ALJs here that the lost sales opportunity model does not take into account future population and economic growth in the Austin AOR, which Dr. Nivin testified about without any dispute by MB of Austin. That is, the lost opportunity was calculated from a 2018 snapshot, and will grow with the growth of the Austin AOR. The Austin historical and prospective growth are in stark contrast to those in *Austin Chevrolet*, where the Third Court of Appeals noted that in 1993, the Houston market was ‘characterized by a “decade of sluggishness, a declining trend in automobile sales, stagnant wages, substantial layoffs, and only modest growth projections.”’ 212 S.W.3d at 434.”

“Using gross loss and all insell has been adopted in a number of Board and appellate decisions. *See, e.g., RCJD Motors, Inc. v. Huffines Dodge Plano, L.P., SOAH Docket No. 608-10-5694.LIC, MVD Docket No. 10-0048.LIC, Final Order (Tex. DMV, MVD, July 12, 2012)*, adopting with minor modification, Proposal for Decision (Apr. 2, 2012), Final Order at 6 and PFD at ¶ 60 and 42 (ruling use of gross loss and insell methodology as appropriate means to determine amount of untapped opportunity in market); *Graff Chevrolet Co. v. Tex. Motor Veh. Bd.*, 60 S.W.3d 154 158, n.4, 159-60 (Tex. App.—Austin 2001, no writ) (affirming Board’s decision in *North Arlington Co. v. Graff Chevrolet*, Docket No, 97-777 (Sept. 1999), adopting Proposal for Decision (July 19, 1999), PFD at 18-21 (using gross loss and insell as measure of lost opportunity); *Burns Motors Ltd. v. Payne Edinburg*, SOAH Docket No. 608-17-1285.LIC,

MVD Docket No. 16-0028.LIC (Tex. DMV, MVD, June 14, 2018), *adopting*, Proposal for Decision (Feb. 15, 2018), PFD at 71 (Board counted all insell as lost opportunity that the protestant could have captured but did not from outlying dealers, based on Mr. Farhat’s analysis).”

VII. PFD at 92, FOF 160, 161, 165, and 166 (based on analysis at 62-69 (embracing MBUSA’s lost sales and opportunity analysis)

“160. MB Austin should not experience any lost sales because the new dealership can capture opportunity existing in the market such as lost registrations in the South Austin AOI and in-sell of entry-level vehicles.”

“161. As of 2018, a total lost opportunity of 755 sales (474 units of gross loss and 281 units of in-sell) existed in the Austin AOR.” *[Ex. I-65 at 099]*

* * *

“165. Based on the sales patterns of MB Austin and MB Georgetown, the new dealership is projected to sell from 500-700 new vehicles per year.” *[Ex. I-65 at 099; Tr. 504:1-509:7]*

“166. That range is below the total lost opportunity of 755 units in 2018, thus the new dealership need not take any sales from the existing dealers.”

VIII. MBUSA’s Reply to Exceptions at 48 (discussing standard for evaluating harm)

“. . . The only standard that the Board has consistently, and for decades, applied [to measure harm to an existing dealer] is ‘whether the establishment will cause so much harm . . .

“as to cause the failure of the [existing] dealership or at least reduce the existing dealer’s profitability to such extent that it could not properly serve the public.” *RCJD*, Final Order at 7, ¶

70; PFD at 41 (quoting *Rockwall Imports v. The Allee Corp.*, *SOAH Docket No. 601-09-*

1276.LIC, *MVD Docket No. 09-0014.LIC* (Tex. DMV, MVD, Jan. 23, 2012), *adopting*, *Proposal*

for Decision (Apr. 20, 2011), PFD at 60, fns. 249 and 250); *see also* *A.C. Collins Ford v. Charlie*

Thomas Ford, Docket No. 87-206 (Tex. MVC, Sept. 6, 1989), adopting as modified, Proposal for Decision (July 14, 1989) PFD at 22, on which MB of Austin relies (“To sustain losses of the magnitude predicted by [protestant’s expert] would result in a reduction of the ability of the dealership to provide service to the public and ultimately go out of business’).”

IX. MBUSA’s Reply to Exceptions at 50-51 (discussing MB of Austin’s profitability and showing lack of harm)

“Those straight-up financial facts are set out by the ALJs in their discussion on the fourth factor, and each was amply supported by the extensive testimony of MBUSA’s forensic accountant Suzanne Heinemann that the ALJs cited (at 71-73 of the PFD):”

- “• Every year since 2015, MB Austin’s net profit has exceeded the benchmark composite groups (FOF 168), with net profit of \$ 5,247,335 in 2015, \$ 4,989,833 in 2016, \$ 4,734,182 in 2017 and \$ 5,616,638 in 2018.¹³⁴”
- “• As of 2018, MB Austin had no long-term debt; a cash position of \$4.6 million, a net cash position of nearly 600 percent, and working capital of 200 percent of what MBUSA requires for a healthy dealership; its net profit for 2018 exceeded its total net fixed assets after depreciation (\$5.6 million versus a little under \$4 million); and MB Austin’s return on equity is very high and far exceeds the average of the composite groups (FOF 169).” [*Tr. 730:23-735:19; 748:8-750:24; Ex. I-14*]
- “• MB Austin’s profitability is not dependent on its new-vehicle sales volume. Specifically, in 2018, MB Austin’s profit increased from \$4.7 million to \$5.6 million, despite selling 16 percent fewer new vehicles than in 2017 (FOF 170).” [*Tr. 750:25-754:14*]
- “• MB Austin generates a higher amount of revenues from its fixed operations (service, parts, and body shop departments) than the benchmark groups, and the profit margins in fixed

¹³⁴ See Exs. I-8, I-9, I-11, and I-14, respectively, at 1, bottom right summary box.

operations are much higher than those in the new or used vehicle departments (FOF 171).”

[Tr. 750:25-754:14]

- “• MB Austin’s net profit in its fixed operations exceeds all of its fixed expenses by 1.72 times, which is more than the composite groups (FOF 172).” *[Tr. 764:7-765:5]*
- “• MB Austin is in a better financial position than most dealerships because fixed operations are more recession-proof than vehicles sales: if customers are not buying new cars, then they will need to have their old cars serviced (FOF 173).” *[Tr. 761:12-764:6]*
- “• Because its net profit from fixed operations fully covers its fixed expenses, MB Austin has more flexibility in its new and used vehicle departments (FOF 174).” *[Tr. 761:12-764:6]*
- “• MB Austin has a large used vehicle department with higher profit per vehicle than the benchmark groups (FOF 175).” *[Tr. 752:23-753:16]*
- “• In 2018, MB Austin increased its gross profit on finance, insurance, and service contract products sold with new vehicles, and made a higher profit than previous years on the sale of those items while maintaining its higher-than-average gross profits on new vehicles (FOF 176 and 178).” *[Tr. 766:4-769:10]*
- “• MB of Austin has had higher than average gross profit on sales of new vehicles, charging more for vehicles than its peers on an average per unit basis (FOF 177).” *[Tr. 769:11-775:22]*

“These are the very financial facts—that MB of Austin is ‘so profitable and financially successful [to] withstand competition from an additional dealer’ —that will allow MB of Austin to ‘easily adjust its business strategy [to meet] additional competition,’ and that ‘will allow it to compete effectively with a new dealership.’ as the ALJs found in [FOF] 167, 178 and 191 . . .”

X. Order No. 15 Denying Protestant’s Motion to Reopen or Abate, Taking Official Notice, and Denying Request to Strike MBUSA’s Response (7/1/2020) at 2 (denying MB of Austin’s efforts to reopen evidentiary record re COVID-19 related issues)

“Based on the pleadings, MB Austin’s motion to reopen the evidentiary record, establish deadlines for parties to file new expert reports, and set a date for hearing on those expert reports; or in the alternative, reconsider Protestant’s prior motion to abate this proceeding is **DENIED** for the reasons urged by MBUSA in its response.”

XI. MBUSA’s (1) Opposition to Protestant’s Second Motion to Reopen the Record, or Alternatively, to Reconsider Motion to Abate and (2) Strike Stockton Affidavit at 1-2 (6/5/20) (citing the reasons urged by MBUSA, and adopted in Order No. 15)

“Despite what Protestant MB of Austin characterizes as a ‘seismic shift’ in the societal and economic conditions of the country (MB of Austin’s Motion, ¶ 5 at 3), . . . [h]ere are the facts:”

- “• As of April 30, 2020,¹ MB of Austin’s new vehicle sales for January through April are up 14 units over the same period in 2019 (258 versus 244) New vehicle sales in April 2020 alone were higher than in April 2019 (74 versus 68 last year)”
- “• MB of Austin sold just four fewer used vehicles this year through April 2020 than through April 2019 (440 versus 444)”
- “• MB of Austin’s net profit through April 30, 2020 is \$ 2,087,969, which is \$ 600,000 over its net profit through April 2019, and \$300,000 over its 2018 net profit for that same period, which puts it on track this year to realize about \$ 6,264,000 in net profit.”

¹ Financial information for month-end April 2020 is the most recent dealer financial statement . . . as of the date of this response. The unsworn declaration of MBUSA Manager Fred W. Newcomb, Jr. sets out the information from MB of Austin’s April 2019 and April 2020 dealer financial statements as submitted to MBUSA in the ordinary course of business. Newcomb unsworn declaration, ¶ 5. MB of Austin’s year-end 2018 financial statement, showing its monthly sales and profits, is Hearing Exhibit I-14. . . .

XII. Id. at 4

“Every one of MBUSA’s bullet points in its opposition to MB of Austin’s initial motion (April 17, 2020 Opp. at 3-4 and throughout) are still true—the economic downturn is limited, at most may go into 2021; we are still three plus years from the date of a Proposal for Decision in this matter before the South Austin dealership would ever open; MB of Austin has been allowed even under the initial shelter-in-place orders to continue its sales and service business, and its current financial statements reflect its success in that regard; all of MBUSA’s experts already anticipated and opined on the effects of a recession in 2020 on Austin specifically . . . ; Mercedes-Benz assembly plant in Alabama is open and running; and Mr. Hardeman has completely expressed his lack of concern in the current economic downturn by buying an Audi dealership on April 10, 2020 in San Juan. . . .”

XIII. Id. at 3

“. . . As Dr. Nivin testified, and without dispute, Austin and the Texas and U.S. economies will rebound from any recession in 2020 in less than one to two years.³ That is long before the South Austin dealership would ever be ready to open for business^[1]”

XIV. Id. at 7

“. . . Perhaps most important, this economic downturn was caused by the shelter-in-place orders that temporarily shut down huge swaths of the economy consisting of mostly flourishing businesses As . . . businesses begin to reopen, per the Governor’s more recent orders,¹² unemployment will ease, people will spend money again, and the economy should begin to recover. Consequently, the effects of the pandemic shutdowns will be in the rear-view mirror way before Mr. Swickard is ready and able to open his new dealership.”

³ Tr. 11/12/19, 183:21-184:13, 196:18-197:8.

¹² See GA-26, attached to Ferguson unsworn declaration as Ex. 2.

XV. MBUSA’s Reply to Exceptions at 8-10 (discussing Austin’s resiliency in recessions and MBUSA’s experts anticipated and accounted for a recession in 2020 or 2021)

“[As Dr. Nivin testified,] [w]hile all area economies decreased during the 2008 recession, Austin’s did not fall quite as much and bounced back stronger and more quickly, due largely to its diversification over the last 15 years.¹³ Undisputed are Dr. Nivin’s opinions that not only has the Austin economy shown a strong ability in the past to absorb a recession and recover from it relatively quickly and strongly,¹⁴ but also should a recession occur in the next year or two (i.e., 2020 or 2021), Austin’s economy will dip some, but not as much as other areas of the country, and will bounce back strongly, as it has in the past.¹⁵”

* * *

“As Suzanne Heinemann, a forensic accounting expert testified, MB of Austin’s operational strengths are in more recession-proof areas, not reliant on new vehicle sales for its profitability—MB of Austin’s overall higher revenues, higher gross profit margins in the new and used vehicle departments, its higher number of used vehicles per new vehicle sold with higher gross profit per used unit it sells and, in particular, its high net profit in fixed operations (i.e., its service and parts business)—are all critically important.²¹ As she explained, fixed operations are more recession-proof, because consumers still have to have their vehicles serviced, a life blood for a dealer in a down market, even if consumers are buying fewer new cars.²² . . . [T]he hearing evidence fully addressed the prospect of an economic downturn or

¹³ Tr. 11/12/19, [167:6-168:11], 169:22-171:2; Ex. I-71, Charts 6, 10 and 11 at 9, 15 and 16.

¹⁴ Ex. I-71 at 14.

¹⁵ Tr. 11/12/19, 183:21-184:13.

²¹ See MBUSA’s post-hearing Opening Brief at 79-82. [Tr. 11/15/19, 752:23-769:10; 774:14-775:4; 818:22-820:4].

²² Tr. 11/15/19, 761:12-23. Contrary to MB of Austin’s Exception in ¶ 53, Ms. Heinemann’s testimony, unrebutted by MB of Austin, and her underlying analysis, is the evidence on which the ALJs based their FOF ¶ 213.

recession in 2020 and 2021. It is . . . still undisputed, that the reasonably foreseeable economic conditions in the Austin metropolitan area will remain very strong over the next ten years.”

XVI. ALJ’s Letter Regarding Exceptions (8/21/20) at 2

“ . . . MBUSA adequately explained in its reply to exceptions the reasons why we did not abate the proceedings or reopen in the evidentiary record post-hearing because of the Covid-19 pandemic. We reviewed the issue and accepted MBUSA’s arguments, as stated in Order No. 15 and referenced in Finding of Fact No. 10. Those reasons will not be restated here.”

XVII. Exhibit I-71 – 012, 037

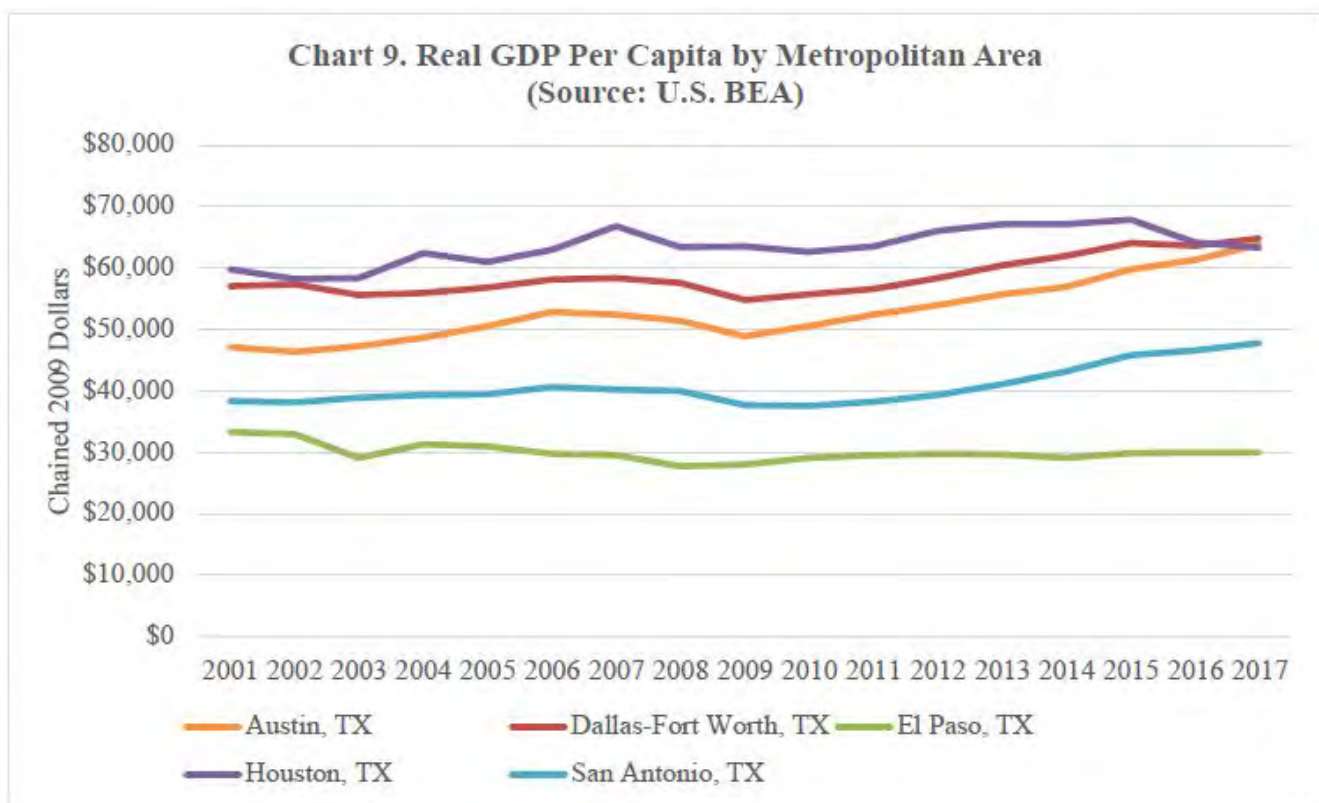


Table 15. Annual Economic Impacts of the Full Operations South Austin Mercedes Benz Dealership

<i>Impact</i>	<i>Employment</i>	<i>Labor Income (2019 \$)</i>	<i>Contributions to GRP (2019 \$)</i>	<i>Output (2019 \$)</i>
Direct	109	\$7,033,820.25	\$41,145,665.84	\$107,795,889.99
Indirect	175	\$9,949,583.63	\$17,061,588.50	\$29,062,205.50
Induced	91	\$4,610,975.68	\$8,148,987.50	\$13,605,384.11
Total	376	\$21,594,379.55	\$66,356,241.85	\$150,463,479.60

To: Texas Department of Motor Vehicles Board
From: Sandra Menjivar-Suddeath, Internal Audit Division Director
Agenda Item: 6.A
Subject: Fiscal Year (FY) 2021 Second Six Month Internal Audit Plan and Risk Assessment Report

RECOMMENDATION

To approve the FY 2021 Second Six Month Internal Audit Plan.

PURPOSE AND EXECUTIVE SUMMARY

The Texas Department of Motor Vehicles Board approves the Internal audit plan each year to be in compliance with the Texas Internal Audit Act (Texas Government Code 2102.008). The FY 2021 Second Six Month Internal Audit plan provides information for engagements in the second half of the fiscal year, including an hour analysis and engagements. The plan also outlines divisional initiatives and added-value services for the second six months.

The Second Six Month Internal Audit Plan was developed based on the results of the second half risk assessment where IAD reviewed and evaluated 315 risks.

FINANCIAL IMPACT

No Financial Impact.

BACKGROUND AND DISCUSSION

The TxDMV Board approves the Internal audit plan each year to be in compliance with the Texas Internal Audit Act (Texas Government Code 2102.008). The FY 2021 Second Six Month Internal Audit plan provides information for engagements in the second half of the fiscal year, including an hour analysis and engagements. The plan also outlines divisional initiatives and added-value services for the second six months. The plan includes five engagements, divisional initiatives, and added-value services for the first six months.

Second Half Risk Assessment Results

IAD assessed 315 risks during the second half risk assessment. The risk assessment results in identifying 39 High and Very High Risks.

Second Half Engagements

IAD identified five engagements that it will conduct during the second six months of the fiscal year. Out of the five engagements, three engagements are required and two engagements are risk-based. The two risk-based engagements are tied to the four themes presented in the first half internal audit plan: Transformation, Information Technology, Human Resources, and Procurement and Supply Chain Management. The specific engagements are as follows:

- **Payment Card Industry Requirement 1 - Firewalls:** This audit engagement would review PCI Compliance with the firewall requirement as Firewalls are essential security devices of a network. Firewalls help protect networks from outside threats.
- **Strategic Communication:** This engagement would review how communication is disseminated and the effectiveness of communication.

The three required engagements include the Quality Assurance and Improvement Program – External Assessment, the Audit Recommendation Implementation Status Follow-Up, and the FY 2022 First Six Month Internal Audit Plan and Risk Assessment.

The five engagements are estimated to take 1,875 hours.

Contingency Engagements

The second half plan also includes contingency engagements that could be done in lieu of one of the second half engagements. The contingency engagements are the following: Incident Response Communication, Business Continuity, Staff Retention and Recruitment, Strategic Purchasing, or Contract Development.

Divisional Initiatives and Added-Value Services

In addition to the engagements, IAD conducts other value-added services and works on divisional initiatives to improve IAD's effectiveness and efficiency. IAD plans on working and conducting the following:

- Key Risk Indicators
- Staff Development Plans and Training
- TeamMate + Development
- Board and Executive Communication
- Fraud, Waste, and Abuse (FWA) Items
- External Coordination Efforts
- Ad hoc Advisory
- Work Group Participation
- Department Training

Second Six Month Internal Audit Plan and Risk Assessment Results Summary

Summary

IAD assessed 315 risks during the second six month risk assessment, including the original 247 risks identified in the first half risk assessment. The additional 68 risks were identified in one of the first half engagements or through the emerging risk area research.

As part of the six month risk assessment, IAD worked with divisions to obtain updates on the high and very high risks that had mitigation plans and used the information to rescore those risks. Through that process, IAD was able to decrease the number of High and Very High risks. The charts below depict the changes of scores for the risks identified in the first half risk assessment, all risk scores for second risk assessment, and the risks that are in scope for second half or have been tested during the first half.

For the second half risk assessment, IAD identified 39 High and Very High Risks.

Chart 1. Current Scores for First Half Risks

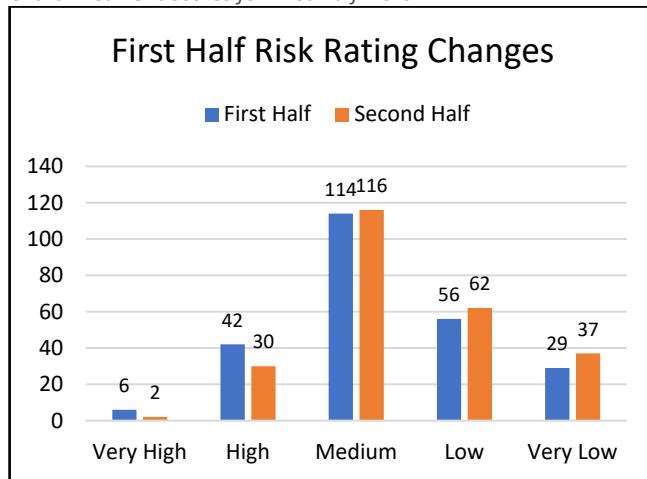


Chart 2. Current Risk Score Information

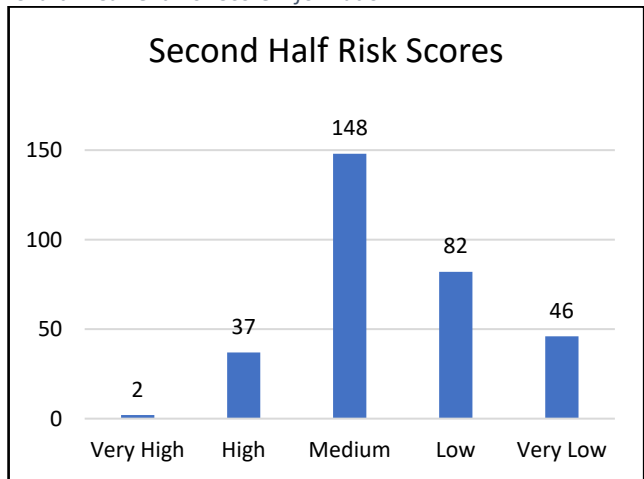
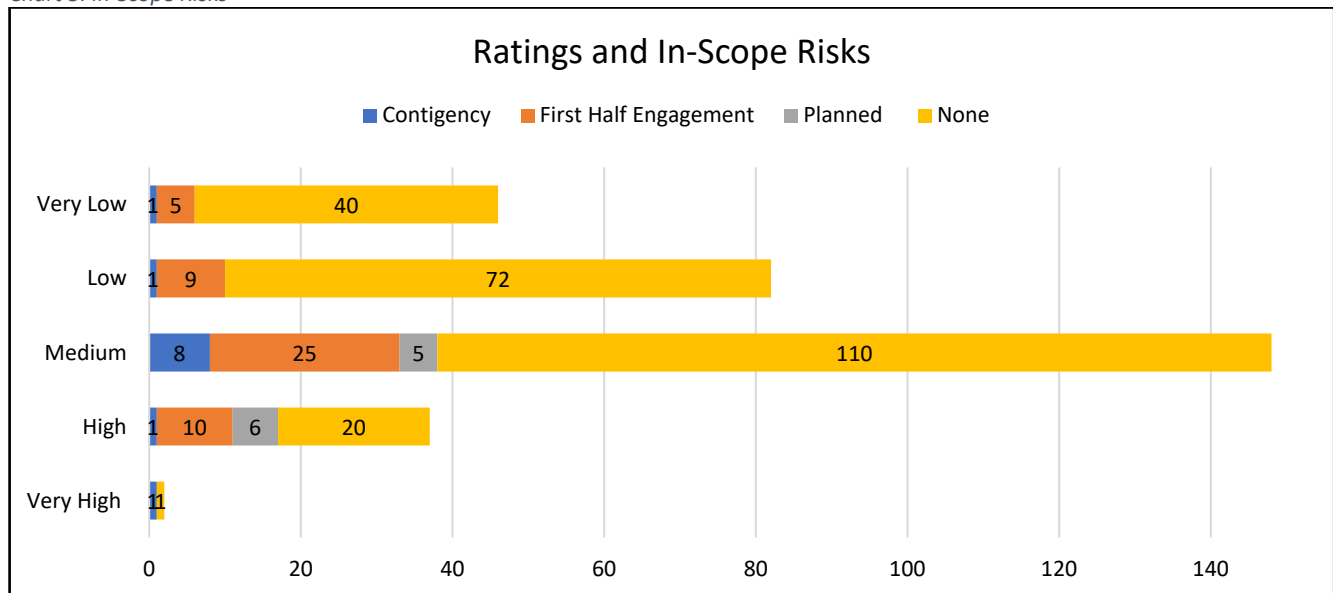


Chart 3. In-Scope Risks



First Half High and Very High Risks

The risks from the first half that were considered High or Very High have been mostly addressed as depicted in Chart 1. In the first half risk assessment, IAD identified 48 high and very high risks. Out of those 48, the Department has mitigated 20 (42%) of them through mitigation plans or IAD evaluating the risk in an engagement.

Second Half High Risk Areas

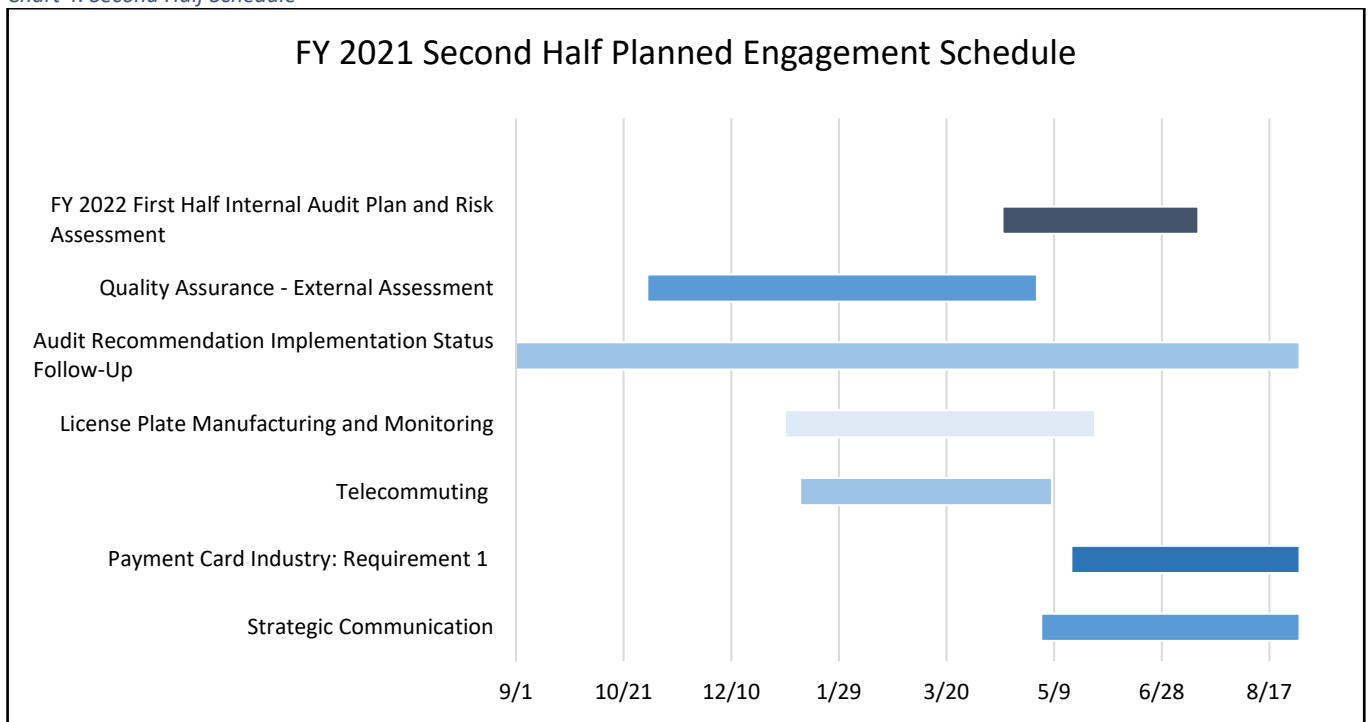
Based on the analysis, IAD identified the following areas as high risks to be considered in the second half plan:

- Strategic Communication
- Payment Card Industry (PCI): Requirement 1 – Maintain and Install a Firewall
- Business Continuity
- Incident Response & Communication
- Staff Recruitment & Retention
- Strategic Purchasing
- Contract Development

Second Half Internal Audit Plan

Out of the seven risk areas, IAD selected Strategic Communication and PCI: Requirement 1 (Firewalls) to audit in the second half. IAD also identified three required engagements that it must conduct to stay in compliance with audit standards: Quality Assurance - External Assessment, Audit Recommendation Implementation Status Follow-Up, and FY 2022 First Half Internal Audit Plan, and Risk Assessment. These engagements are anticipated to begin in April and end by August 2021 as depicted in Chart 4. More details follow in the Second Half Internal Audit Plan.

Chart 4. Second Half Schedule





**Texas Department
of Motor Vehicles**
HELPING TEXANS GO. HELPING TEXAS GROW.

Fiscal Year (FY) 2021 Second Six Month Internal Audit Plan

Internal Audit Division

March 2021

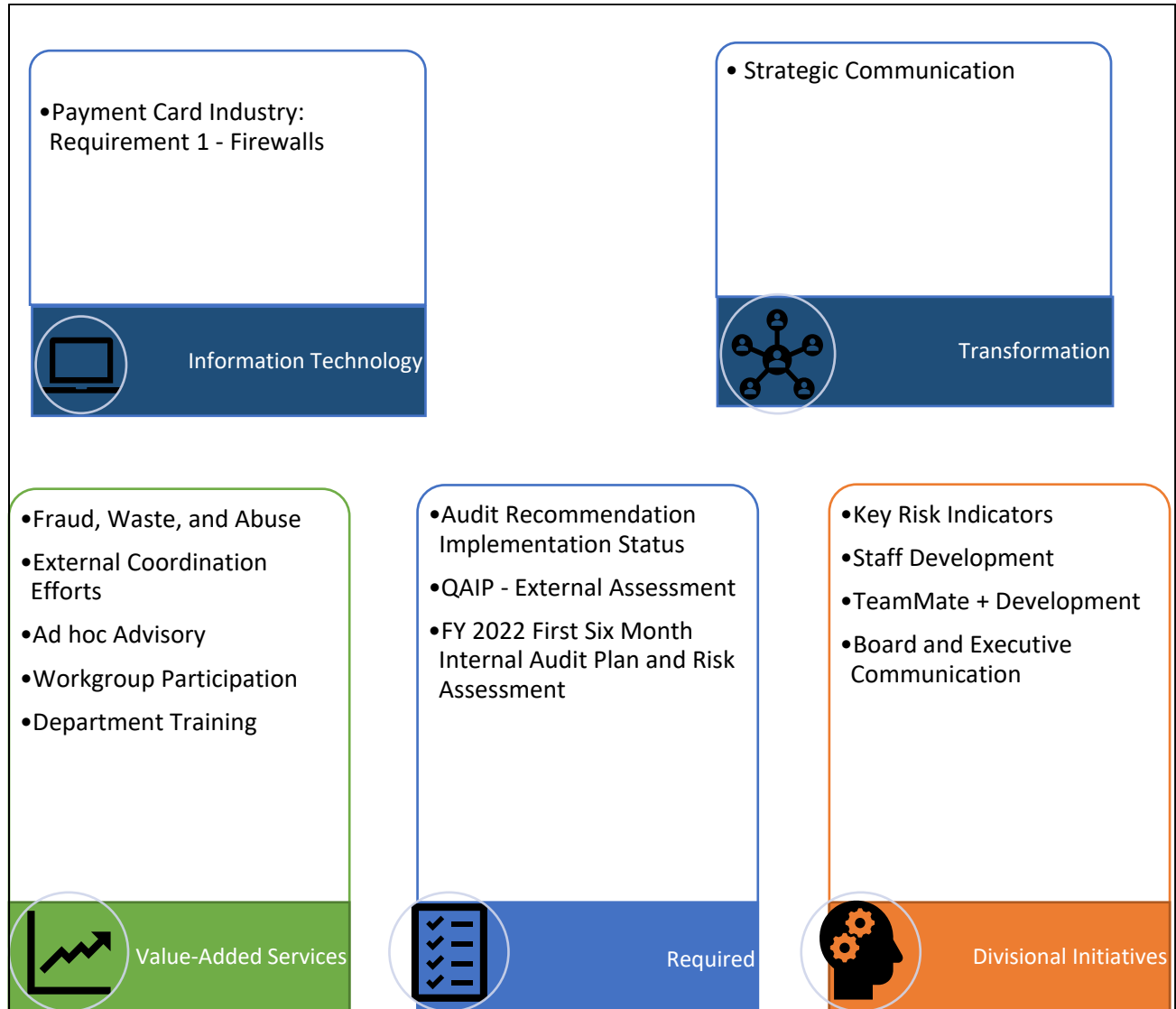
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FY 2021 Second Half Summary

The Internal Audit Division (IAD) audit plan for fiscal year (FY) 2021 is divided into two six-month plans. IAD moved to a six-month audit plan to allow for flexibility as Texas Department of Motor Vehicles' (TxDMV) risks change rapidly. The audit plan for the second half of the fiscal year includes two risk-based engagements tied to two themes and three required engagements. In addition, the plan includes division initiatives, and added-value services. The second half summary is illustrated in figure 1.

Figure 1. Second Half Audit Plan Summary



Engagement and Services Information



Risk-Based Engagements

- **Strategic Communication:** With communications occurring in traditional, digital, and social media outlets, information can be misinterpreted or ignored by key stakeholders. This can potentially cause a risk that stakeholders may miss critical facts or information that impacts their decision making or causes delays in implementation of Department rules and processes. This audit engagement would review how communication is disseminated and the effectiveness of communication.
- **Payment Card Industry (PCI) – Requirement 1:** A key objective of PCI is having a secure network and network architecture that controls entry to and exit from the network. Firewalls are essential security devices of a network. Firewalls help protect networks from outside threats. Firewalls filter and block traffic that is trying to obtain unauthorized access to the network. This audit engagement would review PCI Compliance with the firewall requirement.



Required Engagements

- **Audit Recommendation Implementation Status Follow-Up:** Verification of the implementation status for internal and external audit recommendation.
- **FY 2022 Risk Assessment and Internal Audit Plan:** An enterprise-wide risk assessment to identify the high – risk engagement areas for the upcoming fiscal year.
- **Quality Assurance and Improvement Program – External Assessment:** An external review to determine the division’s compliance with internal audit standards. The review occurs every three years and a final report with the results is produced.



Divisional Initiatives

- **Key Risk Indicators:** IAD will be finalizing and providing quarterly reporting on the following indicators:
 - *Fraud Indicators:* IAD will monitor leave balances and payment information.
 - *Regional Service Center (RSC) Transactions:* IAD will be monitoring RSC transactions to identify potential fraud.
 - *Procurement and Contract Management Monitoring:* IAD will monitor procurement and high-risk contracts.
- **TeamMate + Development:** IAD continues to enhance its audit software, TeamMate +.
- **Staff Development Plans and Training:** IAD staff take training and create development plans to obtain required knowledge, skills, and abilities.
- **Board and Executive Communication:** IAD will continue refining dashboards and other items to provide a snapshot of the Department's risk management and governance information.



Added – Value Services

- **Fraud, Waste, and Abuse (FWA) Items:** IAD is responsible for reviewing, tracking, and investigating any internal FWA allegations, including those received through the State Auditor's Office Hotline.
- **External Coordination Efforts:** IAD coordinates and facilitates any external audits. External coordination efforts include providing audit status update and coordinating responses.
- **Ad hoc Advisory:** IAD sets aside 150 hours to address any short-term assessment or information requests by TxDMV staff during the first half of the fiscal year.
- **Workgroup Participation:** IAD participates in TxDMV work groups to help identify any unforeseen risk in enterprise projects or activities.
- **Department Training:** IAD provides training to help TxDMV staff understand their responsibilities for audits, recommendation implementation, and preventing fraud, waste, and abuse.

Detailed Engagement Information

Engagements

Tables 1 and 2 provide information on the risk-based and required engagements that will be conducted in the second half of the FY 2021. The information includes engagement name, engagement hours, TxDMV strategic goal alignment, impacted division(s), and background. The background includes information on how the engagement ties to Committee of Sponsoring Organizations of the Treadway Commission (COSO) framework. Information on COSO can be found in Scope and Methodology section, under the [Committee of Sponsoring Organizations of the Treadway Commission \(COSO\) Methodology](#). Table 1 provides information on the risk-based engagement and table 2 provides information on the required engagements.

Table 1. Risk-Based Engagements

Engagement Area	Hours	Strategic Goal(s)	Impacted Division(s)	Background
Strategic Communication	900	Customer Centric Performance Driven	Government & Strategic Communication Vehicle Titles and Registration Enforcement Compliance and Investigations	The Department provides written communications, in various forms, to customers and employees with key information that impact the operations internally and externally and to employees. With the need to communicate quickly and effectively, processes should exist to ensure effective communication. This engagement ties to COSO elements of Control Environment and Information and Communication.
Payment Card Industry (PCI)	600	Performance Driven	Information Technology Services Division	The Department accepts credit cards and is required to meet PCI standards. This engagement would evaluate PCI compliance with compliance requirement 1: Install and Maintain a Firewall. This audit was identified as an area of review in the Cybersecurity roadmap. This engagement ties to COSO elements of Risk Assessment, Control Activities, and Monitoring.

Table 2. Required Engagements

Engagement Area	Hours	Strategic Goal(s)	Impacted Division(s)	Background
Quality Assurance and Improvement Program – External Assessment	100	Performance Driven	Internal Audit Division	Every three years, the division is required to obtain an External Assessment (Peer Review) on whether the internal audit function complies with the applicable professional auditing standards in all material aspects. A final report with compliance information is produced by the Peer Review team.
Audit Recommendation Implementation Status Follow-Up	75	Optimized Services and Innovation Customer Centric Performance Driven	Department-wide	An engagement to verify if outstanding audit recommendations have been fully implemented. Quarterly reporting for internal audit recommendations will be done.
FY 2022 Risk Assessment and First Half Internal Audit Plan	200	Optimized Services and Innovation Customer Centric Performance Driven	Department-wide	An engagement to identify high – risks areas where engagement may be warranted in the upcoming year.

Contingency Engagements

Table 3 denotes the potential engagements that could be performed during the second half of the fiscal year if one of the risk-based engagements cannot be done.

Table 3. Contingency

Engagement Area	Strategic Goal(s)	Impacted Division(s)	Preliminary Engagement Information
Incident Response Communication	Performance Driven	Department-wide	Over the past few years, organization's incident response plans have been used more often. As natural disasters and cybersecurity events become more common, the communication plan to staff and stakeholders should be flexible and consider different scenarios. This engagement would look at the Department's incident response plan and communication. This engagement ties to COSO elements of Control Environment, Risk Assessment, and Information and Communication.
Business Continuity	Performance Driven	Department-wide	Business Continuity Plans were activated several times over the past year to address a multitude of natural disaster events and changes have been made to plans based on those events. This engagement would evaluate the effectiveness of the Department's Business Continuity Plan and whether it accurately reflects the needs of the Department during a business continuity event. This engagement ties to COSO elements of Control Environment, Risk Assessment, Control Activities, and Information and Communication.
Staff Retention and Recruitment	Optimized Services and Innovation Performance Driven	Human Resources Division	Staff retention and recruitment begins with processes and policies that help divisions identify the talent needed to achieve organizational goals. It also includes those divisions using available policies and processes to keep employees. This engagement ties to COSO elements of Control Environment, Risk Assessment, Control Activities, Information and Communication, and Monitoring.
Strategic Purchasing	Optimized Services and Innovation	Finance & Administrative Services Division	Purchasing is a key component to ensure the Department's needs and objectives are met. Without a purchasing strategy, needs and objectives may not be met. This includes key purchases, such

Engagement Area	Strategic Goal(s)	Impacted Division(s)	Preliminary Engagement Information
	Performance Driven		as technology purchases. This engagement ties to COSO elements of Control Environment, Risk Assessment, Control Activities, Information and Communication, and Monitoring.
Contract Development	Optimized Services and Innovation	Finance & Administrative Services Division Office of General Counsel	The state continues to evolve its procurement and contract rules and regulations and has begun focusing more on the development of contracts. This engagement would review processes that exist to develop contracts and amend contracts. This engagement ties to COSO elements of Control Environment, Risk Assessment, Control Activities, Information and Communication, and Monitoring.

Scope and Methodology

Scope

The Internal Audit Plan covers activities and engagements for the second half of the fiscal year, March 2021 to August 2021, and identifies potential engagements for the second half of the fiscal year.

Risk Assessment

Risk Methodology

The audit plan was developed using a risk-based methodology, which incorporated input from TxDMV board members, executive management, division management, and risks identified by audit staff through previous fiscal year engagements and observations. IAD also analyzed TxDMV information and reviewed internal audit and industry publications to identify and rank potential audit topics by risk. In addition, IAD collected information on the potential controls that were in place to mitigate the identified risks.

Each risk was reviewed using approved Department risk guidance that included the following factors:

- Revenue or expense impact
- Asset or liability impact
- Operational effectiveness and efficiency impact
- Legal or regulatory impact
- Brand or reputational impact
- Degree of change in the program, function, or process
- Degree of complexity
- Degree of centralization
- Control design strength

315 Department risks have been identified through the risk assessment, including an additional 68 risks that had not been identified in previous risk assessments or were new risks due to the changing environments. Each risk identified was scored using the above factors to determine the engagements for the second half of fiscal year 2021 and contingency engagements.

The risk scores ranged from zero, which is the lowest risk score, to ten, which is the highest risk score. Table 4 provides information on the risk scores for each item.

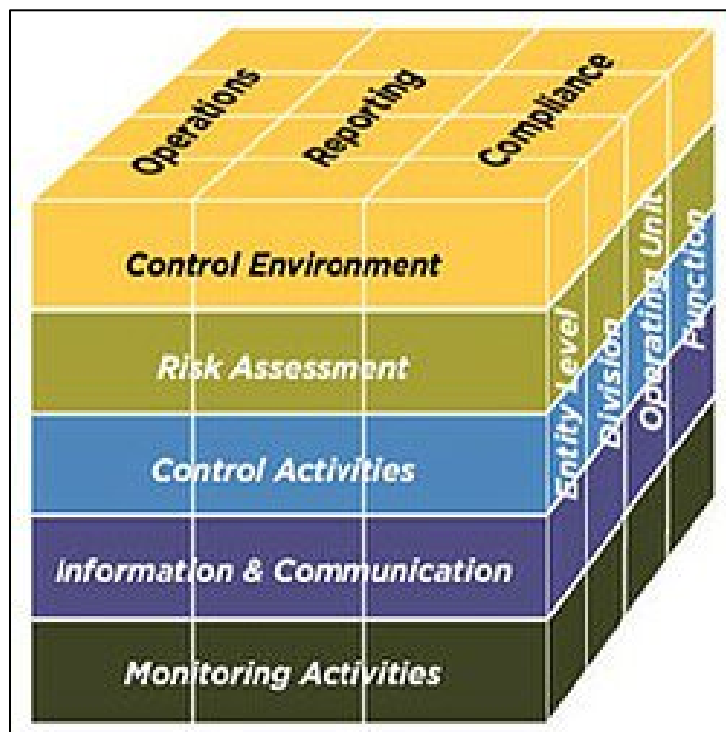
Table 4. Risk Scores

Very Low Risk	Low Risk	Medium Risk	High Risk	Very High Risk
0 - 1.49	1.5 – 2.49	2.5 – 3.49	3.5 – 4.49	4.5 +

Committee of Sponsoring Organizations of the Treadway Commission (COSO) Methodology

Once all risks were reviewed and ranked, the audit team evaluated each risk using the COSO *Internal Control – Integrated Framework*. The framework integrates three broad objectives (Operations, Reporting, and Compliance) and ties those objectives to risks and controls through five internal control components and four structural levels as depicted in Figure 2, COSO cube. The COSO cube depicts how the internal controls framework has a direct relationship between objectives, the components needed to achieve objectives, and a typical organizational structure.

Figure 2. COSO Cube



The definition for the COSO Internal Control Components are as follows:

- Control Environment:** The foundation for an internal control system. The Control Environment is a set of standards, processes, and structures that provide the basis for carrying out internal control across the organization. It provides the discipline and structure to help an entity achieve its objectives. The TxDMV Board and executive management establish the tone at the top regarding the importance of internal control including expected standards of conduct.

- **Risk Assessment:** The processes used to determine how risk is to be managed. TxDMV management assesses the risks facing the entity as it seeks to achieve its objectives.
- **Control Activities:** The actions TxDMV management established through policies and procedures to achieve objectives and respond to risks in the internal control system, which includes information systems.
- **Information and Communication:** The quality of information TxDMV management and staff generate and use to communicate and support the internal control system on an ongoing and iterative basis.
- **Monitoring:** The activities TxDMV management established to assess the quality of performance over time. The activities include ongoing evaluations, separate evaluations, or some combination of the two. The activities are used to ascertain whether each of the five components of internal control, are present and functioning.

Themes

For the FY 2021, the Internal Audit Division introduced “themes” to help organize and categorize the internal audit plan. The themes include: Human Resources, Transformation, Information Technology, and Procurement & Supply Chain Management. In addition, the themes were significantly impacted by COVID-19:

- **Transformation:** Areas where new solutions are needed to address the post COVID-19 environment, which poses difficult problems that significantly disrupt current operations.
- **Human Resources:** Areas within human resources that play a critical role in ensuring our organization has a competitive advantage in hiring and retaining staff, as well as improving morale and coaching staff.
- **Information Technology:** Areas where the spread of new technologies, data collection methodologies, and automation increases risks to our organization and customers.
- **Procurement & Supply Chain Management:** Areas in procurement and supply chain that are critical to ensure costs are being contained and services/goods are provided on time and as needed.

Hour Analysis

Engagement hours were calculated using historical data and auditor’s judgement. Hours are an estimate and could be adjusted at the beginning of an engagement.

To: Texas Department of Motor Vehicles Board
From: Sandra Menjivar-Suddeath, Internal Audit Division Director
Agenda Item: 6.B
Subject: Internal Audit Division Status

RECOMMENDATION

Briefing Only – No recommendation.

PURPOSE AND EXECUTIVE SUMMARY

The status update provides information on current Internal Audit Division (IAD) activities. The April 2021 update contains information on external coordination efforts, the fiscal year (FY) 2021 Internal Audit Plan status, and Peer Review Self-Assessment results and process. IAD updated its template to provide an update on all current engagements.

FINANCIAL IMPACT

None.

BACKGROUND AND DISCUSSION

At every TxDMV Board meeting, IAD provides an update and status on current activities, including any recent reports issued, external coordination efforts, and other activities.

External Engagements

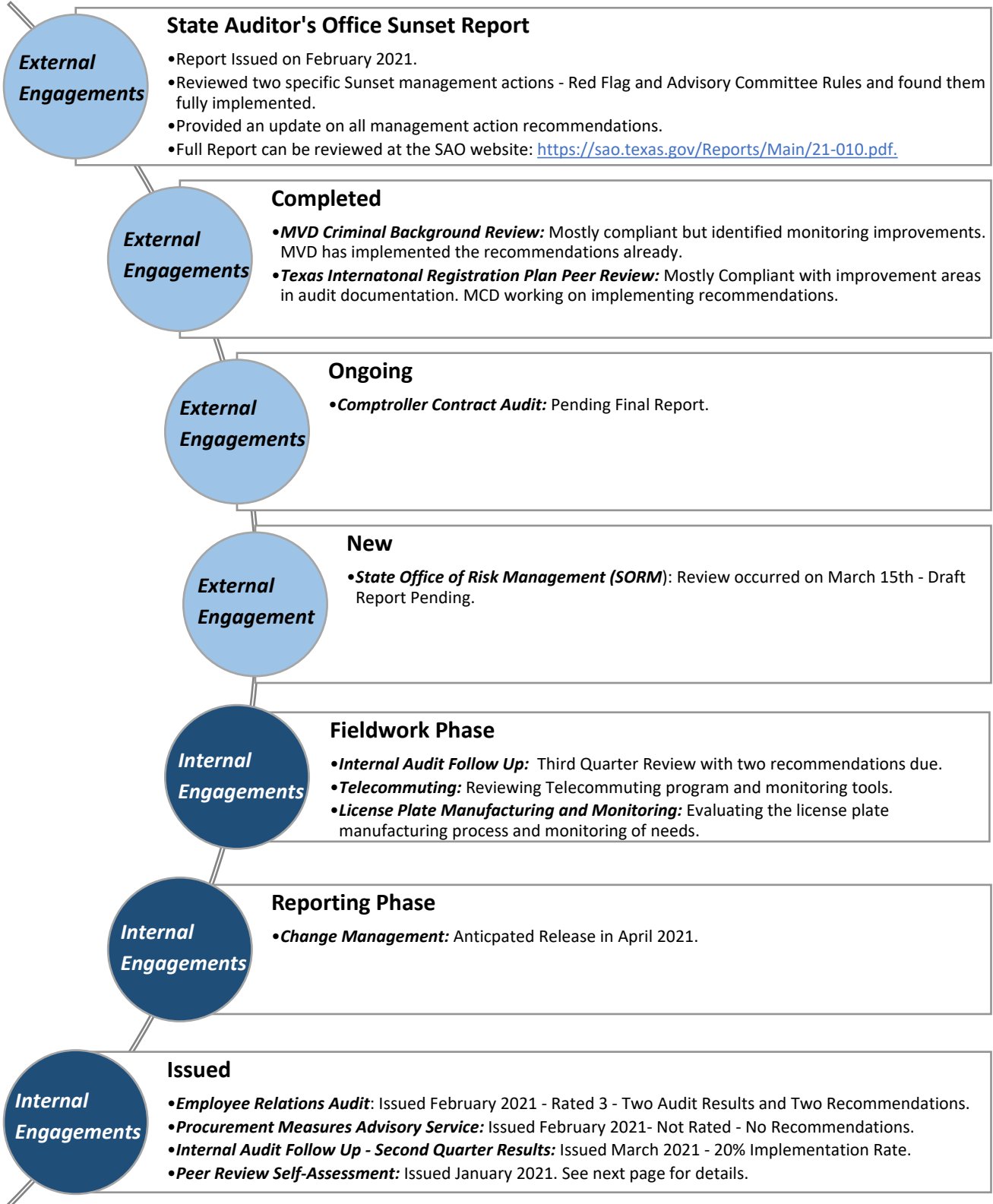
IAD tracked five external coordination efforts, including the newly released State Auditor's Office (SAO) report regarding Sunset Commission Management Action recommendations. The SAO report provided an update on where the Department is in implementing management action recommendations and validated two management action recommendations were fully implemented.

Internal Engagements

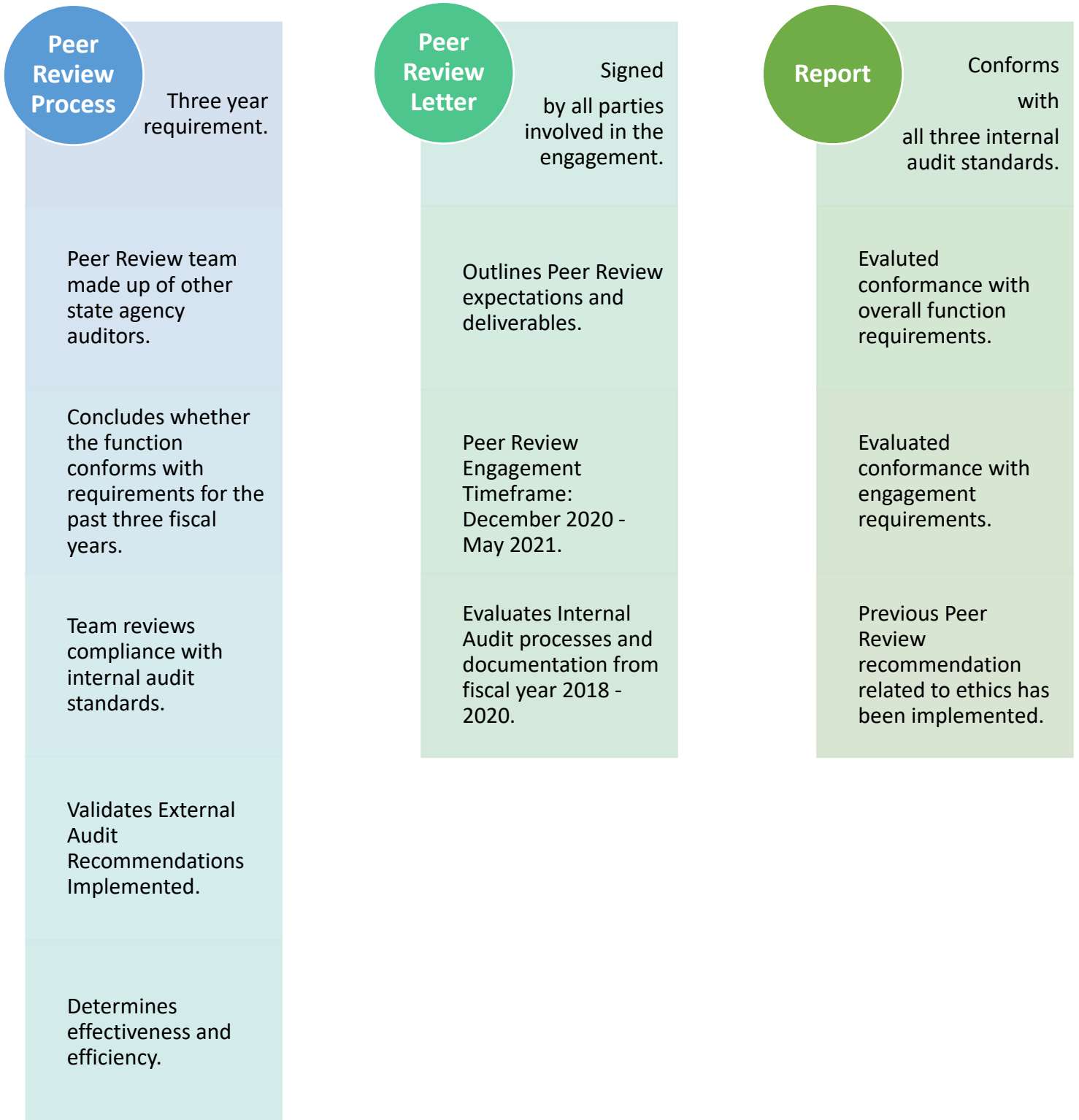
IAD worked on seven engagements in the past few months. The engagements are in various stages of completion. The Internal Audit Follow-Up, Telecommuting, and License Plate Manufacturing and Monitoring engagements are in the fieldwork phase while the Change Management engagement is in the reporting phase. IAD also issued reports or memorandums on four engagements: Procurement Measures Advisory Service, Employee Relations Audit, Internal Audit Follow-Up and the Peer Review Self-Assessment.

In January 2021, IAD issued its Peer Review Self-Assessment report. The report is a key step in the Peer Review process. The self-assessment report provides information on how the division has been in compliance with audit standards over the past three years and provides an overall conclusion on whether the division was in compliance with audit standards.

The Self-Assessment determined that IAD generally conformed with the applicable standards in all material aspects from September 2017 to August 2020. IAD has established policies and procedures to ensure compliance with applicable auditing standards. IAD followed those standards in work performed during the peer review period. IAD also fully implemented previous external audit recommendations related to ethics. The **one-pager details all key information** found in the report and outlines the Peer Review process.



Internal Audit Division – Peer Review Process





Arby Gonzales, CPA, CFE
Internal Audit Director
Texas Department of Insurance
333 Guadalupe Street
Austin, Texas 78701

Harold Rogers, CIA, CISA
Information Technology Audit Project Manager
Texas Workforce Commission
101 E 15th Street
Austin, Texas 78778

December 30, 2020

Dear Mr. Gonzales and Mr. Rogers:

This letter is to document the terms of our agreement regarding the peer review of the internal audit function at the Texas Department of Motor Vehicles. It is understood that Mr. Arby Gonzales will serve as the Peer Review Team Leader and Mr. Harold Rogers will serve as the Peer Review Team Member. No member of the review team has a conflict of interest with the Texas Department of Motor Vehicles or the Internal Audit Division.

The Peer Review Team will perform a quality assurance review of the Texas Department of Motor Vehicles internal audit activity to assess compliance with The Texas Internal Auditing Act (Texas Government Code, Chapter 2102), the Institute of Internal Auditors Code of Ethics and International Standards for the Professional Practice of Internal Auditing, and U.S. Government Accountability Office Government Auditing Standards in effect at the time the audits were conducted.

The review will be conducted in accordance with the State Agency Internal Audit Forum (SAIAF) Peer Review Manual. Completed audit and consulting projects performed by the Texas Department of Motor Vehicles Internal Audit Department from September 2017 to August 2020 (fiscal year 2018 through fiscal year 2020) may be reviewed during this engagement. The peer review team may cover any one year during that time period.

The Chief Audit Executive/Internal Audit Director (Director) agrees to:

- Provide the Peer Review Team with a completed self-assessment, reference file, and self-assessment report
- Coordinate with the Peer Review Team in sending out a survey to a sample of representatives from agency management
- Coordinate meetings with Executive Management and the Texas Department of Motor Vehicles Board Members
- Assist the Peer Review Team throughout the fieldwork process
- Review the draft report for accuracy and provide comments or clarification as needed

- Provide management responses to the report as needed

The Board Members agree to:

- Be kept informed of the Peer Review Progress
- Respond to answers from the Peer Review Team
- Review the final report on the observations and recommendations

The Peer Review Team Leader agrees to:

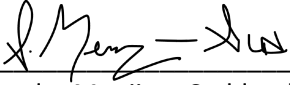
- Review and approve the self-assessment prior to starting on-site work for the review
- Retain all working papers for one year after the report has been issued, in accordance with the SAIAF Records Retention Procedure

The Peer Review Team (Team) agrees to:

- Review all relevant documentation
- Administer a survey to a sample of representatives from agency management
- Review the working papers of at least one project completed during the review period that is representative of the work performed during the period
- Conduct interviews of Internal Audit management and staff, and a sample of representatives from agency management, Board members, and external auditors
- Provide the Director and Board Members with periodic progress updates
- Issue a final report on the observations and recommendations identified during the Peer Review to the Director, with the complete report also issued to the members of the Board and Executive Management
- Include the Peer Review Team's opinion in a letter on whether the internal audit function generally conforms/passes, partially conforms/passes with deficiencies, or does not conform/fails to comply with the Standards, as defined in the *SAIAF Peer Review Manual*, Table 1. The report will also include the Director's responses, including action plans for addressing any recommendations

The peer review will begin in February 2021 with fieldwork scheduled to start in March 2021. A draft report will be provided to the Director for review by May 2021 with a final report available to be released by May 2021. An exit conference will be scheduled with the Director and the Texas Department of Motor Vehicles Executive Director.

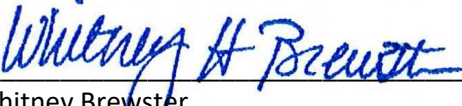
The signatures below indicate that the terms of this agreement are acceptable.



Sandra Menjivar-Suddeath, CIA, CISA, CFE, CGAP
Director of Internal Audit
Texas Department of Motor Vehicles

01/13/2021

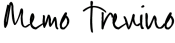
Date



Whitney Brewster
Executive Director
Texas Department of Motor Vehicles

01/07/2021

Date

DocuSigned by:


FDB22F52328947C...
Guillermo "Memo" Treviño
Chairman of the Board
Texas Department of Motor Vehicles

1/22/2021

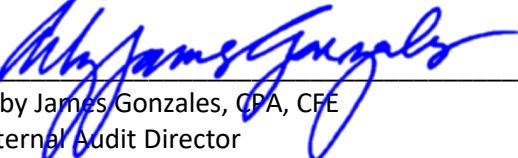
Date

DocuSigned by:


C7382D362011471...
Brett Graham
Chairman of the Finance & Audit Committee
Texas Department of Motor Vehicles

1/26/2021

Date



Arby James Gonzales, CPA, CFE
Internal Audit Director
Texas Department of Insurance
Peer Review Team Leader

12/30/2020

Date



Harold Rogers, CIA, CISA
Information Technology Audit Project Manager
Texas Workforce Commission
Peer Review Team Member

12/30/2020

Date

cc: SAIAF Peer Review Committee



Texas Department *of* Motor Vehicles

HELPING TEXANS GO. HELPING TEXAS GROW.

Peer Review Self – Assessment Report

Internal Audit Division

January 2021

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Peer Review Self-Assessment

Executive Summary

BACKGROUND

Every three years, the Internal Audit Division (IAD) is required to obtain an External Assessment (Peer Review) on whether the internal audit function complies with the applicable professional auditing standards in all material aspects. The applicable standards are the (1) Institute of Internal Auditors' International Professional Practices Framework, the definition of internal auditing, the Core Principles for the Professional Practice of Internal Auditing and the Code of Ethics; (2) U.S. Government Accountability Office's (GAO) Generally Accepted Auditing Standards; and (3) Texas Internal Auditing Act, Texas Government Code, Chapter 2102.

As part of the Peer Review, the IAD conducts a self-assessment, produces a report with the results of the self-assessment, and provides the report to the Peer Review Team. The Peer Review team uses the report to obtain information on how the IAD meets applicable auditing standards.

The IAD reviewed documentation created during the peer review period (September 2017 – August 2020), with a focus on documentation created in fiscal year 2020, to develop this self-assessment.

RESULTS

From September 2017 to August 2020, the Texas Department of Motor Vehicles (TxDMV or Department) – IAD generally conformed with the applicable standards in all material aspects. The IAD has established policies and procedures to ensure compliance with applicable auditing standards. The IAD followed those standards in work performed during the peer review period.

IAD also fully implemented previous external audit recommendations related to ethics.

Background

Peer Review Process

Every three years, the Internal Audit Division (IAD) is required to obtain an External Assessment (Peer Review) on whether the internal audit function generally complies with the applicable professional standards (audit standards)¹ during the peer review period (period). The peer review period was September 2017 to August 2020. The Peer Review determines if the IAD generally complies with audit standards by reviewing engagements conducted during the period and by evaluating the IAD's compliance with the eleven areas. Those eleven areas are the following²:

1. **Purpose, Authority, and Responsibility** - The internal audit function must be formally defined in an internal audit charter, consistent with the Mission of Internal Audit and the mandatory elements of the International Professional Practices Framework (the Core Principles for the Professional Practice of Internal Auditing, the Code of Ethics, the Institute of Internal Auditors (IIA) Standards, and the Definition of Internal Auditing).
2. **Independence and Objectivity** - The internal audit function must be independent and perform work in an objective manner.
3. **Proficiency and Due Professional Care** – Engagements must be performed by staff that are proficient and have due professional care.
4. **Quality Assurance and Improvement Program** – A quality assurance and improvement program must be established and must enable an evaluation of the internal audit function's conformance with the audit standards and any applicable other requirements. The program also should assess the efficiency and effectiveness of the internal audit function and identifies opportunities for improvement for the function.
5. **Managing the Internal Audit Activity** - The internal audit function must be effectively managed to ensure it adds value to the organization.
6. **Nature of Work** - The internal audit function must evaluate and contribute to the improvement of the organization's governance, risk management, and control processes using a systematic, disciplined, and risk-based approach.
7. **Engagement Planning** – A plan must be developed and documented for each engagement.
8. **Performing the Engagement** – Internal auditors must identify, analyze, evaluate, and document sufficient information to achieve the engagement's objectives.
9. **Communicating Results** – Results from the audit engagements must be communicated to management and those in charge with governance.

¹ The applicable standards are the (1) Institute of Internal Auditors' International Professional Practices Framework, the definition of internal auditing, the Core Principles for the Professional Practice of Internal Auditing and the Code of Ethics (IIA Standards); (2) U.S. Government Accountability Office's (GAO) Generally Accepted Auditing Standards (GAGAS); and (3) Texas Internal Auditing Act, Texas Government Code, Chapter 2102 (Act).

² Definitions obtained from the IIA Standards

10. **Monitoring Progress** – A system to monitor the disposition of results must be established, maintained, and communicated.
11. **Resolution of Senior Management's Acceptance of Risk** – When it has been concluded that management has accepted a level of risk that may be unacceptable to the organization, the risk must be discussed with senior management. If the matter is not resolved, the risk acceptance must be communicated to the board.

The Peer Review team reviews this self-assessment report, engagement documentation, and other documentation submitted to them and concludes on whether the internal audit function has complied with the applicable professional standards in all material aspects by preparing a report. It concludes whether the internal audit function is meeting standards by assigning one of the following ratings:

- **Pass/Generally Conforms** - the internal audit function is in compliance with the IIA Standards, GAGAS, and the Texas Internal Auditing Act. The internal audit function's policies, procedures, and practices are in place to implement the standards and requirements necessary for ensuring the independence, objectivity, and proficiency.
- **Pass with Deficiencies/Partially Conforms** – the internal audit function generally complies with the IIA Standards, GAGAS, and the Texas Internal Auditing Act. The internal audit function has an internal quality control system that is suitably designed and operating effectively to provide reasonable assurance of conformance with the Standards for assurance and consulting engagements during the review period. However, deficiencies in the internal quality control system have been noted that resulted in nonconformance with the IIA Standards, the GAO Standards, and/or the Texas Internal Auditing Act.
- **Fail/Does Not Conform** – the internal audit function is not in compliance with the Standards for assurance and consulting engagements during the review period. The Peer Review team found serious deficiencies in the internal quality control system for the internal audit function.

Self-Assessment Process

As part of the Peer Review Process, the IAD must conduct a self-assessment and produce a report with the results of the self-assessment. The self-assessment reviews the internal audit function related to complying with the key audit standards. The self-assessment is provided to the independent Peer Review team for their evaluation and consideration in their review.

For this self-assessment, the IAD reviewed documentation created, maintained, and used from September 2017 to August 2020.

The self-assessment was prepared the IAD during fiscal year (FY) 2021.

Self-Assessment Results

Overall Conclusion

Through the review conducted in this self-assessment, the Texas Department of Motor Vehicles (TxDMV or Department) – Internal Audit Division (IAD) concludes that it passes its peer review and is in compliance with the following required auditing standards: the 1) Institute of Internal Auditors' International Professional Practices Framework, the definition of internal auditing, the Core Principles for the Professional Practice of Internal Auditing and the Code of Ethics (IIA Standards); (2) U.S. Government Accountability Office's (GAO) Generally Accepted Auditing Standards (GAGAS); and (3) Texas Internal Auditing Act, Texas Government Code, Chapter 2102 (Act). The IAD generally complies (Pass) with the auditing standards. IAD did not identify any issues that must be corrected.

IIA Code of Ethics

The IAD maintains an ethical environment and complies with the IIA Code of Ethics by including the Code of Ethics in its Internal Audit Charter and Internal Audit Policies and Procedures Manual (standard operating procedures). In addition, the IAD demonstrates its commitment to ethics by being an active participant in reducing fraud, waste, and abuse in the Department and by conducting work in an ethical manner.

Previous Peer Review Recommendation Status

The IAD has implemented the 2018 Peer Review recommendation that recommended the IAD consider performing a periodic project related to the agency's ethics-related objectives, programs, and activities. Since the issuance of the audit recommendation, IAD completed an advisory service identifying fraud, waste, and abuse risks and controls and participated in the Ethics Policy workgroup as a facilitator and advisor. In the workgroup, IAD provided advice and potential risks with the updates to the Ethic policy and provided guidance on the structure of the ethics programs in the Department.

Purpose, Authority, and Responsibility

The IAD maintains an active Internal Audit Charter where the purpose, authority, roles, and responsibilities are defined. The charter also provides information on the IAD's mission and the standards it must follow. The Internal Audit Charter is reviewed every year during the Quality Assurance & Improvement Program (QAIP) and is updated as necessary.

The most recent update to the Internal Audit Charter was in November 2020. The charter was signed by the Executive Director, the Internal Audit Director, the Finance & Audit Committee Chairman, and the Board Chairman after it was approved by the Board. The Internal Audit Charter was posted on both the Department's Intranet and Internet

Independence and Objectivity

The IAD reports directly to the TxDMV Board and also has an administrative line to the Executive Director (and management). This structure ensures that the IAD is independent. Independence is confirmed during each engagement. Staff assigned to an engagement must confirm their independence prior to starting the engagement.

The IAD is objective since the IAD has no management responsibility. Moreover, the TxDMV Board is responsible for approving the audit plan, operating budget, and the appointment of the Internal Audit Director. The Internal Audit Charter also identifies roles and responsibilities to ensure independence and objectivity.

Proficiency and Due Professional Care

The IAD assures internal auditors are proficient and have due professional care by having job descriptions that accurately describe roles and responsibilities and by having an annual training planning process that develops staff for current and future engagements. Currently, the IAD has over 30 years of audit experience and has staff with active certifications. Staff currently have the following certifications: Certified Internal Auditor, Certified Government Auditing Professional, Certified Fraud Examiner, and Certified Information Security Auditor.

Each year, the Internal Audit Director meets with the internal audit staff to go over individual training plans. The development of the training plan follows the process set in the IAD's standard operating procedures.

The standard operating procedures also outline the necessary steps needed to ensure that internal staff (including internal and external specialists) have sufficient proficiency and due professional care to meet audit standards. Information related to proficiency and due professional care is captured through proficiency forms and the TeamMate³ control programs⁴.

Quality Assurance and Improvement Program

The IAD has a comprehensive QAIP that ensures audit standards are met. The comprehensive plan includes obtaining an external assessment every three years and conducting an internal assessment every year. The external assessment, also known as a Peer Review, is typically conducted by similar state agencies and ensures conformance and compliance with the applicable auditing standards. The last peer review was done in 2018.

The internal assessment includes a comprehensive review of the efficiency and effectiveness of the internal audit function as well as reviewing compliance with audit standards. The internal assessment includes a review of all audit documentation, audit recommendations, and reports for each engagement conducted by the IAD in a fiscal year prior to finalizing an engagement file. For each engagement, the IAD follows the review steps outlined in the Teammate control programs and the standard operating procedures. This ensures that each engagement has sufficient, relevant, and appropriate evidence and that performance standards are followed.

In addition, IAD provides progress and result information on the following:

- Key Performance Indicators (KPIs)
 - Audit Recommendation Implementation
 - Audit Plan Completion
 - Engagements completed within 10% of budgeted hours
 - Percentage of overall client satisfaction
 - Percentage of client surveys that agree the IAD communicated results clearly and timely

³ TeamMate AM is the audit software used by the IAD. IAD implemented TeamMate + (Plus) in FY2021.

⁴ A TeamMate control program details the steps used to perform the engagement. The control program also ensures audit standards are followed. The IAD has two TeamMate control programs: Audit Engagement TeamMate Control Program and Advisory Service (Consulting) Engagement TeamMate Control Program.

- Number of Internal Audit Education Efforts conducted annually
- Percentage of clients that believe audit recommendations were useful and beneficial when implemented
- Percentage of client survey responses that agreed the IAD had sufficient knowledge about the audited area
- Percentage of relevant certifications maintained by the IAD
- Percentage of staff working on operational initiatives
- Institute of Internal Auditors (IIA) – Internal Audit Capability Model for the Public Sector (Capability Model)
- Fraud, waste, and abuse allegations and disposition
- External assessment recommendations progress

Managing the Internal Audit Activity

The IAD is managed through the division's standard operating procedures and TeamMate control programs. The activity is also managed by continuously assessing risk and through the audit plans. Throughout the year, the IAD collects risks that may need to be audited in future years⁵. The risks are evaluated by reviewing data and obtaining stakeholder and staff feedback. The risks that are considered high are added to a future audit plan. The audit plan is reviewed and approved the TxDMV Board.

The TxDMV Board also approves the IAD's operating budget and allocation of the number of full-time equivalents (FTEs). The TxDMV Board is kept abreast on the audit plan status through board meetings and monthly conversations with the Board Chair and the Finance & Audit Chair, respectively. In addition, TxDMV Executive Office is kept abreast on the audit plan status through monthly meetings.

Nature of Work

The IAD aligns itself with the Department's missions, vision, and goals to provide assurance on the risks that may have the most impact to the Department. For each risk identified, the IAD ties that risk to the Department's strategic plan, goal, and the Legislative Budget Board (LBB) performance and budget area/strategy. This provides the division a comprehensive view of the risk areas throughout the Department and which areas may have more risk. In addition, IAD created a strategic plan that supports the Department's strategic plan and objectives. The strategic plan includes information on how IAD has position itself to help the Department respond to risks. In addition, it codifies IAD's vision, mission, and goals.

IAD's vision is to be a future focused internal audit function protecting and serving the Department and its customers and the mission is to identify emerging strategic risks, support adaptability in an evolving environment, and foster trusted relationships and an ethical environment.

By aligning the IAD's vision and mission to the Department's, IAD can focus on where it can add-value and have the most impact.

⁵ Any risk that is significant will be audited at the time (see the revision to the FY 2019 Annual Audit Plan).

Engagement Planning

The IAD uses its standard operating procedures and the TeamMate Control programs to plan engagements. IAD staff obtain an understanding of the process being evaluated, based on the preliminary objectives established in the audit plan. The staff collect and evaluate information from several sources: program data, interviews, and documented procedures. Next, the staff evaluate the risks to the Department and which controls are in place to mitigate the risk. The staff uses this information to develop final audit objective and fieldwork testing program. All testing and final objectives are approved by the IAD Director. The staff communicates this information to the clients through an End of Planning Conference. IAD also logs all risks and controls identified in the planning phase for future consideration.

Performing the Engagement

IAD uses its standard operating procedures and the TeamMate control programs to perform its engagements. All engagements are documented within TeamMate. The IAD staff enter work papers and summarize conclusions based on evidence gathered during fieldwork and as outlined in the fieldwork program. All work is reviewed by the engagement lead and the Internal Audit Director, or designee. Work that may need clarification receives coaching notes and the staff address those coaching notes. Upon completion of coaching notes, the IAD Director or designee reviews and finalizes the corrected workpapers.

While performing the engagement, staff enter and keep track of potential findings, observations, management discussions, and other items the Issue Viewer in TeamMate. They also track and test risks and controls and document the outcome. The issues that become findings and observations are reviewed by the IAD Director to ensure sufficient, appropriate, and relevant evidence is used to support the finding or observation.

Communicating Results

Results are communicated to TxDMV management and Board members in a timely manner. TxDMV management (client) obtains written and verbal communication on the audit's progress and results regularly. IAD has established a goal of communicating with the client every two weeks during the fieldwork phase. In addition, results and progress are communicated to the TxDMV Executive Office, Finance & Audit Committee Chair, Board Chair, and the Committee monthly.

Draft reports are reviewed by TxDMV Management, TxDMV Executive Office, TxDMV Finance & Audit Committee, and the TxDMV Board Chair prior to being issued. All audit reports are presented or provided to all Board members via the Board SharePoint site or via a Board meeting.

Monitoring Progress

The IAD monitors the progress of the issued recommendations (external and internal) as they become due. IAD uses TeamMate to track and determine if recommendations have been fully implemented. Based on the severity of the audit recommendation (high or low priority), the IAD may conduct additional testing when the audit recommendation is implemented. The monitoring progress process is detailed in the standard operating procedures.

Resolution of Senior Management's Acceptance of Risks

The IAD would report any risk acceptance (management accepted risk) that were considered outside acceptable risk levels, as required by audit standards. During the review period, the Department did not accept any risk that the IAD found to be outside acceptable risk levels. Risk acceptance communication is implied and discussed in the standard operating procedures and TeamMate control programs.

Appendix 1: Compliance Standards

Compliance Standards Summary

The TxDMV Internal Audit Division conducted its internal periodic self - assessment to assess whether the internal audit function met the Compliance Standards that are outlined by the IIA (IIA Standards) and GAO (GAGAS) as well as the compliance requirements within the Texas Internal Auditing Act (Texas Government Code 2102). The assessment found that the internal audit function generally conforms/passes with the Compliance Standards.

The assessment was conducted by students from the University of Texas at Austin. These students were taking an internal audit class as part of the accounting curriculum and had sufficient training to conduct the assessment. Internal Auditor Jason Gonzalez and IAD Director Sandra Menjivar-Suddeath oversaw the students to ensure the work was done in accordance with SAIAF Peer Review standards.

Documentation of Compliance Standards Review

Entity Name: Texas Department of Motor Vehicles			
Preparer: Annie Hu, Faizan Manji, Rahul Mehta, Zoey Rasch (University of Texas at Austin Students)		Review Date: 11/17/2020	
Reviewer: Sandra Menjivar-Suddeath		Review Period: 9/1/2017 to 8/31/2020	
Type of Assessment (check one)	<input type="checkbox"/> Internal – On-going monitoring	<input checked="" type="checkbox"/> Internal - Periodic self-assessment	<input type="checkbox"/> External
Overall Assessment: Generally Conforms/Pass			

Internal Assessment

An internal audit function may use this program at any time to satisfy the requirement of a Quality Assurance and Improvement Program for on-going monitoring and periodic internal and external quality assessments. The preparer will conclude on compliance by making one selection from the pulldown menu:

- Yes = conforms/pass
- No = does not conform/fail
- OI = conforms/pass with opportunity for improvement
- N/A = not applicable

No.	Citation	Standard	References	Conform/ Pass
ETHICS				
1	IA Act 2102.011, Code of Ethics, GAGAS 1.14	Does the charter or other Internal Audit document establish the expectation that audit staff will conform to the Institute of Internal Auditors' Code of Ethics and be guided by ethical principles?	Internal Audit Charter	Yes
★	CONCLUSION	Ethics. Does the internal audit activity comply with Ethics requirements?		Yes
COMMENTS:				
PURPOSE, AUTHORITY, AND RESPONSIBILITY				
1	AS 1000, AS 1000.A1	Are the purpose, authority, and responsibility of the internal audit activity formally defined in a charter, consistent with the Standards, and approved by the board? Is the nature of assurance services, including those provided to outside parties, defined in the audit charter?	Internal Audit Charter	Yes
2	AS 1000.C1	Is the nature of consulting services defined in the audit charter?	Internal Audit Charter	Yes
3	AS 1010	Is the mandatory nature of the Core Principles for the Practice of Internal Auditing, the Code of Ethics, the Standards, and the Definition of Internal Auditing recognized in the internal audit charter? Has the chief audit executive discussed the Mission of Internal Audit and the mandatory elements of the International Professional Practices Framework with senior management and the board?	Internal Audit Charter. The Internal Audit Charter was signed by the Executive Director and the Board.	Yes
★	CONCLUSION	Purpose, Authority, and Responsibility. Does the internal audit activity comply with the standard on defining purpose, authority, and responsibility?		Yes

No.	Citation	Standard	References	Conform/ Pass
COMMENTS:				
INDEPENDENCE and OBJECTIVITY				
1	IA Act 2102.006(a)	Does the governing board of the state agency, or the administrator if the state agency does not have a governing board, appoint the internal auditor?	Internal Audit Charter Organizational Chart	Yes
2	IA Act 2102.007(a)(1)	Does the internal auditor report directly to the state agency's governing board or the administrator of the state agency if the state agency does not have a governing board?	Internal Audit Charter Organizational Chart	Yes
3	IA Act 2102.007(b) GAGAS 3.31	<p>Does the program of internal auditing conducted by a state agency provide for the auditor to:</p> <ul style="list-style-type: none"> • Have access to the administrator • Be free of all operational and management responsibilities that would impair the auditor's ability to review independently all aspects of the state agency's operation <p>Is the Chief Audit Executive:</p> <ul style="list-style-type: none"> • Accountable to the head or deputy head of the government entity or to those charged with governance? • Required to report the results of the audit organization's work to the head or deputy head of the government entity and to those charged with governance? • Located organizationally outside the staff or line management functions of the unit under audit? • Granted access to those charged with governance? 	Internal Audit Charter Organizational Chart	Yes

No.	Citation	Standard	References	Conform/ Pass
		<ul style="list-style-type: none"> Sufficiently removed from political pressures to conduct audits and report findings, opinions, and conclusions objectively without fear of political reprisal? 		
4	GAGAS 3.46	<p>Before agreeing to perform non-audit services, did the audit organization perform an assessment to determine if:</p> <ul style="list-style-type: none"> The non-audit services are not expressly prohibited The auditor has determined that the requirements for performing non-audit services in paragraphs 3.49 through 3.58 have been met, including: <ol style="list-style-type: none"> Management is able to effectively oversee the non-audit service to be performed Auditors obtained assurance that management assumes all management responsibilities; designates an individual who possesses suitable skill, knowledge, or experience to oversee the services; evaluates the adequacy and results of the services performed; and accepts responsibility for the results of the services Auditors documented their understanding with management regarding objectives; services to be performed; audited entity's acceptance of its responsibilities; the auditor's responsibilities; and any limitation of the nonaudit service An auditor who previously performed non-audit services for an entity that is a prospective subject of an audit, evaluated the impact of those non-audit 	<p>Internal Audit Charter</p> <p>Advisory Service Agreement Template</p> <p>Consulting Engagement TeamMate Control Program</p> <p>Internal Audit Policies & Procedures Manual</p>	Yes

No.	Citation	Standard	References	Conform/ Pass
		<p>services on independence before accepting an audit</p> <p>e. An auditor in a government entity required to perform a non-audit services disclosed the nature of the threat that could not be eliminated or reduced to an acceptable level and modify the GAGAS compliance statement accordingly</p> <ul style="list-style-type: none"> • Any significant threats to independence have been eliminated or reduced to an acceptable level through the application of safeguards 		
5	AS 1100	<p>Independence and Objectivity. Is the internal audit activity independent, and are internal auditors' objective in performing their work?</p> <p><i>Interpretation:</i></p> <p><i>Organizational independence is effectively achieved when the chief audit executive reports functionally to the board. Examples of functional reporting to the board involve the board:</i></p> <ul style="list-style-type: none"> • Approving the internal audit charter • Approving the risk based internal audit plan • Approving the internal audit budget and resource plan • Receiving communications from the chief audit executive on the internal audit activity's performance relative to its plan and other matters • Approving decisions regarding the appointment and removal of the chief audit executive 	<p>Internal Audit Charter</p> <p>FY 2018 – FY 2020 Audit Plans</p>	Yes

No.	Citation	Standard	References	Conform/ Pass
		<ul style="list-style-type: none"> • Approving the remuneration of the chief audit executive • Making appropriate inquiries of management and the chief audit executive to determine whether there are inappropriate scope or resource limitations 		
6	AS 1110	<p>Organizational Independence. Does the chief audit executive report to a level within the organization that allows the internal audit activity to fulfill its responsibilities?</p> <p>Does the chief audit executive confirm to the board, at least annually, the organizational independence of the internal audit activity?</p>	<p>Internal Audit Charter</p> <p>FY2018 - 2020 Quality Assurance & Improvement Program (QAIP) Reports</p> <p>Internal Audit Policies & Procedures Manual</p>	Yes
7	AS 1110.A1	<p>Is the internal audit activity free from interference in determining the scope of internal auditing, performing work, and communicating results?</p> <p>Does the chief audit executive disclose such interference to the board and discuss the implications?</p>	Internal Audit Charter	Yes
8	AS 1111	Direct Interaction with the Board. Does the Chief Audit Executive communicate and interact directly with the board?	<p>Internal Audit Charter</p> <p>Internal Audit Policies & Procedures Manual</p>	Yes
9	AS 1112	Chief Audit Executive Roles Beyond Internal Auditing. Where the chief audit executive has or is expected to have roles and/or responsibilities that fall outside of internal auditing, are safeguards in place to limit impairments to independence or objectivity?		N/A

No.	Citation	Standard	References	Conform/ Pass
10	GAGAS 3.59	Documentation of Independence. Does the audit organization document threats to independence that require the application of safeguards, along with safeguards applied, in accordance with the conceptual framework for independence outlined in GAGAS 3.20 – 3.26?	Internal Audit Policies & Procedures Manual TeamMate control programs	Yes
11	AS 1120 GAGAS 1.19	Individual Objectivity. Do the internal auditors have an impartial, unbiased attitude and avoid any conflict of interest?	TeamMate control programs Independence Forms	Yes
12	AS 1130	Impairments to Independence or Objectivity. If independence or objectivity is impaired in fact or appearance, are the details of the impairment disclosed to appropriate parties? (The nature of the disclosure will depend upon the impairment.)	Internal Audit Policies & Procedures Manual TeamMate Control programs	Yes
13	1130.A1	Do the internal auditors refrain from assessing specific operations for which they were previously responsible within the previous year?	Internal Audit Policies & Procedures Manual TeamMate control programs	Yes
14	1130.A2	Does a party outside the internal audit activity oversee assurance services over functions over which the Chief Audit Executive has been responsible?		N/A
15	1130.A3	Is individual objectivity managed when assigning resources to assurance services engagements that are provided where the internal audit activity has previously performed consulting services?	TeamMate control programs Independence Forms	Yes

No.	Citation	Standard	References	Conform/ Pass
16	1130.C1 1130.C2	If internal auditors provide consulting services relating to operations for which they had previous responsibilities, are potential impairments to independence or objectivity disclosed to the client prior to performing consulting services?	FY2018 – FY2019 Advisory Service Control Programs	Yes
17	GAGAS 3.88	<p>Does the audit organization have policies and procedures on independence, legal, and ethical requirements that are designed to provide reasonable assurance that the audit organization and its personnel maintain independence and comply with applicable legal and ethical requirements? Do the policies and procedures assist the audit organization in:</p> <ul style="list-style-type: none"> • Communicating independence requirements to its staff • Identifying and evaluating circumstances and relationships that create threats to independence, and take appropriate action to eliminate those threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, withdraw from the audit where withdrawal is not prohibited by law or regulation 	Internal Audit Policies & Procedures Manual	Yes
18	GAGAS 3.08 – 3.09	<p>In situations where the audit organization identifies a personal impairment to independence, is the impairment resolved in a timely manner? Is there a process to:</p> <ul style="list-style-type: none"> • Identify threats to independence • Evaluate the significance of the threats identified, both individually and in the aggregate • Apply safeguards as necessary to eliminate the threats or reduce them to an acceptable level 	Internal Audit Policies & Procedures Manual TeamMate control programs Independence Policy or Statements	Yes

No.	Citation	Standard	References	Conform/ Pass
		If no safeguards are available to eliminate an unacceptable threat or reduce it to an acceptable level, is independence considered to be impaired?		
19	GAGAS 3.24	Has the audit organization established internal policies and procedures for identifying, applying safeguards and documenting conclusions on impairments to independence?	Internal Audit Policies & Procedures Manual	Yes
★	CONCLUSION	<p style="text-align: center;">Independence and Objectivity.</p> <p style="text-align: center;">Is the internal audit activity independent, and are the internal auditors' objective in performing their work (AS 1100)?</p> <p style="text-align: center;">Independence. In all matters relating to the audit work, is the audit organization and are the individual auditors, whether government or public, independent (GAGAS)?</p>		Yes
COMMENTS:				
PROFICIENCY and PROFESSIONAL JUDGMENT				
1	IA Act 2102.006 (b)	<p>Is the Chief Audit Executive a Certified Public Accountant or a Certified Internal Auditor?</p> <p style="text-align: center;">AND</p> <p>Does s/he have at least three years of auditing experience?</p>	Sandra Menjivar-Suddeath -Resumes and Certifications	Yes
2	AS 1210.A1 GAGAS 3.79 - 3.81	<p>Does the chief audit executive obtain competent advice and assistance if the internal auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement?</p> <p>Has the internal audit organization determined that <u>external specialists</u> who assist in performing a GAGAS audit are qualified and competent in their areas of specialization?</p>	Internal Audit Policies & Procedures Manual	Yes

No.	Citation	Standard	References	Conform/ Pass
		Has the internal audit organization determined that <u>internal specialists</u> consulting on a GAGAS audit who are not involved in directing, performing audit procedures, or reporting on a GAGAS audit, are qualified and competent in their areas of specialization? (Note: These specialists do not have to comply with GAGAS CPE requirements. However, <u>internal specialists</u> who are involved in these activities must comply with GAGAS CPE requirements.)		
3	1210.A2	Do the internal auditors have sufficient knowledge to evaluate the risk of fraud and the manner in which it is managed by the organization? (NOTE: Internal auditors are not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud.)	Internal Audit Policies & Procedures Manual Staff Training Record and Staff Resumes and Certifications	Yes
4	1210.A3	Do the internal auditors have knowledge of key information technology risks and controls and available technology-based audit techniques to perform their assigned work? (NOTE: Not all internal auditors are expected to have the expertise of an internal auditor whose primary responsibility is information technology auditing.)	Staff Training Record and Staff Resumes and Certifications	Yes
5	1210.C1	Does the chief audit executive decline the consulting engagement or obtain competent advice and assistance if the internal audit staff lacks the knowledge, skills, or other competencies needed to perform all or part of the engagement?	Internal Audit Policies & Procedures Manual TeamMate control programs	Yes
6	GAGAS 3.70	Does the audit organization have a process for recruitment, hiring, continuous development, assignment, and evaluation	Internal Audit Policies & Procedures Manual	Yes

No.	Citation	Standard	References	Conform/ Pass
		of staff to maintain a competent workforce?		
7	AS 1210 GAGAS 3.72	<p>Proficiency. Do internal auditors possess the knowledge, skills, and other competencies needed to perform their individual responsibilities?</p> <p>Does the internal audit activity collectively possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities?</p> <p>Do the staff members collectively possess the technical knowledge, skills, and experience necessary to be competent for the type of work being performed before beginning work on that assignment?</p>	<p>Internal Audit Policies & Procedures Manual</p> <p>TeamMate control programs</p> <p>Audit Team Proficiency Document</p> <p>Temporary Personnel Template</p>	Yes
8	AS 1220 1220.A1	<p>Due Professional Care. Do the internal auditors apply the care and skill expected of a reasonably prudent and competent internal auditor? (NOTE: Due professional care does not imply infallibility.)</p> <p>Do the internal auditors exercise due professional care by considering the:</p> <ul style="list-style-type: none"> • Extent of work needed to achieve the engagement's objectives • Relative complexity, materiality, or significance of matters to which assurance procedures are applied • Adequacy and effectiveness of governance, risk management, and control processes • Probability of significant errors, fraud, or noncompliance • Cost of assurance in relation to potential benefits 	<p>Audit Team Proficiency Document</p> <p>Temporary Personnel Template</p>	Yes

No.	Citation	Standard	References	Conform/ Pass
9	1220.A2	In exercising due professional care, do the internal auditors consider the use of technology-based audit and other data analysis techniques?	TeamMate control programs	Yes
10	1220.A3	Are the internal auditors alert to the significant risks that might affect objectives, operations, or resources? (NOTE: Assurance procedures alone, even when performed with due professional care, do not guarantee that all significant risks will be identified.)	TeamMate control programs	Yes
11	1220.C1	<p>Do the internal auditors exercise due professional care during a consulting engagement by considering the:</p> <ul style="list-style-type: none"> • Needs and expectations of clients, including the nature, timing, and communication of engagement results • Relative complexity and extent of work needed to achieve the engagement's objectives • Cost of the consulting engagement in relation to potential benefits 	<p>TeamMate control programs</p> <p>Advisory Service Agreement Template</p> <p>Internal Audit Policies & Procedures Manual</p>	Yes
12	AS 1230	Continuing Professional Development. Do the internal auditors enhance their knowledge, skills, and other competencies through continuing professional development?	<p>Internal Audit Policies & Procedures Manual</p> <p>Staff Proficiency and Training Records</p>	Yes
13	GAGAS 3.76 GAGAS 3.78	Does the audit organization maintain quality control procedures, including documentation, to help ensure that each auditor completed Continuing Professional Education (CPE) in accordance with the following?	Staff Proficiency and Training Records	Yes

No.	Citation	Standard	References	Conform/ Pass
		<ul style="list-style-type: none"> • Complete 24 hours of CPE every 2 years that directly relate to governmental auditing, the government environment, or the specific/unique environment in which the audited entity operates • At least an additional 56 hours (for a total of 80 hours every two-year period) that directly enhance the auditor's professional proficiency to perform audits and/or attestation engagements • At least 20 of the 80 hours completed in each year of the 2-year period. Or, if hired in the middle of a 2-year period, complete a defined pro-rated number of CPE hours 		
14	GAGAS 3.79	IF USING THE WORK OF EXTERNAL & INTERNAL SPECIALISTS. Does the audit organization ensure such specialists are qualified and competent in their areas of specialization?	Internal Audit Policies & Procedures Manual Temporary Personnel Template	Yes
15	GAGAS 3.81	IF USING THE WORK OF INTERNAL SPECIALISTS. Does the audit organization ensure that internal specialists performing work as part of the audit team are meeting GAGAS CPE requirements?	Internal Audit Policies & Procedures Manual	Yes
★	CONCLUSION	<p>Proficiency and Due Professional Care. Are engagements performed with proficiency and due professional care (AS 1200)?</p> <p>Professional Judgment. Is professional judgment used in planning and performing audits and in reporting the results (GAGAS 3.60)?</p> <p>Competence. Does the staff assigned to perform the audit collectively possess adequate professional competence for the tasks required (GAGAS 3.69)?</p>		Yes

No.	Citation	Standard	References	Conform/ Pass
COMMENTS:				
QUALITY ASSURANCE AND IMPROVEMENT PROGRAM				
1	IA Act 2102.007(a)(5)	Does the Chief Audit Executive conduct quality assurance reviews in accordance with the Standards for the Professional Practice of Internal Auditing, the Code of Ethics contained in the International Professional Practices Framework as promulgated by the Institute of Internal Auditors, and generally accepted government auditing standards, and periodically take part in a comprehensive external peer review?	Internal Audit Policies & Procedures Manual	Yes
2	AS 1310	Requirements of the Quality Assurance and Improvement Program – Does the quality assurance and improvement program include both internal and external assessments?	Internal Audit Policies & Procedures Manual	Yes
3	AS 1311	Internal Assessments. Do internal assessments include: <ul style="list-style-type: none"> • Ongoing monitoring of the performance of the internal audit activity • Periodic self-assessments or assessments by other persons within the organization who have sufficient knowledge of internal audit practices 	Internal Audit Policies & Procedures Manual 2018 - 2020 QAIP Report 2018 Peer Review Self-Assessment Report	Yes
4	GAGAS 3.83 GAGAS 3.85	Does the audit organization's system of quality control encompass the audit organization's leadership, emphasis on performing high quality work, and the organization's policies and procedures designed to provide reasonable assurance of complying with professional standards	Internal Audit Policies & Procedures Manual TeamMate control programs	Yes

No.	Citation	Standard	References	Conform/ Pass
		<p>and applicable legal and regulatory requirements that collectively address the following?</p> <ul style="list-style-type: none"> • Leadership responsibilities for quality within the audit organization • Independence, legal, and ethical requirements • Initiation, acceptance, and continuance of audit engagements • Human resources • Audit performance, documentation, and reporting • Monitoring of quality 		
5	GAGAS 3.84	<p>Does the audit organization do the following?</p> <ul style="list-style-type: none"> • Document its quality control policies and procedures • Communicate those policies and procedures to its personnel • Document compliance with its quality control policies and procedures • Maintain such documentation for a period of time sufficient to enable those performing monitoring procedures and peer reviews to evaluate the extent of the audit organization's compliance with its quality control policies and procedures 	<p>Internal Audit Policies & Procedures Manual 2018 – 2020 QAIP Reports Records Schedule</p>	Yes
6	GAGAS 3.95	<p>Does the audit organization analyze and summarize the results of its monitoring procedures at least annually, with identification of any systemic issues</p>	2018 – 2020 QAIP Reports	Yes


No.	Citation	Standard	References	Conform/ Pass
		needing improvement along with recommendations for corrective action?		
7	AS 1312	<p>External Assessments. Are external assessments, such as quality assurance reviews, conducted at least once every five years by a qualified, independent assessor or assessment team from outside the organization?</p> <p>The chief audit executive must discuss with the board:</p> <ul style="list-style-type: none"> • The form and frequency of external assessments • The qualifications and independence of the external assessor or assessment team, including any potential conflict of interest <p>Does the chief audit executive encourage board participation in the external assessments to reduce perceived or potential conflicts of interest?</p>	<p>2018 Peer Review</p> <p>Internal Audit Policies & Procedures Manual</p>	Yes
8	GAGAS 3.96	<p>Does the audit organization have an external peer review at least once every 3 years by reviewers independent of the audit organization being reviewed to determine if the audit organization is conforming to applicable professional standards? (This review should include determining if the system of quality control was suitably designed and whether the audit organization is complying with its quality control system.)</p> <p>Did the audit organization take remedial, corrective actions as needed based on the results of the peer review? (While the Yellow Book is currently silent on this</p>	<p>2018 Peer Review</p> <p>Internal Audit Policies & Procedures Manual</p>	Yes

No.	Citation	Standard	References	Conform/ Pass
		matter, the SAI AF encourages consideration be given to this area.)		
9	AS 1320	<p>Reporting on the Quality Assurance and Improvement Program. Does the chief audit executive communicate the results of the quality assurance and improvement program to senior management and the board at least annually?</p> <p>Disclosure should include</p> <ul style="list-style-type: none"> • The Scope and frequency of both the internal and external assessments • The qualifications and independence of the assessor(s) or assessment team, including potential conflicts of interest • Conclusions of assessors • Corrective action plans 	<p>2019 & 2020 QAIP Letters</p> <p>2018 Peer Review</p>	Yes
10	GAGAS 3.105	Does the chief audit executive provide a copy of the external peer review report to those charged with governance including the appropriate oversight bodies?	Board Communication through SharePoint and Board Internal Audit Site	Yes
11	AS 1321	Use of “Conforms with the International Standards for the Professional Practice of Internal Auditing.” Does the internal audit activity indicate that it conforms with the International Standards for the Professional Practice of Internal Auditing only if supported by the results of the quality assurance and improvement program?	Internal Audit Policies & Procedures Manual	Yes
12	AS 1322	Disclosure of Nonconformance. If nonconformance with the Code of Ethics or the Standards impacts the overall scope or operation of the internal audit activity,	Internal Audit Policies & Procedures Manual	Yes

No.	Citation	Standard	References	Conform/ Pass
		does the chief audit executive disclose the nonconformance and the impact to senior management and the board?		
13	GAGAS 2.23	Stating Compliance with GAGAS in the Auditors' Report. Does the audit organization refer to compliance with GAGAS in its audit reports, as appropriate with the level of compliance outlined in GAGAS 2.24 – 2.25?	Internal Audit Policies & Procedures Manual	Yes
★	CONCLUSION	<p align="center">Quality Assurance and Improvement Program.</p> <p>Does the chief audit executive develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit activity and assesses the efficiency and effectiveness and identifies opportunities for improvement (AS 1300)?</p> <p>Quality Control and Assurance. When performing audits or attestation engagements in accordance with GAGAS, has the audit organization established and maintained a system of quality control that is designed to provide reasonable assurance that the organization and its personnel comply with professional standards and applicable legal and regulatory requirements; and does it have an external peer review at least once every 3 years (GAGAS)?</p>		Yes
COMMENTS:				
MANAGING THE INTERNAL AUDIT ACTIVITY				
1	IA Act 2102.005(1) & 2102.007 (a)(2)	Does the chief audit executive develop an annual audit plan that is prepared using risk assessment techniques and that identifies the individual audits to be conducted during the year?	FY 2018– FY 2020 Internal Audit Plans	Yes
2	PS 2010	Planning. Has the chief audit executive established risk-based plans to determine the priorities of the internal audit activity, consistent with the organization's goals?	FY 2018– FY 2020 Internal Audit Plans	Yes
3	2010.A1	<ul style="list-style-type: none"> Is the internal audit activity's plan of engagements based on a documented 	FY 2018– FY 2020 Internal Audit Plans	Yes

No.	Citation	Standard	References	Conform/ Pass
		<p>risk assessment undertaken at least annually?</p> <ul style="list-style-type: none"> Is the input of senior management and the board considered in this process? 		
4	2010.C1	<ul style="list-style-type: none"> Does the chief audit executive consider accepting proposed consulting engagements based on the engagement's potential to improve management of risks, add value, and improve the organization's operations? Are engagements that have been accepted included in the plan? 	<p>FY 2018– FY 2020 Internal Audit Plans Board Communication through SharePoint and Board Internal Audit Site Organizational Review</p>	Yes
5	IA Act 2102.007(a)(3)	Has the chief audit executive conducted audits specified in the audit plan and documented deviations?	Annual Reports	Yes
6	PS 2020	<ul style="list-style-type: none"> Communication and Approval. Does the chief audit executive communicate the internal audit activity's plans and resource requirements, including significant interim changes, to senior management and to the board for review and approval? Has the chief audit executive also communicated the impact of resource limitations? 	<p>FY 2018– FY 2020 Internal Audit Plans Annual Reports</p>	Yes
7	IA Act 2102.006(d)	Does the governing board of the state agency, or the administrator of the state agency if the state agency does not have a governing board, periodically review the resources dedicated to the internal audit program and determine if adequate resources exist to ensure that risks identified in the annual risk assessment are adequately covered within a reasonable time frame?	FY 2018– FY 2020 Internal Audit Plans	Yes

No.	Citation	Standard	References	Conform/ Pass
8	IA Act 2102.008	Is the annual audit plan that is developed by the chief audit executive approved by the state agency's governing board, or by the administrator of the state agency if the state agency does not have a governing board?	FY 2018– FY 2020 Internal Audit Plans	Yes
9	PS 2030	Resource Management. Does the chief audit executive ensure that internal audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan?	FY 2018– FY 2020 Internal Audit Plans	Yes
10	PS 2040	Policies and Procedures. Has the chief audit executive established policies and procedures to guide the internal audit activity?	Internal Audit Policies & Procedures Manual	Yes
11	PS 2050	Coordination and Reliance. Does the chief audit executive share information, coordinate activities, and consider relying upon the work of other internal and external assurance and consulting service providers to ensure proper coverage and minimize duplication of efforts?	Board Activity Reports	Yes
12	PS 2060	<p>Reporting to Senior Management and the Board.</p> <ul style="list-style-type: none"> • Does the chief audit executive report periodically to senior management and the board on the internal audit activity's purpose, authority, responsibility, and performance relative to its plan and on its conformance with the Code of Ethics and the Standards? • Does the reporting include significant risk and control issues, including fraud risks, governance issues, and other matters that require the attention of senior management and/or the board? • Does the chief audit executive's reporting and communication to senior 	<p>Board Activity Reports</p> <p>Monthly Meetings with the TxDMV Executive Office (Activity Reports)</p> <p>Internal Audit Policies & Procedure Manual</p>	Yes


No.	Citation	Standard	References	Conform/ Pass
		management and the board include information about management's response to risk that, in the chief audit executive's judgment, may be unacceptable to the organization?		
13	IA Act 2102.0091 and 2102.015	<ul style="list-style-type: none"> Does the chief audit executive prepare an annual report and submit the report before November 1 of each year to the governor, the Legislative Budget Board, the Sunset Advisory Commission, the state auditor, the state agency's governing board, and the administrator? Do the form and content of the report conform to the State Auditor's instructions? Does the agency post on its Internet website the approved internal audit plan and annual report? 	Annual Reports Internal Audit Policies & Procedures Manual	Yes
	CONCLUSION	<p style="text-align: center;">PS 2000 Managing the Internal Audit Activity.</p> <p>Does the chief audit executive effectively manage the internal audit activity to ensure it adds value to the organization?</p>		Yes
COMMENTS:				
NATURE OF WORK				
1	IA Act 2102.005 (2)	<p>Does the program of internal auditing include periodic audits of the agency's major systems and controls, including:</p> <ul style="list-style-type: none"> Accounting systems and controls Administrative systems and controls Electronic data processing systems and controls 	Risk Assessment and Audit Plans	Yes
2	IA Act 2102.007(6)	Does the chief audit executive conduct economy and efficiency audits and program results audits as directed by the state agency's governing board or the	Risk Assessment and Audit Plans	Yes

No.	Citation	Standard	References	Conform/ Pass
		administrator of the state agency if the state agency does not have a governing board?		
3	PS 2100	Nature of Work. Does the internal audit activity evaluate and contribute to the improvement of the organization's governance, risk management, and control processes using a systematic, disciplined, and risk-based approach?	Risk Assessment and Audit Plans	Yes
4	PS 2110	<p>Governance. Does the internal audit activity assess and make appropriate recommendations to improve the organization's governance processes for:</p> <ul style="list-style-type: none"> • Making strategic and operational decisions • Overseeing risk management control • Promoting appropriate ethics and values within the organization • Ensuring effective organizational performance management and accountability • Communicating risk and control information to appropriate areas of the organization • Coordinating the activities of and communicating information among the board, external and internal auditors, other assurance providers, and management 	Risk Assessment and Audit Plans	Yes
5	2110.A1	Does the internal audit activity evaluate the design, implementation, and effectiveness of the organization's ethics-related objectives, programs, and activities?	Risk Assessment and Audit Plans	Yes

No.	Citation	Standard	References	Conform/ Pass
6	2110.A2	Does the internal audit activity assess whether the information technology governance of the organization sustains and supports the organization's strategies and objectives?	Risk Assessment and Audit Plans	Yes
7	PS 2120	<p>Risk Management. Does the internal audit activity evaluate the effectiveness and contribute to the improvement of risk management processes?</p> <p><i>Interpretation: Determining whether risk management processes are effective is a judgment resulting from the internal auditor's assessment that:</i></p> <ul style="list-style-type: none"> • Organizational objectives support and align with the organization's mission • Significant risks are identified and assessed • Appropriate risk responses are selected that align risks with the organization's risk appetite • Relevant risk information is captured and communicated in a timely manner across the organization, enabling staff, management, and the board to carry out their responsibilities <p><i>Does the internal audit activity gather the information to support this assessment during multiple engagements? The results of these engagements, when viewed together, should provide an understanding of the organization's risk management processes and their effectiveness.</i></p>	Risk Assessment and Audit Plans	Yes

No.	Citation	Standard	References	Conform/ Pass
		Are risk management processes monitored through ongoing management activities, separate evaluations, or both?		
8	2120.A1	<p>Does the internal audit activity evaluate risk exposures relating to the organization's governance, operations, and information systems regarding the following?</p> <ul style="list-style-type: none"> • Achievement of the organization's strategic objectives • Reliability and integrity of financial and operational information • Effectiveness and efficiency of operations and programs • Safeguarding of assets • Compliance with laws, regulations, policies, procedures and contracts 	Risk Assessment and Audit Plans	Yes
9	2120.A2	Does the internal audit activity evaluate the potential for the occurrence of fraud and how the organization manages fraud risk?	Risk Assessment and Audit Plans	Yes
10	2120.C1	During consulting engagements, do the internal auditors address risk consistent with the engagement's objectives, and are they alert to the existence of other significant risks?	Risk Assessment and Audit Plans TeamMate Advisory Service Engagement – Control Program	N/A
11	2120.C2	Do the internal auditors incorporate their knowledge of risks gained from consulting engagements into their evaluation of the organization's risk management processes?	FY 2019 – FY 2020 Annual Audit Plan TeamMate control programs	Yes
12	2120.C3	When assisting management in establishing or improving risk management processes, do internal auditors refrain from assuming any management responsibility by actually managing risks?	Internal Audit Policies & Procedures Manual Internal Audit Charter	Yes

No.	Citation	Standard	References	Conform/ Pass
13	PS 2130	Control. Does the internal audit activity assist the organization in maintaining effective controls by evaluating their effectiveness and efficiency and by promoting continuous improvement?	FY 2019 – FY 2020 Annual Audit Plan Internal Audit Policies & Procedures Manual	Yes
14	2130.A1	<p>Does the internal audit activity evaluate the adequacy and effectiveness of controls in responding to risks within the organization’s governance, operations, and information systems regarding the:</p> <ul style="list-style-type: none"> • Achievement of the organization’s strategic objectives • Reliability and integrity of financial and operational information • Effectiveness and efficiency of operations and programs • Safeguarding of assets • Compliance with laws, regulations, policies, procedures and contracts 	FY 2019 – FY 2020 Annual Audit Plan	Yes
15	2130.C1	Are internal auditors incorporating knowledge of controls gained from consulting engagements into evaluations of the organization’s control processes?	FY 2019 – FY 2020 Annual Audit Plan TeamMate control programs Internal Audit Policies & Procedures Manual	Yes
★	CONCLUSIONS	<p style="text-align: center;">Nature of Work.</p> <p>Does the internal audit activity evaluate and contribute to the improvement of the organization’s governance, risk management, and control processes using a systematic, disciplined, and risk-based approach (PS 2100)?</p>		Yes
COMMENTS:				

No.	Citation	Standard	References	Conform/ Pass
MONITORING PROGRESS				
1	PS 2500.A1	Has the chief audit executive established a follow-up process to monitor and ensure that management actions have been effectively implemented or that senior management has accepted the risk of not taking action?	Internal Audit Policies & Procedures Manual	Yes
2	PS 2500.C1	Does the internal audit activity monitor the disposition of results of consulting engagements to the extent agreed upon with the client?	Internal Audit Policies & Procedures Manual	Yes
3	PS 2500	Monitoring Progress – Has the chief audit executive established and maintained a system to monitor the disposition of results communicated to management?	Internal Audit Policies & Procedures Manual	Yes
	CONCLUSIONS	Monitoring Progress. Has the chief audit executive established and maintained a system to monitor the disposition of results communicated to management (PS 2500)?		Yes
COMMENTS:				

Appendix 3: Work Paper Review Checklist

Work Paper Review Summary

As part of the self-assessment, the Internal Audit Division is required to review the audit documentation (work papers) obtained and developed for one audit engagement that was conducted during the peer review period. The audit selected for review was audit number #20-03, the Title and Registration Customer Support (audit). The audit was conducted in FY 2020 and had one audit finding related to title and registration customer service delivery processes. The audit was found to have a maturity rating of a 2, which meant that the process had similar procedures followed by several employees, but the results may not be consistent. The process is not completely documented and has not been sufficiently evaluated to address risks.

The workpaper review found that the audit generally conformed/passed. Below is the detailed review and documentation

Documentation of Work Papers Review

Entity Name: Texas Department of Motor Vehicles			
Engagement Name: Title and Registration Customer Support			
Preparer: Jason Gonzalez		Review Date: 1/8/2021	
Reviewer: Sandra Menjivar-Suddeath		Review Period: 9/1/2017 to 8/31/2020	
Type of Assessment (check one)	<input type="checkbox"/> Internal - On-going monitoring	<input checked="" type="checkbox"/> Internal - Periodic self- assessment	<input type="checkbox"/> External
Overall Assessment: Generally Conforms/Pass			

Internal Assessment

An internal audit function may use this program to review audit documentation for an individual engagement at any time to satisfy the requirement of a Quality Assurance and Improvement Program for on-going monitoring and periodic internal and external quality assessments. The preparer will conclude on compliance by making one selection from the pull-down menu:

- Yes = conforms/pass
- No = does not conform/fail
- OI = conforms/pass with opportunity for improvement
- N/A = not applicable

Compliance Standard	Comply/P ass	References
PLANNING CONCLUSIONS		
1. Do the internal auditors develop and document a plan for each engagement, including the engagement's objectives, scope, timing, and resource allocations? Does the plan consider the organization's strategies, objectives, and risks relevant to the engagement? (PS 2200)	Yes	C.2.PRG program steps #1-2 Project Profile
2. Do the auditors adequately plan and document the planning of the work necessary to address the audit objectives? (GAGAS 6.06-6.12)	Yes	Gain a Preliminary Understanding Folder
3. Did the internal auditor determine appropriate and sufficient resources to achieve engagement objectives based on an evaluation of the nature and complexity of each engagement, time constraints, and available resources? (PS 2230)	Yes	Audit Timeline
4. Did the auditors obtain a sufficient understanding of information systems controls necessary to assess the audit risk and plan the audit within the context of the audit objectives for the systems that were significant to the objectives? (GAGAS 6.23 – 6.27)	Yes	Identify Significant Information System PRG
5. Did the internal auditor develop and document work programs that achieve the engagement objectives? (PS 2240)	Yes	Project Plan
Conclusion: Planning Steps met audit standards.		
SCOPE		
6. Is the internal auditor's scope sufficient to achieve the objectives of the engagement? (PS 2220)	Yes	Project Plan & Risk Assessment Folder
7. Did the auditors adequately identify and define the scope, and was it directly tied to the objectives of the engagement? (GAGAS 6.09)	Yes	Project Plan & Risk Assessment Folder
Conclusion: Scope was properly defined.		
PERFORMING THE ENGAGEMENT		
8. Do the internal auditors identify, analyze, evaluate, and document sufficient information to achieve the engagement's objectives? (PS 2300)	Yes	Quality Assurance Strategic Analysis PRG B.3
9. Are audit staff properly supervised? (GAGAS 6.53-6.55; PS 2340)	Yes	See review sign offs in TeamMate
10. Is sufficient, appropriate evidence obtained to provide a reasonable basis for the auditors' findings and conclusions? (GAGAS 6.56-6.78; PS 2320)	Yes	Referenced Draft Report – IAD Review

Compliance Standard	Comply/P ass	References
<p>11. Do the auditors prepare audit documentation related to planning, conducting, and reporting for each audit in sufficient detail to enable an experienced auditor, who has had no previous connection with the audit, to understand from the audit documentation the nature, timing, extent, and results of audit procedures performed, the audit evidence obtained and its source and the conclusions reached, including evidence that supports the auditors' significant judgments and conclusions? Do the auditors prepare audit documentation that contains support for findings, conclusions, and recommendations before they issue their report? (GAGAS 6.79-6.85)</p>	Yes	<p>See the following folders:</p> <ul style="list-style-type: none"> • Quality Assurance Strategic Analysis • Communication Procedures • Training • Customer Follow-up • Ticket Resolution • Fieldwork Phase
Conclusion: Sufficient evidence was gathered to support conclusions.		
REPORTING		
<p>12. Do the internal auditors communicate the engagement results as required? (PS 2400 – PS 2450)</p>	Yes	Audit Report and Draft (AS2)
<p>13. Do the auditors issue reports communicating the results of each completed performance audit? (GAGAS 7.03)</p>	Yes	Reporting Phase PRG
<p>14. Do the auditors use a form of the audit report that is appropriate for its intended use in writing or in some other retrievable form? (GAGAS 7.04)</p>	Yes	Reporting Phase PRG
<p>15. Do the auditors prepare reports that contain (1) the objectives, scope, and methodology of the audit; (2) the audit results, including findings, conclusions, and recommendations, as appropriate; (3) a statement about the auditors' compliance with generally accepted government auditing standards; (4) a summary of the views of responsible officials; and, (5) if applicable, the nature of any confidential or sensitive information omitted? (GAGAS 7.08)</p>	Yes	Audit Report and Draft (AS2) PRG
<p>16. Is the report timely, complete, accurate, objective, convincing, clear, and as concise as the subject permits? (GAGAS A7.02)</p>	Yes	Audit Report and Draft (AS2) PRG
<p>17. Distributing Reports. Are audit reports distributed to those charged with governance, to the appropriate officials of the audited entity, and to the appropriate oversight bodies or organizations requiring or arranging for the audits? (GAGAS 7.44 a)</p>	Yes	Reporting Phase PRG
<p>Conclusion: The reporting phase met the audit standards, but there was a delay in submitting the report to the Sunset Commission. The Sunset Commission was inadvertently left off the original external distribution due to an</p>		

Compliance Standard	Comply/P ass	References
error in the distribution list. The issue was corrected once it was identified, but it was about two months after the original distribution. The IAD has corrected this issue by updating their distribution list.		
RESOLUTION OF MANAGEMENT'S ACCEPTANCE OF RISKS		
<p>18. When the chief audit executive believes that senior management has accepted a level of residual risk that may be unacceptable to the organization, does the chief audit executive discuss the matter with senior management? (PS 2600)</p> <p>If the decision regarding residual risk is not resolved; does the chief audit executive report the matter to the board for resolution?</p>	N/A	
Conclusion: Not applicable as no instances were found during the peer review period.		

Appendix 4: Summary of Issues

Issue Summary

The IAD was in compliance with auditing standards and had a pass rating in the self-assessment. The IAD did identify an opportunity to refine its audit goals and performance measures. Below is the detailed documentation.

Summary of Issues Documentation

Entity Name: Texas Department of Motor Vehicles			
Preparer: Sandra Menjivar-Suddeath		Review Date: 1/8/2021	
Reviewer:		Review Period: 9/1/2017 to 8/31/2020	
Type of Assessment (check one)	<input type="checkbox"/> Internal - On-going monitoring	<input checked="" type="checkbox"/> Internal - Periodic self- assessment	<input type="checkbox"/> External
Overall Assessment: Generally Conforms/Pass			

Instructions: For every issue that the peer review team determines should be carried forward from the Compliance Standards and Review of Audit Documentation forms, the peer review team should identify the applicable auditing standard (standard reference) and the corresponding number (e.g., E3), describe the issue, develop a recommendation, and indicate whether the issue is an example of “does not comply/fail” or an “opportunity for improvement” (OI). Add rows as necessary.

Peer Reviews are intended to help the Internal Audit function and the organization receiving the review. In addition to evaluating compliance with Standards and the Act and identifying any instances of noncompliance, peer reviews provide an opportunity to identify best practices and opportunities for improvement for the Internal Audit function’s consideration. An OI does not require any action on the part of the organization; however, the organization should give them serious consideration. The organization should provide a management response indicating what action, if any, they will take. The current peer review did not identify any opportunities for improvement.

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To: Texas Department of Motor Vehicles Board
From: Linda M. Flores, CPA, Chief Financial Officer, Finance & Administrative Services Division Director
Agenda Item: 6.C
Subject: FY 2020 End of Year Reports

RECOMMENDATION

Briefing Only

PURPOSE AND EXECUTIVE SUMMARY

The **Annual Financial Report** is prepared in compliance with Texas Government Code, Section 2101.011 and in accordance with the reporting requirements established by the Comptroller's Office. The report is not audited but will be considered for audit by the State Auditor's Office as part of the State of Texas Comprehensive Annual Financial Report. The annual report was submitted to the Texas Comptroller by November 20, 2020, in compliance with the established deadline.

Government Code Section § 2101.0115 was added by Act of May 26, 2001, 77th Leg., R.S., H.B. 2914 and requires state agencies to submit an **Annual Report of Nonfinancial Data**. This report includes nonfinancial schedules previously included in the Annual Financial Report. The **Annual Report of Nonfinancial Data** was submitted to the Office of the Governor, State Auditor, Legislative Budget Board and the Legislative Reference Library in accordance with the established December 31, 2020 deadline.

FINANCIAL IMPACT

In Fiscal Year (FY) 2020, the TxDMV's expenditures were funded by the General Revenue Fund 0001 (Expenditures = \$13,353,329), State Highway Fund 0006 (Expenditures = \$590,249) and the Texas Department of Motor Vehicle Fund 0010 (Expenditures = \$137,082,395), as detailed on Exhibits A-2 Combining Statement of Revenues and Expenditures and Changes in Fund Balances All General and Consolidated Funds and B-2 Combining Statement of Revenues, Expenditures and Changes in Fund Balances Special Revenue Funds.

BACKGROUND AND DISCUSSION

Annual Financial Report

Exhibit I – Combined Balance Sheet (Statement of Net Assets)

The TxDMV closes FY 2020 with a net asset balance increase of \$12,311,050. Total net asset amount on August 31, 2020 is \$295.4 million.

- Cash in State Treasury consist of the net of revenues collected and deposited and legislative appropriation expense into the TxDMV Fund.
- Legislative Appropriations represents the unspent appropriations in General Revenue (Fund 0001.) This includes any benefits appropriations. Motor Vehicle Crime Prevention Authority (MVCPA) is the only item in Fund 0001.
- Accounts Receivable (A/R) represents the amounts due from Tax Assessor Collectors and Regional Offices less collections. The decrease of \$4.65 million in A/R compared to the prior year is primarily a timing difference in counties processing deposits at year end.

- In Capital Assets, the non-current asset had a net decrease of \$292,212 due to the disposal of old assets and the removal of the associated accumulated depreciation.
- Payables were \$1.19 million greater in 2020 because more invoices were outstanding at year end.
- Employees Compensable Leave represents unused vacation and overtime of employees at year end. Leave balances increased \$981,008 due to staff not using their vacation time, primarily due to COVID-19.

Exhibit II – Combined Statement of Revenues, Expenditures, and Changes in Fund Balances

Revenues

The TxDMV collected \$1.74 billion at year end with a decrease in revenue of approximately \$168.43 million from the previous year.

- Federal Revenues decreased \$117,871 in FY 2020 due to a half year of billings for the Commercial Vehicle Information Systems and Networks (CVISN) grant which began in late FY 2018.
- Licenses, Fees and Permits reflects only the revenue collected and reportable by the TxDMV. In 2020, TxDMV Fund 0010 revenue from the issuance of licenses, fees, and permits totaled approximately \$153 million. Revenue deposited to the State Highway Fund decreased by approximately \$151.5 million, or 8.8% compared to FY 2019. The decrease in revenue is primarily attributable to economic changes in the second half of the fiscal year due to the COVID-19 pandemic.
- Interest & Investment Income decreased \$152,375 due to interest rates decreasing from 2.4% to 1.6%.

Expenditures

Expenditures totaled \$152.3 million (after adjustments) and increased approximately \$7.19 million from the prior year primarily due to an increase in pre-printed license plates and a Texas Facilities Commission study on repairs for the Camp Hubbard facility.

- Salaries and Wages increased \$2.18 million from the prior year as a result of an overall increase in staffing. There was an average of 713 full-time equivalents (FTE's) in FY 2019 and 727 in FY 2020. Also, the Legislature approved 23 additional positions beginning in FY 2020.
- Professional Fees and Services reflect a net increase of \$2.1 million from FY 2019 primarily due to an increase in IT and Consultant services.
- Materials & Supplies reflect a decrease of \$1.18 million primarily due to additional postage meter funding in FY 2019.
- Repairs and Maintenance reflect a net increase from FY 2019 of \$89,113 primarily due to the Windows 10 Registration and Titling System upgrade.
- Printing and Reproduction reflect a decrease of \$432,832 primarily due to a decrease in Digital Imaging services related to COVID-19 waivers in place.

Exhibit VI – Combined Statement of Net Assets

This exhibit reflects the August 31 cash balances in funds that are fiduciary in nature. TxDMV has no funds that meet the new criteria for fiduciary activity as established in GASB 84 for FY 2020.

Annual Report of Nonfinancial Data

The annual report contains non-financial information that depicts an agency's operational activities during the fiscal year. It includes various schedules required by Government Code 2101.0115 Financial Information Required of State Agencies. The following items are of particular interest.

- **Appropriation Item Transfer Schedule** identifies transfers of appropriated money between the agency's appropriated strategies.
 - In Fiscal Year 2020, transfers were limited to one-time, unanticipated costs.
- **HUB Strategic Plan Progress Form** provides a percentage of historically underutilized businesses (HUBs) used by an agency for specific procurement categories.



- The TxDMV exceeded the Fiscal Year 2020 HUB goals for its three categories: Commodities, Other Services and Special Trade Construction. This is a result of the continued concerted efforts to expand the inclusion of HUBs not already on the Centralized Master Bidders List (CMBL) when requesting bids/quotes on procurements, especially for spot purchases services. Special trade services, i.e. building and facility services, previously processed through the interagency memorandum of agreement with the Texas Department of Transportation, is a growing procurement category for TxDMV. In Fiscal Year 2020, although the percentage spend was less than 2019, total HUB expenditures in this category grew from \$4,918 to \$113,990.
- TxDMV takes a proactive stance on the HUB program. In the new virtual environment, TxDMV continues reaching out to potential HUB vendors through virtual spot-bid fairs, and with online training sessions and online introductory meetings between the vendors and Department business and purchasing staff.
- **Indirect Cost Schedule** provides detailed information about expenditures paid by or on behalf of the TxDMV for employee benefits including Social Security benefits, health insurance, retirement contributions, benefit replacement pay, and workers' and unemployment compensation. It also includes indirect costs related to debt service and services provided by oversight agencies like the Comptroller, Attorney General, Department of Information Resources, and State Auditor.
 - Payroll related costs were higher for FY 2020 due to an overall increase in staffing headcount.
 - The Statewide Cost Allocation Plan (SWCAP) identifies and allocates costs the State incurs for central services such as accounting, computing, payroll and other statewide support provided by specific agencies. Agencies reimburse the General Revenue from other funding sources based on an allocation of current year appropriated funds. In FY 2020, there was a decrease of approximately \$556K for the CAPPs (Centralized Accounting & Payroll/Personnel System) costs allocated from the Comptroller of Public Accounts.
- **Schedule of Professional/Consulting Fees and Legal Service Fees** provides an itemized list of fees paid for professional, consulting and legal services. The schedule includes the name of the vendor paid, the amount paid, and the reason the services were provided.
 - In FY 2020, there was an increase of approximately \$2.1 million in expenditures attributable to Information Technology and Consultant services, primarily related to the Registration and Title System Refactoring project.

Professional/Consulting Services Vendors – Expenditures over \$300,000 in FY 2020

Name	Amount	Service Provided
Apex Systems Inc	761,780.30	Information Technology Services
Carahsoft Technology Corporation	1,310,211.02	Information Technology Services
Datamanusa LLC	305,025.00	Information Technology Services
NF Consulting Services	1,316,678.72	Information Technology Services
Nipun Systems Inc	408,540.93	Information Technology Services
Southwest Research Institute	321,830.38	Consultant Services Other
Southwest Research Institute	313,042.96	Information Technology Services
Texas Department of Information Resources	10,509,272.62	Computer Services-Statewide Tech
Workquest	341,043.60	Information Technology Services

- **Schedule of Space Occupied** lists the name and address of each building an agency occupies, the total amount of square feet leased, and the amount of square feet used in a state-owned building. It also lists the cost per square foot leased, the annual and monthly costs of leased space, and the name of each lessor.
- **Schedule of Vehicles Purchased** lists the vehicles purchased during this fiscal year.
 - Four vehicles were procured during FY 2020.
- **Alternative Fuel Program Status** lists the number of vehicles purchased by fiscal year that use alternative fuel. Fuel usage is listed with the number of gallons used during the year.
- **Schedule of Itemized Purchases** identifies proprietary purchases that are procured from one vendor without considering an equivalent product to be supplied by another vendor. The schedule must provide a written justification explaining the need for the specifications, the reasons that competing products were not satisfactory and additional information as required by the Comptroller. The schedule identifies each product purchased, the amount of the purchase, and the name of the vendor.
 - Promiles Software Development Corp. and Explore Information Service LLC wrote the source code for Texas Permitting and Routing Optimization System (TxPROS) and Texas International Apportioned Registration (TxIRP) and are the only vendors that can provide support services for these applications.

Annual Financial Report

Fiscal Year Ended August 31, 2020



Annual Financial Report

Fiscal Year Ended August 31, 2020



Texas Department *of* Motor Vehicles

Prepared by the
Finance & Administrative Services Division

November 20, 2020

Texas Department of Motor Vehicles Board

Guillermo "Memo" Treviño, Chair

Charles Bacarisse
Stacey Gillman
Brett Graham
Tammy McRae

John M. Prewitt
Paul R. Scott
Shelley Washburn
Law Enforcement
Representative – Vacant

Whitney H. Brewster
Executive Director

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November 20, 2020

Honorable Greg Abbott, Governor
Honorable Glenn Hegar, Texas Comptroller
Mr. Jerry McGinty, Director, Legislative Budget Board
Ms. Lisa R. Collier, CPA, CFE, CIDA, First Assistant State Auditor

Ladies and Gentlemen:

We are pleased to submit the annual financial report of the Texas Department of Motor Vehicles for the year ended August 31, 2020, in compliance with Texas Government Code Annotated, Section 2101.011, and in accordance with the requirements established by the Texas Comptroller of Public Accounts.

Due to the statewide requirements embedded in Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*, the Comptroller of Public Accounts does not require the accompanying annual financial report to comply with all the requirements in this statement. The financial report will be considered for audit by the state auditor as part of the audit of the State of Texas *Comprehensive Annual Financial Report* (CAFR); therefore, an opinion has not been expressed on the financial statements and related information contained in this report.

If you have any questions, please contact Mr. Sergio Rey, Assistant Chief Financial Officer, at (512) 465-1216, or Ms. Linda M. Flores, CPA, Chief Financial Officer, at (512) 465-4125.

Sincerely,

A handwritten signature in blue ink that reads "Whitney H. Brewster".

Whitney H. Brewster
Executive Director

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COMBINED FINANCIAL STATEMENTS

-UNAUDITED-

**EXHIBIT I
COMBINED BALANCE SHEET
Statement of Net Assets - Governmental Funds
For the Year Ended August 31, 2020**

	Governmental Fund Types		Total Governmental	Capital Asset Adjustments	Long Term Liabilities Adjustments	Statement of Net Assets
	General Revenue (EXH A-1)	Special Revenue (EXH B-1)				
Assets						
Current Assets:						
Cash on Hand	\$ 0.00	\$ 37,100.00	\$ 37,100.00	\$	\$	\$ 37,100.00
Cash in Bank	0.00	20,000.00	20,000.00			20,000.00
Cash in State Treasury	29,149,003.65	160,693,082.92	189,842,086.57			189,842,086.57
Legislative Appropriations	15,628,657.21	0.00	15,628,657.21			15,628,657.21
Receivables:						
Federal	0.00	0.00	0.00			0.00
Accounts Receivable	0.00	132,955,412.62	132,955,412.62			132,955,412.62
Due From Other Funds (Note 12)	0.00	0.00	0.00			0.00
Due From Other Agencies (Note 12)	0.00	62,730.00	62,730.00			62,730.00
Consumable Inventories	0.00	54,820.67	54,820.67			54,820.67
Total Current Assets	44,777,660.86	293,823,146.21	338,600,807.07			338,600,807.07
Non - Current Assets:						
Capital Assets:						
Non - Depreciable						
Land and Land Improvements						
Depreciable						
Buildings and Building Improvements						
Less - Accumulated Depreciation						
Furniture and Equipment						
Less - Accumulated Depreciation						
Vehicles, Boats, & Aircraft						
Less - Accumulated Depreciation						
Intangibles Computer Software						
Less - Accumulated Amortization						
Total Non Current Assets				1,922,603.98		1,922,603.98
Total Assets	\$ 44,777,660.86	\$ 293,823,146.21	\$ 338,600,807.07	\$ 1,922,603.98	\$ 0.00	\$ 340,523,411.05

The accompanying notes to the financial statements are an integral part of this exhibit.

-UNAUDITED-

	Governmental Fund Types		Total Governmental	Capital Asset Adjustments	Long Term Liabilities Adjustments	Statement of Net Assets
	General Revenue (EXH A-1)	Special Revenue (EXH B-1)				
Liabilities						
Current Liabilities:						
Payables:						
Vouchers Payable	\$ 368,309.86	\$ 859,380.75	\$ 1,227,690.61	\$	\$	\$ 1,227,690.61
Accounts Payable	895,159.28	8,359,073.56	9,254,232.84			9,254,232.84
Payroll Payable	42,729.71	4,900,614.98	4,943,344.69			4,943,344.69
Due to Other Funds (Note 12)	0.00	0.00	0.00			0.00
Due to Other Agencies (Note 12)	48,671.49	0.00	48,671.49			48,671.49
Unearned Revenues	24,750,343.62	0.00	24,750,343.62			24,750,343.62
Employees Compensable Leave (Note 5)					3,415,798.80	3,415,798.80
Total Current Liabilities	26,105,213.96	14,119,069.29	40,224,283.25		3,415,798.80	43,640,082.05
Non-Current Liabilities:						
Employees' Compensable Leave (Note 5)					1,491,625.98	1,491,625.98
Total Non-Current Liabilities					1,491,625.98	1,491,625.98
Total Liabilities	26,105,213.96	14,119,069.29	40,224,283.25		4,907,424.78	45,131,708.03
Fund Financial Statement						
Fund Balances:						
Non Spendable (Inventory)	0.00	54,820.67	54,820.67			54,820.67
Restricted	0.00	279,649,256.25	279,649,256.25			279,649,256.25
Committed	3,955,694.80	0.00	3,955,694.80			3,955,694.80
Assigned	48,015.90	0.00	48,015.90			48,015.90
Unassigned	14,668,736.20	0.00	14,668,736.20			14,668,736.20
Total Fund Balances	18,672,446.90	279,704,076.92	298,376,523.82			298,376,523.82
Total Liabilities and Fund Balance	\$ 44,777,660.86	\$ 293,823,146.21	\$ 338,600,807.07			
Government-Wide Statement of Net Assets						
Net Assets:						
Invested in Capital Assets, Net of Related Debt				\$ 1,922,603.98	\$	\$ 1,922,603.98
Unrestricted					(4,907,424.78)	(4,907,424.78)
Total Net Assets				\$ 1,922,603.98	\$ (4,907,424.78)	\$ 295,391,703.02

-UNAUDITED-

EXHIBIT II
COMBINED STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES
Statement of Activities - Governmental Funds
For the Year Ended August 31, 2020

	Governmental Fund Types			Capital Assets Adjustments	Long-Term Liabilities Adjustments	Statement of Activities
	General (EXH A-2)	Special Revenue (EXH B-2)	Total Governmental			
Revenues						
Legislative Appropriations:						
Original Appropriations	\$ 12,835,851.00	\$ 0.00	\$ 12,835,851.00	\$	\$	\$ 12,835,851.00
Additional Appropriations	83,452.07	0.00	83,452.07			83,452.07
Federal Revenues	0.00	106,386.71	106,386.71			106,386.71
Federal Pass-Through Revenues	0.00	0.00	0.00			0.00
State Grant Pass- Through	0.00	0.00	0.00			0.00
Licenses, Fees and Permits	46,077.32	1,724,236,393.17	1,724,282,470.49			1,724,282,470.49
Interest & Investment Income	6,503.35	2,576,740.52	2,583,243.87			2,583,243.87
Settlement of Claims	0.00	0.00	0.00			0.00
Sales of Goods and Services	0.00	244,260.00	244,260.00			244,260.00
Other	(15,914.91)	34,685.21	18,770.30			18,770.30
Total Revenues	12,955,968.83	1,727,198,465.61	1,740,154,434.44			1,740,154,434.44
Expenditures						
Salaries and Wages	365,476.26	40,780,199.35	41,145,675.61		981,007.85	42,126,683.46
Payroll Related Costs	88,631.90	15,143,272.69	15,231,904.59			15,231,904.59
Professional Fees and Services	527,179.64	17,050,599.37	17,577,779.01			17,577,779.01
Travel	6,631.22	229,878.41	236,509.63			236,509.63
Materials and Supplies	362,664.10	14,658,845.94	15,021,510.04			15,021,510.04
Communications and Utilities	1,577.76	5,013,709.66	5,015,287.42			5,015,287.42
Repairs and Maintenance	(297,417.74)	3,851,209.02	3,553,791.28			3,553,791.28
Rentals and Leases	6,914.95	1,039,835.98	1,046,750.93			1,046,750.93
Printing and Reproduction	4,594.68	4,117,148.01	4,121,742.69			4,121,742.69
Claims and Judgements	0.00	0.00	0.00			0.00
Federal Pass-Through Expenditures	0.00	0.00	0.00			0.00
State Grant Pass-Through Expenditures	13,673.00	0.00	13,673.00			13,673.00
Intergovernmental Payments	12,162,092.31	0.00	12,162,092.31			12,162,092.31
Public Assistance Programs	88,691.72	0.00	88,691.72			88,691.72
Other Operating Expenditures	22,619.56	35,430,282.99	35,452,902.55			35,452,902.55
Capital Outlay	0.00	357,661.84	357,661.84	(357,661.84)		0.00
Depreciation Expense			0.00	646,630.46		646,630.46
Total Expenditures	13,353,329.36	137,672,643.26	151,025,972.62	288,968.62	981,007.85	152,295,949.09
Excess (Deficit) of Revenues over Expenditures	(397,360.53)	1,589,525,822.35	1,589,128,461.82	(288,968.62)	(981,007.85)	1,587,858,485.35
Other Financing Sources (Uses)						
Transfers In (Note 12)	599,051.23	0.00	599,051.23			599,051.23
Transfers Out (Note 12)	(667,771.97)	(1,575,461,468.64)	(1,576,129,240.61)			(1,576,129,240.61)
Sale of Capital Assets	4,267.30	1,422.43	5,689.73	(6,372.50)		(682.77)
Legislative Financing Sources	0.00	0.00	0.00			0.00
Insurance Recoveries	0.00	0.00	0.00			0.00
Legislative Transfers In (Note 12)	0.00	0.00	0.00			0.00
Legislative Transfers Out (Note 12)	0.00	0.00	0.00			0.00
Gain (Loss) on Capital Assets	0.00	0.00	0.00	3,129.28		3,129.28
Inc (Dec) in Net Assets Due to Interagency Transfer	0.00	0.00	0.00			0.00
Total Other Financing Sources (Uses)	(64,453.44)	(1,575,460,046.21)	(1,575,524,499.65)	(3,243.22)	0.00	(1,575,527,742.87)
Net Change in Fund Balances/Net Assets	(461,813.97)	14,065,776.14	13,603,962.17	(292,211.84)	(981,007.85)	12,330,742.48
Fund Financial Statement - Fund Balance						
Fund Balance - Beginning	19,156,850.34	265,638,300.78	284,795,151.12			284,795,151.12
Restatements			0.00			0.00
Fund Balance as Restated	19,156,850.34	265,638,300.78	284,795,151.12			284,795,151.12
Appropriations Lapsed	(22,589.47)		(22,589.47)			(22,589.47)
Fund Balances - August 31, 2020	\$ 18,672,446.90	\$ 279,704,076.92	\$ 298,376,523.82			\$ 297,103,304.13
Government-wide Statement of Net Assets						
Net Change in Net Assets			\$ 298,376,523.82	(292,211.84)	(981,007.85)	\$ 297,103,304.13
Net Assets-Beginning				2,214,815.82	(3,926,416.93)	(1,711,601.11)
Restatements						0.00
Net Assets, September 1, 2020, as Restated and Adjusted				2,214,815.82	(3,926,416.93)	(1,711,601.11)
Net Assets-August 31, 2020			\$ 298,376,523.82	\$ 1,922,603.98	\$ (4,907,424.78)	\$ 295,391,703.02

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NOTES TO THE FINANCIAL STATEMENTS

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Scope of Entity

The Texas Department of Motor Vehicles (TxDMV), created in 2009 by the authority of H.B. 3097, 81st Legislature, Regular Session, is an agency of the State of Texas. TxDMV is responsible for titling and registering vehicles, licensing and regulating of the motor vehicle sales and distribution, salvage dealers, registering commercial oversize/overweight (OS/OW) vehicles, and providing auto theft prevention grants.

The TxDMV has not identified any component units which should have been blended into an appropriated fund.

Basis of Presentation

Due to the statewide requirements included in Governmental Accounting Standards Board Statement No. 34, Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments, the Comptroller of Public Accounts does not require the accompanying annual financial report to comply with all the requirements of this statement. The financial report will be considered for audit by the State Auditor as part of the audit of the State of Texas Comprehensive Annual Financial Report; therefore, an opinion has not been expressed on the financial statements and related information contained in this report.

Fund Structure

The accompanying financial statements are presented on the basis of funds, each of which is considered a separate accounting entity.

Governmental Fund Types & Government-wide Adjustment Fund Types

General Revenue Funds

General Revenue Fund (0001) – This fund is used to account for all financial resources of the State except those required to be accounted for in another fund.

License Plate Trust Fund (0802) – This fund is used to receive and account for fees charged from the sale of specialty license plates collected under Subchapter G, Transportation Code. Funds are to be used in accordance with their specific statutory purpose.

Suspense Funds

Suspense Funds, known as Agency Funds in prior years, are used to account for assets held in a custodial capacity for the benefit of other agencies or individuals. These funds had previously been classified as fiduciary activities. However, with the State of Texas implementing GASB 84 in Fiscal Year 2020, these funds are now classified as governmental and are consolidated with General Revenue Funds.

Proportional Registration Distributive Trust Fund (0021) – This fund is used primarily to collect and distribute registration fees from trucking companies that operate in more than one state. The fees are distributed to the individual states based on mileage driven.

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Intermodal Container & Milk Transport TxDMV Fund (1623) – This fund is used as a holding account for the county and/or municipality portions of three new oversize/overweight permit fees created in FY 2018. The fees are held until they can be disbursed to the appropriate county or municipality.

Child Support Deductions (0807) – This fund is used as a holding account where child support payroll deductions are held until disbursed.

City, County, MTA, & SPD Fund (0882) - This fund is used as a holding account where taxes for the State are collected until disbursed.

Suspense Fund (0900) - This fund is used when depositing funds where final disposition has not been determined at the time of the receipt of funds.

Direct Deposit Correction Account (0980) – This fund is used to temporarily hold and account for direct deposits that are unable to be processed until the correct disposition of the item is determined.

Special Revenue Funds

State Highway Fund (0006) – This fund is restricted to expenditures for the building, maintaining, and policing of the State highways. It derives its financing primarily from legally dedicated revenues such as motor fuels tax and vehicle registration fees, and from federal reimbursements for selected construction projects.

Texas Department of Motor Vehicles Fund (0010) – This fund is used by the department for operations, administration, enforcement, accounting costs and related liabilities for the fund. Revenue includes fees from motor vehicle registration, title certificates, special vehicle permits, specialty license plates and other transportation-related permits. This fund was initially enacted by H.B. 2202, 83rd Legislature; however, it was not exempted from funds consolidation. The 84th Legislature recreated the fund through S.B. 1512, and it was exempted in funds consolidation.

Capital Assets Adjustments Fund Type

Capital Assets Adjustment fund type is used to convert governmental fund types' capital assets from modified accrual to full accrual.

Long Term Liabilities Adjustments Fund Type

The Long-Term Liabilities Adjustments fund type is used to convert all other governmental fund types' debt from modified accrual to full accrual. The composition of this fund type is discussed in Note 5.

Fiduciary Fund Types

Fiduciary funds account for assets held by the State in a trustee capacity or as an agent for individuals, private organizations, other governmental units, and/or other funds. When assets are held under the terms of a formal trust agreement, either a pension trust fund, or a private purpose trust fund is used. TxDMV has no funds that meet the new criteria for fiduciary activity as established in GASB 84 for Fiscal Year 2020.

Basis of Accounting

The basis of accounting determines when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements. The accounting and financial reporting treatment applied to a fund is

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determined by its measurement focus.

Governmental fund types that build the fund financial statements are accounted for using the modified accrual basis of accounting. Under the modified accrual basis, revenues are recognized in the period in which they become measurable and available to finance operations of the fiscal year or liquidate liabilities existing at fiscal year-end. The State of Texas considers receivables collected within sixty days after year-end to be available and recognizes them as revenues of the current year for Fund Financial Statements prepared on the modified accrual basis. For federal contracts and grants, revenues have been accrued to the extent earned by eligible expenditures within each fiscal year. Expenditures and other uses of financial resources are recognized when the related liability is incurred.

Governmental adjustment fund types that will build the government-wide financial statements are accounted for using the full accrual method of accounting. This includes capital assets, accumulated depreciation, unpaid Employee Compensable Leave, the unmatured debt service (principal and interest) on general long-term liabilities, long-term capital leases, and long-term claims and judgments. The activity will be recognized in these new fund types.

Budgets and Budgetary Accounting

The budget is prepared biennially and represents appropriations authorized by the Legislature and approved by the Governor (the General Appropriations Act). The Board adopts an annual operating budget and policies consistent with these appropriations. Encumbrance accounting is utilized for budgetary control purposes. An encumbrance is defined as an outstanding purchase order or other commitment for goods or services. It reserves a part of the applicable appropriation for future expenditure. Encumbrance balances are reported in Note 15.

Unencumbered and unexpended funds are generally subject to lapse 60 days after the end of the fiscal year for which they were appropriated.

Assets, Liabilities and Fund Balances

Assets

Cash and Cash Equivalents

Short-term highly liquid investments with an original maturity of three months or less are considered cash equivalents. Cash in bank represents the TxDMV Travel Advance Fund.

Receivables

The receivables represent revenue from fees and federal funds that has been earned but not received. This account is presented net of Allowance for Bad Debts.

Inventories and Prepaid Items

This represents supplies and postage on hand. Supplies for governmental funds are accounted for using the consumption method of accounting. The cost of these items is recognized as an expenditure when items are consumed.

Capital Assets

Assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of one year are capitalized. These assets are capitalized at cost or, if purchased, at appraised fair value as of the date of acquisition. Depreciation is reported on all "exhaustible" assets. Assets are depreciated over the estimated useful life of the asset using the straight-line method.

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Liabilities

Accounts Payable

Accounts payable represents the liability for the value of assets or services received at the balance sheet date for which payment is pending.

Payroll Payable

Payroll payable represents the liability for the August payroll payable on September 1st.

Employees' Compensable Leave

Employees' compensable leave represents the liability that becomes due upon the occurrence of relevant events such as resignations, retirements, and uses of leave balances by covered employees. Liabilities are reported separately as either current or non-current in the statement of net assets. These obligations are normally paid from the same funding source from which each employee's salary or wage compensation was paid.

Fund Balance/Net Assets

The difference between fund assets and liabilities is "Net Assets" on the government-wide, proprietary and fiduciary fund statements, and the "Fund Balance" is the difference between fund assets and liabilities on the governmental fund statements.

Fund Balance Components

Nonspendable fund balance includes amounts not available to be spent because they are either (1) not in spendable form or (2) legally or contractually required to be maintained intact.

Restricted fund balance includes those resources that have constraints placed on their use through external parties or by law through constitutional provisions.

Committed fund balance can only be used for specific purposes pursuant to constraints imposed by formal action of the State's highest level of decision-making authority (the Legislature). Those committed amounts cannot be used for any other purposes unless the Legislature removes or changes the specified use by taking the same action it employed to previously commit those amounts.

Assigned fund balance amounts are constrained by the agency's intent to use them for specific purposes that are neither restricted nor committed.

Unassigned fund balance is the residual classification for the general fund. This classification represents fund balance that was not assigned to other funds and was not restricted, committed or assigned to specific purposes within the general fund.

Invested in Capital Assets, Net of Related Debt

Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for outstanding balances for bond, notes, and other debt that are attributed to the acquisition, construction or improvement of those assets.

Unrestricted Net Assets

Unrestricted net assets consist of net assets that have no constraints placed on net asset use by external sources or by law through constitutional provisions or enabling legislation. Unrestricted net assets often have constraints on resources, which are imposed by management but can be removed or modified.

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Interfund Activities and Balances

The agency has the following types of transactions among funds:

Transfers

Legally required transfers that are reported when incurred as Transfers In by the recipient fund and as Transfers Out by the disbursing fund.

Reimbursements

Reimbursements are repayments from funds responsible for expenditures or expenses to funds that made the actual payment. Reimbursements of expenditures made by one fund for another that are recorded as expenditures in the reimbursing fund and as a reduction of expenditures in the reimbursed fund. Reimbursements are not displayed in the financial statements.

Accrual of Operating Transfers, Reimbursements, and Residual Equity Transfers are shown as Due To and Due From instead of accounts receivable or accounts payable.

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NOTE 2: CAPITAL ASSETS

A summary of changes in Capital Assets for the year ended August 31, 2020, is presented below:

Governmental Activities	PRIMARY GOVERNMENT							
	Balance 09/01/19	Adjust/ Restate	Reclass. Completed CIP	Reclass. Increase Inter-Agency Transaction	Reclass. Decrease Inter-Agency Transaction	Additions	Deletions	Balance 08/31/20
Non-Depreciable Assets	\$	\$	\$		\$	\$	\$	\$
Total Non-Depreciable Assets								
Depreciable Assets								
Buildings/Building Improvements								
Furniture and Equipment	4,670,870.25					268,463.84	(56,492.04)	4,882,842.05
Vehicles, Boats, & Aircraft	1,307,773.18					89,198.00	(55,275.00)	1,341,696.18
Other Assets								
Total Depreciable Assets	5,978,643.43					357,661.84	(111,767.04)	6,224,538.23
Less Accumulated Depreciation for:								
Buildings/Building Improvements								
Furniture and Equipment	(3,451,252.21)					(403,190.74)	53,248.82	(3,801,194.13)
Vehicles, Boats, & Aircraft	(461,471.03)					(143,728.00)	55,275.00	(549,924.03)
Other Capital Assets								
Total Accumulated Depreciation	(3,912,723.24)					(546,918.74)	108,523.82	(4,351,118.16)
Depreciable Assets, Net	2,065,920.19					(189,256.90)	(3,243.22)	1,873,420.07
Amortizable Assets – Intangible:								
Land Use Rights								
Computer Software	3,875,591.07							3,875,591.07
Other Capital Intangible								
Total Amortizable Assets – Intangible	3,875,591.07							3,875,591.07
Less Accumulated Amortization for:								
Land Use Rights								
Computer Software	(3,726,695.44)					(99,711.72)		(3,826,407.16)
Other Capital Intangible								
Total Accumulated Amortization	(3,726,695.44)					(99,711.72)		(3,826,407.16)
Amortizable Assets – Intangible, Net	148,895.63					(99,711.72)		49,183.91
Governmental Activities Capital Assets, Net	\$ 2,214,815.82					(288,968.62)	(3,243.22)	1,922,603.98

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NOTE 3: DEPOSITS, INVESTMENTS, & REPURCHASE AGREEMENTS

Deposits of Cash in Bank

As of August 31, 2020, the carrying amount of deposits was \$20,000.00 as presented below:

	Amount
Cash in Bank – Carrying Amount	\$ 20,000.00
Total Cash in Bank (Exhibit I)	\$ 20,000.00

NOTE 4: SHORT-TERM DEBT

Not Applicable

NOTE 5: LONG-TERM LIABILITIES

Changes in Long-Term Liabilities

During the year ended August 31, 2020, the following changes occurred in liabilities.

Governmental Activities	Balance 9/01/19	Additions	Reductions	Balance 8/31/20	Amounts Due Within Year
Compensable Leave	\$3,926,416.93	\$4,815,512.68	\$3,834,504.83	\$4,907,424.78	\$3,415,798.80

Employees' Compensable Leave

A State employee is entitled to be paid for all unused vacation time accrued, in the event of the employee's resignation, dismissal, or separation from State employment, provided the employee has had continuous employment with the State for six months. Expenditures for accumulated vacation leave balances are recognized in the period paid or taken in governmental fund types. For these fund types, the liability for unpaid benefits is recorded in the Statement of Net Assets. An expense and liability for proprietary fund types are recorded in the proprietary funds as the benefits accrue to employees. No liability is recorded for non-vesting accumulating rights to receive sick pay benefits.

NOTE 6: BONDED INDEBTEDNESS

Not Applicable

NOTE 7: DERIVATIVE INSTRUMENTS

Not Applicable

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NOTE 8: LEASES

Operating Leases

Included in the expenditures reported in the financial statement are the following amounts of rent paid or due under operating lease obligations:

Fund Type	Amount
Fund 0001	\$ 4,325.62
Fund 0010	\$ 998,368.37

Note: Future minimum lease rental payments under non-cancelable operating leases having an initial term in excess of one year are as follows:

Year Ended August 31,	Amount
2021	\$ 908,637.38
2022	801,909.39
2023	716,779.71
2024	424,029.85
2025	323,945.67
2026-29	248,350.78
Total Minimum Future Lease Rental Payments	\$ 3,423,652.78

NOTE 9: PENSION PLANS AND OPTIONAL RETIREMENT PROGRAM

Not Applicable

NOTE 10: DEFERRED COMPENSATION

Not Applicable

NOTE 11: POST EMPLOYMENT HEALTH CARE AND LIFE INSURANCE BENEFITS

Not Applicable

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NOTE 12: INTERFUND ACTIVITY AND TRANSACTIONS

The agency experienced routine transfers with other State agencies, which were consistent with the activities of the fund making the transfer. Repayment of interfund balances will occur within one year from the date of the financial statement. Individual balances and activity at August 31, 2020, are as follows:

	Transfer In	Transfer Out	Source
General Revenue (01)			
Appd Fund 0802, D23 fund 0802			
Agy 300, D23 fund 0803	8,204.94		Shared Fund
Agy 300, D23 fund 0804	12,859.68		Shared Fund
Agy 300, D23 fund 0805		(12,385.18)	Shared Fund
Agy 300, D23 fund 0807		(1,610.20)	Shared Fund
Agy 302, D23 fund 0804	1,861.43		Shared Fund
Agy 302, D23 fund 0805		180.77	Shared Fund
Agy 305, D23 fund 0015		930.95	Shared Fund
Agy 306, D23 fund 0802	2,524.91		Shared Fund
Agy 307, D23 fund 0802	201.66		Shared Fund
Agy 332, D23 fund 0802		397.12	Shared Fund
Agy 403, D23 fund 3004		3,536.70	Shared Fund
Agy 403, D23 fund 3005	183.59		Shared Fund
Agy 403, D23 fund 3006		45.39	Shared Fund
Agy 403, D23 fund 3008	4,232.86		Shared Fund
Agy 407, D23 fund 0802	2,540.18		Shared Fund
Agy 411, D23 fund 0802		(2,882.31)	Shared Fund
Agy 506, D23 fund 0802	1,806.08		Shared Fund
Agy 529, D23 fund 0802	11,310.93		Shared Fund
Agy 530, D23 fund 0802		8,073.65	Shared Fund
Agy 537, D23 fund 0802	5,453.93		Shared Fund
Agy 537, D23 fund 0803	65,254.31		Shared Fund
Agy 537, D23 fund 0804	1,213.19		Shared Fund
Agy 537, D23 fund 0805	4,268.29		Shared Fund
Agy 542, D23 fund 0802	0.03		Shared Fund
Agy 542, D23 fund 4100	4,283.69		Shared Fund
Agy 542, D23 fund 4200	5,489.46		Shared Fund
Agy 551, D23 fund 0802	30,588.98		Shared Fund
Agy 555, D23 fund 1802	2,431.64		Shared Fund
Agy 555, D23 fund 2802		279.35	Shared Fund
Agy 555, D23 fund 3802	628.30		Shared Fund
Agy 576, D23 fund 0802	8,284.47		Shared Fund
Agy 582, D23 fund 0802	268.92		Shared Fund
Agy 701, D23 fund 2242		72.35	Shared Fund
Agy 701, D23 fund 2250		308.15	Shared Fund
Agy 701, D23 fund 2260		23.96	Shared Fund
Agy 701, D23 fund 2270		164.00	Shared Fund
Agy 701, D23 fund 2271		173.97	Shared Fund
Agy 701, D23 fund 2273		402.73	Shared Fund
Agy 701, D23 fund 2274		286.02	Shared Fund

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	Transfer In	Transfer Out	Source
Agy 711, D23 fund 0802	6,969.22		Shared Fund
Agy 714, D23 fund 0802		12,508.90	Shared Fund
Agy 715, D23 fund 0802		2,349.87	Shared Fund
Agy 717, D23 fund 0802	4,142.25		Shared Fund
Agy 718, D23 fund 0802	9,142.09		Shared Fund
Agy 721, D23 fund 0802		234,406.13	Shared Fund
Agy 724, D23 fund 0802	3,814.61		Shared Fund
Agy 730, D23 fund 0802		82.55	Shared Fund
Agy 732, D23 fund 0802	24.15		Shared Fund
Agy 733, D23 fund 0802	11,665.37		Shared Fund
Agy 734, D23 fund 0802	12.07		Shared Fund
Agy 737, D23 fund 0802	53.49		Shared Fund
Agy 738, D23 fund 0802		6,034.57	Shared Fund
Agy 743, D23 fund 0802		115.19	Shared Fund
Agy 751, D23 fund 0802	1,274.37		Shared Fund
Agy 752, D23 fund 0802	11,977.04		Shared Fund
Agy 753, D23 fund 0802		2,131.77	Shared Fund
Agy 754, D23 fund 0802		22,492.72	Shared Fund
Agy 755, D23 fund 0802	570.11		Shared Fund
Agy 756, D23 fund 0802	1,713.73		Shared Fund
Agy 757, D23 fund 0802		4,056.17	Shared Fund
Agy 759, D23 fund 0802		705.24	Shared Fund
Agy 765, D23 fund 0802		174.61	Shared Fund
Agy 781, D23 fund 4003	1,832.93		Shared Fund
Agy 781, D23 fund 4004	(0.22)		Shared Fund
Agy 781, D23 fund 4005	(2,250.62)		Shared Fund
Agy 781, D23 fund 4006	0.08		Shared Fund
Agy 781, D23 fund 4007	105.79		Shared Fund
Agy 781, D23 fund 4008	23,034.34	(1,107.32)	Shared Fund
Agy 781, D23 fund 4009	13,449.89	(916.64)	Shared Fund
Agy 781, D23 fund 4010	87.38		Shared Fund
Agy 781, D23 fund 4011	618.92		Shared Fund
Agy 781, D23 fund 4012	345.61		Shared Fund
Agy 781, D23 fund 4013	17.70		Shared Fund
Agy 781, D23 fund 4014	149.08		Shared Fund
Agy 781, D23 fund 4015	43.71		Shared Fund
Agy 781, D23 fund 4016	91.81		Shared Fund
Agy 781, D23 fund 4017	114.72		Shared Fund
Agy 781, D23 fund 4018	149.98		Shared Fund
Agy 781, D23 fund 4019	80.13		Shared Fund
Agy 781, D23 fund 4020	(0.38)		Shared Fund
Agy 781, D23 fund 4021	21.48		Shared Fund
Agy 781, D23 fund 4022	(285.83)		Shared Fund
Agy 781, D23 fund 4023	43.76		Shared Fund
Agy 781, D23 fund 4025	(384.46)		Shared Fund
Agy 783, D23 fund 0802		200.76	Shared Fund
Agy 802, D23 fund 3030		38,613.47	Shared Fund

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	Transfer In	Transfer Out	Source
Agy 802, D23 fund 3043		111,018.79	Shared Fund
Agy 802, D23 fund 3044	89,135.84	(471.16)	Shared Fund
Agy 802, D23 fund 3045		76,506.59	Shared Fund
Agy 802, D23 fund 3046	33,049.27	(284.52)	Shared Fund
Agy 802, D23 fund 3047		75,708.54	Shared Fund
Agy 802, D23 fund 3048		22,842.64	Shared Fund
Agy 802, D23 fund 3049	22,092.81	(31.81)	Shared Fund
Agy 802, D23 fund 3050	7,503.97	(1,400.00)	Shared Fund
Agy 802, D23 fund 3051	6,538.26		Shared Fund
Agy 802, D23 fund 3057		1,990.60	Shared Fund
Agy 802, D23 fund 3116		33,728.42	Shared Fund
Agy 802, D23 fund 3120		11,093.35	Shared Fund
Agy 802, D23 fund 3142		1,291.60	Shared Fund
Agy 802, D23 fund 3151	253.60		Shared Fund
Agy 802, D23 fund 3152		3,982.47	Shared Fund
Agy 808, D23 fund 0802	1,338.37		Shared Fund
Agy 813, D23 fund 0802	175,899.94		Shared Fund
Agy 902, D23 fund 8020	723.40		Shared Fund
Appd Fund 0001, D23 fund 0001			
Agy 902, D23 fund 0001		11,951.05	Surplus Property
Total Transfer In/Out Other Agencies	599,051.23	667,771.97	
Special Revenue (02)			
Appd Fund 0006, D23 fund 0006			
Agy 601, D23 fund 0006		1,575,461,468.64	Shared Cash
Total Transfers In/Out	599,051.23	1,576,129,240.61	

	Due from Other Agencies	Due to Other Agencies	Source
General Revenue (01)			
Appd Fund 0802, D23 fund 0802			
Agy 902, D23 fund 0001	22,680.00		Shared Fund
Agy 902, D23 fund 0010	40,050.00		Shared Fund
Agy 701, D23 fund 2242		1,302.56	Shared Fund
Agy 701, D23 fund 2250		3,113.78	Shared Fund
Agy 701, D23 fund 2260		46.05	Shared Fund
Agy 701, D23 fund 2270		2,840.39	Shared Fund
Agy 701, D23 fund 2271		2,034.28	Shared Fund
Agy 701, D23 fund 2273		5,304.16	Shared Fund
Agy 701, D23 fund 2274		3,580.77	Shared Fund
Agy 802, D23 fund 3030		9,227.54	Shared Fund
Agy 802, D23 fund 3043		13,901.58	Shared Fund
Agy 802, D23 fund 3116		7,320.38	Shared Fund
Total Due From/ To Other Agencies	62,730.00	48,671.49	

-UNAUDITED-

NOTE 13: CONTINUANCE SUBJECT TO REVIEW

Under the Texas Sunset Act, the agency will be abolished effective September 1, 2031, unless continued in existence by the Legislature as provided by the Act. If abolished, the agency may continue until September 1, 2032, to close out its operations.

NOTE 14: ADJUSTMENTS TO FUND BALANCES AND NET POSITION

Not Applicable

NOTE 15: CONTINGENCIES AND COMMITMENTS

Federal Assistance

The TxDMV receives federal financial assistance for specific purposes that are subject to review or audit by the federal grantor agencies. Entitlement to this assistance is generally conditional upon compliance with the terms and conditions of the grant agreements and applicable federal regulations. Such audits could lead to requests for reimbursements to grantor agencies for expenditures disallowed under the terms of the grant. Management believes such disallowance, if any, will be immaterial.

Encumbrances

As of August 31, 2020, the TxDMV had encumbered the following amounts in governmental funds for signed contracts and purchase orders:

	General Revenue Fund (0001)	Special Revenue Fund (0006)	Texas Department of Motor Vehicle Fund (0010)
Encumbrances	\$ 5,829,803.47	\$ 0.00	\$ 12,258,636.05

NOTE 16: SUBSEQUENT EVENTS

Not Applicable

NOTE 17: RISK MANAGEMENT

The department is exposed to a wide range of risks, due to the size, scope and nature of its activities. Some of these risks include, but are not limited to property and casualty losses, workers' compensation and health benefit claims, theft, damage of assets, etc. The department retains these risks, and manages them through insurance and safety programs. In FY 2020, the department had \$0.00 in payments related to claims.

	Beginning Balance	Increases	Decreases	Ending Balance
2020	-	\$0.00	\$0.00	-
2019	-	\$ 6,500.00	\$ (6,500.00)	-

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NOTE 18: MANAGEMENT DISCUSSION AND ANALYSIS

The Texas Department of Motor Vehicles (TxDMV) is funded through the TxDMV Fund, with the exception of the Motor Vehicle Crime Prevention Authority (MVCPA), which is funded through the General Revenue (GR) Fund.

During FY 2020, revenue for all funds totaled \$1.74 billion. This represents a decrease of \$168.43 million or 8.82% compared to FY 2019 revenues of \$1.91 billion. Of the FY 2020 amount, \$1.57 billion was deposited into the State Highway Fund, \$155.96 million was deposited into the TxDMV Fund and \$12.96 million was deposited for use by MVCPA. The decrease in revenue is primarily attributable to economic changes in the second half of the fiscal year due to the COVID-19 pandemic. Major factors contributing to the decrease in FY 2020 are due to the effect of the Governor suspending and waiving certain fees/permits beginning March 16 and continuing through the end of the fiscal year.

Title revenues decreased due to a drop in overall vehicle sales as compared to FY 2019, as well as a loss in delinquent title transfer penalty revenue from March 16 to August 31 due to those penalty fees being temporarily waived. Registration and associated Processing & Handling fee revenue decreased in FY 2020 compared to FY 2019, also related to the waivers.

FY 2020 Capital Budget expenditures totaled \$18.1 million, primarily consisting of expenditures for the Data Center Consolidation services (\$10.4 million); TxDMV Automation project (\$3.1 million); County Technology Replacement & Upgrades (\$2.1 million); and TxDMV Headquarters Maintenance (\$1.3 million). Other capital expenditures (\$1.2 million) were for Agency Growth & Enhancement, Replacement Vehicles, Personal Computer (PC) Replacement, Cybersecurity, Regional Service Center Maintenance and TxDMV Headquarters Badge and Security.

FY 2020 expenditures totaled \$152.30 million, an increase of \$7.19 million, or 4.95% compared to FY 2019 expenditures of \$145.11 million. The primary factors contributing to this increase include 1) an increase in pre-printed license plates and 2) additional money for a Texas Facilities Commission study on repairs for the Camp Hubbard facility in Other Operating Expenditures, totaling \$3.80 million. An additional \$2.10 million increase in Professional Fees and Services is attributable to Information Technology and Consultant services, primarily related to the Registration and Title System Refactoring project. Other significant items included a \$1.20 million increase in Salaries and Wages due to higher full-time employee headcount in FY 2020.

Through the end of August 2020, TxDMV expended a total of \$1.75 million in response to COVID-19. The expenditures are primarily for staff time, the acquisition of personal protective equipment (PPE) items for employees and customers, cleaning supplies and facility preparation activities such as cleaning and defogging services and the installation of plexiglass.

NOTE 19: THE FINANCIAL REPORTING ENTITY

Not Applicable

NOTE 20: STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Not Applicable

NOTE 21:

Not Applicable to the reporting requirement process.

-UNAUDITED-

NOTE 22: DONOR RESTRICTED ENDOWMENTS

Not Applicable

NOTE 23: EXTRAORDINARY AND SPECIAL ITEMS

Not Applicable

NOTE 24: DISAGGREGATION OF RECEIVABLE AND PAYABLE BALANCES

Not Applicable

NOTE 25: TERMINATION BENEFITS

Not Applicable

NOTE 26: SEGMENT INFORMATION

Not Applicable

NOTE 27: SERVICE CONCESSION ARRANGEMENTS

Not Applicable

NOTE 28: DEFERRED OUTFLOWS AND DEFERRED INFLOWS OF RESOURCES

Not Applicable

NOTE 29: TROUBLE DEBT RESTRUCTURING

Not Applicable

NOTE 30: NON-EXCHANGE FINANCIAL GUARANTEES

Not Applicable

NOTE 31: TAX ABATEMENTS

Not Applicable

-UNAUDITED-

NOTE 32: FUND BALANCES

GAAP Fund	Fund	AFR 54 Class	Amount	Citation	Purpose
0010	0010	Restricted	\$149,812,305.96	TEXAS TRANSPORTATION CODE ANNOTATED SECTION 1001.151, 1001.152	Used by the department for operations, administration, enforcement, accounting costs and related liabilities for the fund. Revenue includes fees from motor vehicle registration, title certificates, special vehicle permits, specialty license plates and other transportation-related permits.
0010	0900	Restricted	\$0.00	TEXAS GOVERNMENT CODE ANNOTATED SECTION 403.035	To provide a temporary depository for money held in suspense pending final disposition. Items held in the fund are cleared to the various Special Funds or the General Revenue Fund, or refunded to the payer.

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COMBINING FINANCIAL STATEMENTS

-UNAUDITED-

**EXHIBIT A-1
COMBINING BALANCE SHEET
All General and Consolidated Funds
For the Year Ended August 31, 2020**

	<u>General Revenue Account (0001)</u>	<u>License Plate Trust Fund Account (0802)</u>	<u>Returned Items Type Activities Account (9001)</u>	<u>Deposit Default Type Activities Account (9000)</u>
Assets				
Current Assets:				
Cash on Hand	\$	\$	\$	\$
Cash in Bank				
Cash in State Treasury	15,914.91	4,048,193.17	(15,914.91)	
Legislative Appropriations	15,628,657.21			
Receivables:				
Federal				
Accounts Receivable				
Due From Other Funds (Note 12)				
Due From Other Agencies (Note 12)				
Consumable Inventories				
Total Current Assets	<u><u>15,644,572.12</u></u>	<u><u>4,048,193.17</u></u>	<u><u>(15,914.91)</u></u>	<u><u>0.00</u></u>
Liabilities				
Current Liabilities				
Payables:				
Vouchers Payable	17,843.00			
Account Payable	895,159.28			
Payroll Payable	42,729.71			
Due to Other Funds (Note 12)				
Due to Other Agencies (Note 12)		48,671.49		
Unearned Revenues				
Total Current Liabilities	<u><u>955,731.99</u></u>	<u><u>48,671.49</u></u>	<u><u>0.00</u></u>	<u><u>0.00</u></u>
Fund Balances				
Non Spendable (Inventory)				
Restricted				
Committed		3,955,694.80		
Assigned				
Unassigned	14,688,840.13	43,826.88	(15,914.91)	
Total Fund Balance	<u><u>14,688,840.13</u></u>	<u><u>3,999,521.68</u></u>	<u><u>(15,914.91)</u></u>	<u><u>0.00</u></u>
Total Liabilities and Fund Balances	\$ <u><u>15,644,572.12</u></u>	\$ <u><u>4,048,193.17</u></u>	\$ <u><u>(15,914.91)</u></u>	\$ <u><u>0.00</u></u>

-UNAUDITED-

EXHIBIT A-1 (CONTINUED)
COMBINING BALANCE SHEET
All General and Consolidated Funds
For the Year Ended August 31, 2020

	Suspense Type Activities Account (0900)	Intermodal Container & Milk Transport Account (1623)	Proportional Registration Distributive Fund Account (0021)	Child Support Employee Deduction Account (8070)	Total
Assets					
Current Assets:					
Cash on Hand	\$	\$	\$	\$	\$ 0.00
Cash in Bank					0.00
Cash in State Treasury	551,445.93	11,522.40	24,533,136.15	4,706.00	29,149,003.65
Legislative Appropriations					15,628,657.21
Receivables:					0.00
Federal					0.00
Accounts Receivable					0.00
Due From Other Funds (Note 12)					0.00
Due From Other Agencies (Note 12)					0.00
Consumable Inventories					0.00
Total Current Assets	551,445.93	11,522.40	24,533,136.15	4,706.00	44,777,660.86
Liabilities					
Current Liabilities					
Payables:					
Vouchers Payable	350,466.86				368,309.86
Account Payable					895,159.28
Payroll Payable					42,729.71
Due to Other Funds (Note 12)					0.00
Due to Other Agencies (Note 12)					48,671.49
Unearned Revenues	200,979.07	11,522.40	24,533,136.15	4,706.00	24,750,343.62
Total Current Liabilities	551,445.93	11,522.40	24,533,136.15	4,706.00	26,105,213.96
Fund Balances					
Non Spendable (Inventory)					0.00
Restricted					0.00
Committed					3,955,694.80
Assigned					0.00
Unassigned					14,716,752.10
Total Fund Balance	0.00	0.00	0.00	0.00	18,672,446.90
Total Liabilities and Fund Balances	\$ 551,445.93	\$ 11,522.40	\$ 24,533,136.15	\$ 4,706.00	\$ 44,777,660.86

-UNAUDITED-

EXHIBIT B-1
COMBINING BALANCE SHEET
Special Revenue Funds
For Fiscal Year Ended August 31, 2020

	State Highway Fund (0006)	Texas Department of Motor Vehicles Fund (0010)	Suspense Type Activities Fund (0900)	Total
Assets				
Current Assets:				
Cash on Hand	\$	\$ 37,100.00	\$	\$ 37,100.00
Cash in Bank		20,000.00		20,000.00
Cash in State Treasury		160,693,082.92		160,693,082.92
Legislative Appropriations				0.00
Receivables:				
Federal				0.00
Accounts Receivable	129,814,270.29	3,141,142.33		132,955,412.62
Due From Other Funds (Note 12)				0.00
Due From Other Agencies (Note 12)	22,680.00	40,050.00		62,730.00
Consumable Inventories		54,820.67		54,820.67
Total Current Assets	129,836,950.29	163,986,195.92	0.00	293,823,146.21
Liabilities				
Current Liabilities				
Payables:				
Vouchers Payable		859,380.75		859,380.75
Account Payable		8,359,073.56		8,359,073.56
Payroll Payable		4,900,614.98		4,900,614.98
Due to Other Funds (Note 12)				0.00
Due to Other Agencies (Note 12)				0.00
Total Current Liabilities	0.00	14,119,069.29	0.00	14,119,069.29
Fund Balances				
Non Spendable (Inventory)		54,820.67		54,820.67
Restricted	129,836,950.29	149,812,305.96	0.00	279,649,256.25
Committed				0.00
Assigned				0.00
Unassigned				0.00
Total Fund Balance	129,836,950.29	149,867,126.63	0.00	279,704,076.92
Total Liabilities and Fund Balances	\$ 129,836,950.29	\$ 163,986,195.92	\$ 0.00	\$ 293,823,146.21

-UNAUDITED-

EXHIBIT A-2
COMBINING STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCES
All General and Consolidated Funds
For the Year Ended August 31, 2020

	General Revenue Account (0001)	License Plate Trust Fund Account (0802)	Suspense Type Activities Account (0900)	Deposit Default Type Activities Account (9000)	Returned Items Type Activities Account (9001)	Totals
Revenues						
Legislative Appropriations:						
Original Appropriations	\$ 12,835,851.00	\$	\$	\$		\$ 12,835,851.00
Additional Appropriations	83,452.07					83,452.07
Federal Revenues						0.00
Federal Pass-Through						0.00
State Grant Pass -Through						0.00
Licenses, Fees and Permits		94,093.22	(48,015.90)			46,077.32
Interest & Investment Income		6,503.35				6,503.35
Settlement of Claims						0.00
Sales of Goods and Services						0.00
Other Revenues					(15,914.91)	(15,914.91)
Total Revenues	12,919,303.07	100,596.57	(48,015.90)	0.00	(15,914.91)	12,955,968.83
Expenditures						
Salaries and Wages	365,476.26					365,476.26
Payroll Related Costs	88,631.90					88,631.90
Professional Fees and Services	527,179.64					527,179.64
Travel	6,631.22					6,631.22
Materials and Supplies	362,664.10					362,664.10
Communications and Utilities	1,577.76					1,577.76
Repairs and Maintenance	(297,417.74)					(297,417.74)
Rentals and Leases	6,914.95					6,914.95
Printing and Reproduction	4,594.68					4,594.68
Claims and Judgements						0.00
Federal Pass-Through Expenditures						0.00
State Grant Pass-Through Expenditures	13,673.00					13,673.00
Intergovernmental Payments	12,162,092.31					12,162,092.31
Public Assistance Payments	88,691.72					88,691.72
Other Operating Expenditures	22,619.56					22,619.56
Capital Outlay						0.00
Total Expenditures	13,353,329.36	0.00	0.00	0.00	0.00	13,353,329.36
Excess (Deficit) of Revenues over Expenditures	(434,026.29)	100,596.57	(48,015.90)	0.00	(15,914.91)	(397,360.53)
Other Financing Sources (Uses)						
Operating Transfers In (Note 12)		599,051.23				599,051.23
Operating Transfers Out (Note 12)	(11,951.05)	(655,820.92)				(667,771.97)
Insurance Recoveries						0.00
Sale of Capital Assets	4,267.30					4,267.30
Legislative Financing Sources						0.00
Legislative Financing Uses						0.00
Legislative Transfers In (Note 12)						0.00
Legislative Transfers Out (Note 12)						0.00
Total Other Financing Sources (Uses)	(7,683.75)	(56,769.69)	0.00	0.00	0.00	(64,453.44)
Excess (Deficit) of Revenues and other Sources Over Expenditures and Other Uses	(441,710.04)	43,826.88	(48,015.90)	0.00	(15,914.91)	(461,813.97)
Fund Balance - Beginning	15,153,139.64	3,955,694.80	48,015.90			19,156,850.34
Restatements						0.00
Fund Balance As Restated	15,153,139.64	3,955,694.80	48,015.90	0.00	0.00	19,156,850.34
Appropriations Lapsed	(22,589.47)					(22,589.47)
Fund Balance - Ending	\$ 14,688,840.13	\$ 3,999,521.68	\$ 0.00	\$ 0.00	\$ (15,914.91)	\$ 18,672,446.90

-UNAUDITED-

EXHIBIT B-2
COMBINING STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCES
Special Revenue Funds
For the Year Ended August 31, 2020

	<u>State Highway Fund (0006)</u>	<u>Texas Department of Motor Vehicles Fund (0010)</u>	<u>Suspense Type Activities Account (0900)</u>	<u>Totals</u>
Revenues				
Legislative Appropriations:				
Original Appropriations	\$	\$	\$	\$ 0.00
Additional Appropriations				0.00
Federal Revenues		106,386.71		106,386.71
Federal Pass-Through				0.00
State Grant Pass -Through				0.00
Licenses, Fees and Permits	1,571,462,777.50	153,000,936.30	(227,320.63)	1,724,236,393.17
Interest & Investment Income		2,576,740.52		2,576,740.52
Settlement of Claims				0.00
Sales of Goods and Services		244,260.00		244,260.00
Other Revenues	7,251.65	27,433.56		34,685.21
Total Revenues	1,571,470,029.15	155,955,757.09	(227,320.63)	1,727,198,465.61
Expenditures				
Salaries and Wages		40,780,199.35		40,780,199.35
Payroll Related Costs		15,143,272.69		15,143,272.69
Professional Fees and Services	68,960.09	16,981,639.28		17,050,599.37
Travel		229,878.41		229,878.41
Materials and Supplies		14,658,845.94		14,658,845.94
Communications and Utilities		5,013,709.66		5,013,709.66
Repairs and Maintenance	521,288.56	3,329,920.46		3,851,209.02
Rentals and Leases		1,039,835.98		1,039,835.98
Printing and Reproduction		4,117,148.01		4,117,148.01
Claims and Judgements				0.00
Federal Pass-Through Expenditures				0.00
State Grant Pass-Through Expenditures				0.00
Intergovernmental Payments				0.00
Public Assistance Programs				0.00
Other Operating Expenditures		35,430,282.99		35,430,282.99
Capital Outlay		357,661.84		357,661.84
Total Expenditures	590,248.65	137,082,394.61	0.00	137,672,643.26
Excess (Deficit) of Revenues over Expenditures	1,570,879,780.50	18,873,362.48	(227,320.63)	1,589,525,822.35
Other Financing Sources (Uses)				
Operating Transfers In (Note 12)				0.00
Operating Transfers Out (Note 12)	(1,575,461,468.64)			(1,575,461,468.64)
Sale of Capital Assets		1,422.43		1,422.43
Legislative Financing Sources				0.00
Insurance Recoveries				0.00
Legislative Transfers In (Note 12)				0.00
Legislative Transfers Out (Note 12)				0.00
Total Other Financing Sources (Uses)	(1,575,461,468.64)	1,422.43	0.00	(1,575,460,046.21)
Excess (Deficit) of Revenues and other Sources				
Over Expenditures and Other Uses	(4,581,688.14)	18,874,784.91	(227,320.63)	14,065,776.14
Fund Balance - Beginning	134,418,638.43	130,992,341.72	227,320.63	265,638,300.78
Restatements				0.00
Fund Balance As Restated	134,418,638.43	130,992,341.72	227,320.63	265,638,300.78
Appropriations Lapsed				0.00
Fund Balance - Ending	\$ 129,836,950.29	\$ 149,867,126.63	\$ 0.00	\$ 279,704,076.92

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SCHEDULES

-UNAUDITED-

SCHEDULE 1A
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Fiscal Year Ended August 31, 2020

Federal Grantor/ Pass-Through Grantor/ Program Title	Pass-Through From			
	CFDA Number	Agency Number	State Agency or University Amount	Non-State Entities Amount
U.S. Department of Transportation				
<u>Direct Programs:</u>				
Motor Carrier Safety Assistance High Priority Activities	20.237			
Total			<u>0.00</u>	<u>0.00</u>
TOTAL FEDERAL FINANCIAL ASSISTANCE			<u><u>0.00</u></u>	<u><u>0.00</u></u>

Note 2 - Reconciliation

Per Combined Statement of Revenues, Expenditures and Changes in Fund Balance (Governmental Fund Types)

Exhibit II

Federal Revenues	\$ 106,386.71
Federal Pass-Through Revenues	<u>0.00</u>
Total	<u><u>\$ 106,386.71</u></u>

Texas Department of Motor Vehicles (608)

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Direct Program Amount	Total Pass Through From & Direct Program	Pass-Through To			Expenditure Amount	Total Pass Through To & Expenditures
		Agency Number	State Agency or University Amount	Non-State Entities Amount		
\$ 106,386.71	\$ 106,386.71				\$ 106,386.71	\$ 106,386.71
<u>\$ 106,386.71</u>	<u>\$ 106,386.71</u>		<u>0.00</u>	<u>0.00</u>	<u>\$ 106,386.71</u>	<u>\$ 106,386.71</u>
<u><u>\$ 106,386.71</u></u>	<u><u>\$ 106,386.71</u></u>		<u><u>0.00</u></u>	<u><u>0.00</u></u>	<u><u>\$ 106,386.71</u></u>	<u><u>\$ 106,386.71</u></u>

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SCHEDULE 1B
SCHEDULE OF STATE GRANT PASS-THROUGHS FROM/TO STATE AGENCIES
For the Fiscal Year Ended August 31, 2020

Pass-Through Grantor/ Program Title	Pass-Through From			Pass-Through To			
	Grant ID	Agency Number	State Agency or University Amount	Total Pass-Through From	Agency Number	State Agency or University Amount	Total Pass-Through To
Motor Vehicle Crime Prevention Authority (MVCPA)							
<u>Programs:</u>							
Texas A&M University - Bait Car Research	608.0004			\$0.00	711	\$ 13,673.00	\$ 13,673.00
Total				<u>0.00</u>		<u>\$ 13,673.00</u>	<u>\$ 13,673.00</u>
TOTAL PASS-THROUGH TO OTHER AGENCIES				<u>0.00</u>		<u>\$ 13,673.00</u>	<u>\$ 13,673.00</u>

Note 2 - Reconciliation

Per Combined Statement of Revenues, Expenditures and Changes in Fund Balance (Governmental Fund Types)

Exhibit II

State Grant Pass-Through Expenditures

Total

\$ 13,673.00
\$ 13,673.00

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Texas Department *of* Motor Vehicles
4000 Jackson Avenue
Austin, Texas 78731

Annual Report of Nonfinancial Data

Fiscal Year Ended August 31, 2020



Annual Report of Nonfinancial Data

Fiscal Year Ended August 31, 2020



Texas Department *of* Motor Vehicles

Prepared by
Finance & Administrative Services Division

December 31, 2020

Texas Department of Motor Vehicles Board

Guillermo "Memo" Treviño, Chair

Charles Bacarisse
Stacey Gillman
Brett Graham
Tammy McRae

John M. Prewitt
Paul R. Scott
Shelley Washburn
Manny Ramirez

Whitney H. Brewster
Executive Director

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December 31, 2020

Honorable Greg Abbott, Governor
Ms. Lisa R. Collier, CPA, CFE, CIDA, First Assistant State Auditor
Mr. Jerry McGinty, Director, Legislative Budget Board

Ladies and Gentlemen:

We are pleased to submit the Texas Department of Motor Vehicle's *Annual Report of Nonfinancial Data* for the year ended August 31, 2020, in compliance with the TEX. GOV'T CODE ANN. §2101.0115 and in accordance with the instructions for completing the *Annual Report of Nonfinancial Data*.

The accompanying report has not been audited and is considered to be independent of the agency's *Annual Financial Report*.

If you have any questions, please contact Mr. Sergio Rey, Assistant Chief Financial Officer, at (512) 465-1216, or Ms. Linda M. Flores, CPA, Chief Financial Officer, at (512) 465-4125.

Sincerely,

A handwritten signature in blue ink that reads "Whitney H. Brewster".

Whitney H. Brewster
Executive Director

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-UNAUDITED-

Appropriation Item Transfers*

For the Fiscal Year Ended August 31, 2020

ITEM OF APPROPRIATION	<u>Transfers-In</u>	<u>Transfers-Out</u>	<u>Net Transfers</u>
C. Goal: Indirect Administration			
<i>Strategies:</i>			
C.1.1 13009 Central Administration	\$ <u>143,147.00</u>	\$ <u>-</u>	\$ <u>143,147.00</u>
C.1.2 13010 Information Resources	<u>-</u>	<u>(143,147.00)</u>	<u>(143,147.00)</u>
Total, Goal C: Indirect Administration	<u>143,147.00</u>	<u>(143,147.00)</u>	<u>-</u>
NET APPROPRIATION ITEM TRANSFERS	\$ <u>143,147.00</u>	\$ <u>(143,147.00)</u>	\$ <u>-</u>

* This schedule does not include transfers for Benefit Replacement Pay, Capital, SWCAP, Fringe, or Rider Reductions.

Texas Department of Motor Vehicles (608)

-UNAUDITED-

STATE AGENCY PROGRESS REPORT

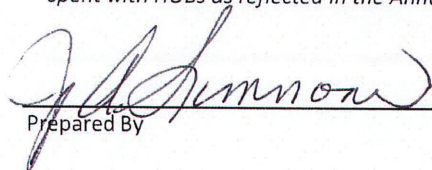
Source: Texas Government Code, Title 10, Subtitle D, Section 2161.124
For the Fiscal Year Ended August 31, 2020

Agency Name: Texas Department of Motor Vehicles Agency #: 608 Report for Fiscal: 2020

HUB Report Procurement Categories	Fiscal 2019		Fiscal 2020		Fiscal 2021
	Agency-Specific HUB Goal*	% of Dollars Spent w/HUBs**	Agency-Specific HUB Goal*	% of Dollars Spent w/HUBs**	Agency-Specific HUB Goal*
Heavy construction other than building contracts		100.00%			
Building construction, including general contractors and operative builders contracts					
Special trade construction contracts		64.18%	32.00%	35.88%	32.00%
Professional services contracts					
Other services contracts	5.00%	11.42%	5.00%	20.08%	10.00%
Commodities contracts	23.00%	30.60%	23.00%	43.59%	23.00%

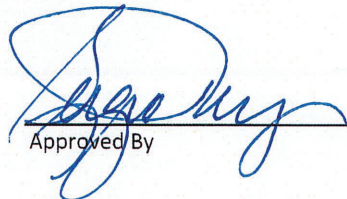
*For each of the procurement categories listed, enter your Agency-Specific HUB Goals.

**For each of the procurement categories listed, enter the percentage of dollars the agency spent with HUBs as reflected in the Annual HUB Reports.


Prepared By

Joy Simmons, Assistant HUB Coordinator
Printed Name

512-465-4177
Phone Number


Approved By

Sergio Rey, Assistant Chief Financial Officer,
CTCD/CTCM
Printed Name

512-465-1216
Phone Number

(Rev. 11/18)

-UNAUDITED-

Indirect Cost Schedule

For the Fiscal Year Ended August 31, 2020

A. Payroll-related Costs

(Exhibit II, Annual Financial Report)

FICA Employer Matching Contribution	\$ 3,005,432.25	
Group Health Insurance	8,113,762.31	
Retirement	3,998,175.67	
Unemployment	<u>114,534.36</u>	
Total Payroll-related Costs		\$ <u>15,231,904.59</u>

Workers' Compensation	\$ 87,637.99	
Benefit Replacement Pay (BRP)	<u>54,121.15</u>	
Total Workers' Compensation and BRP		\$ <u>141,759.14</u>

B. Indirect Costs

(Not reported in Agency's Annual Financial Report)

Bond Debt Service Payments		
Texas Facilities Commission (TFC)	\$ -	
Texas Public Finance Authority (TPFA)	-	
Other (if applicable)	<u>-</u>	
Total Indirect Costs		\$ <u>-</u>

C. Indirect Costs - Statewide Full Cost Allocation Plan (SWCAP)

Comptroller of Public Accounts (CPA)	\$ 646,922.00	
Department of Public Safety (DPS)	1,170.00	
Texas Facilities Commission (TFC)	6,675.00	
Office of the Governor (OOG), Budget & Planning	<u>2,196.00</u>	
Total Indirect Costs - Statewide Full Cost Allocation Plan		\$ <u>656,963.00</u>

TOTAL INDIRECT COSTS		\$ <u><u>16,030,626.73</u></u>
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-UNAUDITED-

Schedule of Professional/Consulting Fees & Legal Service Fees

For the Fiscal Year Ended August 31, 2020

Professional/Consulting Fees:

Name	Service Provided	Amount
Anchor Computer Inc	Data Processing Services	13,598.23
Apex Systems Inc	Information Technology Services	761,780.30
Appeon Inc	Information Technology Services	995.00
Association of Certified Fraud Examiners	Educational/Training Services	1,225.40
Bansar Technologies Inc	Information Technology Services	275,404.37
Black Book National Auto Research	Information Technology Services	9,000.00
Capitol Systems Inc	Information Technology Services	182,305.00
Carahsoft Technology Corporation	Information Technology Services	1,310,211.02
Carolyn Conn	Educational/Training Services	2,000.00
Catapult Systems Inc	Consultant Services - Computer	10,515.51
Complete Book & Media Supply Inc	Educational/Training Services	2,396.00
DatamanUSA LLC	Information Technology Services	305,025.00
EDX Inc	Educational/Training Services	1,000.00
iLead Consulting & Training	Educational/Training Services	17,280.00
Insight Public Sector Inc	Consultant Services - Computer	159,660.00
Insight Public Sector Inc	Information Technology Services	239,490.00
Knowbility Inc	Educational/Training Services	362.81
Neos Consulting Group LLC	Information Technology Services	42,740.88
New Horizons CLC of Austin	Educational/Training Services	33,681.64
NF Consulting Services	Information Technology Services	1,316,678.72
Nipun Systems Inc	Information Technology Services	408,540.93
Occupational Health Centers of the SW, P.A.	Medical Services	130.50
PHCC Association of Texas	Educational/Training Services	85.00
Presidio Networked Solutions Group LLC	Consultant Services - Computer	9,000.00
Red River Consulting Services LLC	Information Technology Services	23,000.00
Safe2Drive	Educational/Training Services	633.60
SHI Government Solutions Inc	Educational/Training Services	8,000.00
SHI Government Solutions Inc	Information Technology Services	275,125.24
Sistema Technologies Inc	Information Technology Services	181,305.00
SmartyStreets LLC	Information Technology Services	10,000.00
Solid Border Inc	Information Technology Services	24,000.00
Southwest Research Institute	Consultant Services - Other	321,830.38
Southwest Research Institute	Information Technology Services	313,042.96
State Bar of Texas	Educational/Training Services	690.00
Surgent Holding Corporation	Educational/Training Services	558.40
TEKsystems Inc	Information Technology Services	248,116.32
Texas Commission on Law Enforcement	Educational/Training Services	195.00

-UNAUDITED-

Schedule of Professional/Consulting Fees & Legal Service Fees (Continued)

For the Fiscal Year Ended August 31, 2020

Professional/Consulting Fees:

<u>Name</u>	<u>Service Provided</u>	<u>Amount</u>
Texas Credit Card Procurement Program	Educational/Training Services	249.00
Texas Department of Information Resources	Computer Services - Statewide Tech	10,509,272.62
Texas Department of Information Resources	Data Processing Services	34,380.00
Texas State Auditor's Office	Educational/Training Services	399.00
The Institute of Internal Auditors Inc	Educational/Training Services	175.00
University of Texas at Austin	Educational/Training Services	1,350.00
Workers Assistance Program Inc	Professional Services - Other	13,708.20
WorkQuest	Information Technology Services	341,043.60
Yellowbook-CPE LLC	Educational/Training Services	1,585.00
Total, Professional/Consulting Fees:		\$ 17,411,765.63

Legal Service Fees:

<u>Name</u>	<u>Service Provided</u>	<u>Amount</u>
Office of the Attorney General	Legal Services	1,575.88
State Office of Administrative Hearings (SOAH)	Legal Services - Approved by SOAH	164,437.50
Total, Legal Service Fees:		\$ 166,013.38

TOTAL, PROFESSIONAL/CONSULTING FEES & LEGAL SERVICE FEES **\$ 17,577,779.01**

-UNAUDITED-

Schedule of Space Occupied

For the Fiscal Year Ended August 31, 2020

The Texas Department of Motor Vehicles (TxDMV) is headquartered in Austin, Texas and maintains 16 regional offices across the state to facilitate delivery of services to the motoring public. Effective November 1, 2009, the Texas Department of Transportation (TxDOT) allocated office space to the TxDMV through a Memorandum of Understanding (MOU) as required by House Bill 3097, 81st Legislature, Regular Session.

Location	Address	Lessor	Lease No.
State Owned Buildings			
Camp Hubbard (CH) Complex	4000 Jackson Avenue, Austin, Texas		
Building, CH 1			
Building, CH 2 (Fiesta Room)			
Building, CH 5			
Building, CH 6			
Regional Offices			
Abilene	4210 North Clack Street, Abilene, Texas		
Amarillo	5715 Canyon Drive, Building H, Amarillo, Texas		
Austin	1001 East Parmer Lane, Suite A, Austin, Texas		
Beaumont	8550 Eastex Freeway, Beaumont, Texas		
Huntsville Operations	810 FM 2821, Huntsville, Texas	TDCJ - Wynne Unit	
Longview	4549 West Loop 281, Longview, Texas		
Lubbock	135 Slaton Road, Lubbock, Texas		
Midland/Odessa	3901 East Highway 80, Odessa, Texas		
Pharr	600 West Expressway 83, Pharr, Texas		
Wichita Falls	1601-A Southwest Parkway, Wichita Falls, Texas		
Leased Space			
Centimeter Warehouse Facility	2000 Centimeter Circle, Austin, Texas	RUT-3-4-7, LTD	MOU with TxDOT
CPA Warehouse	1811 Airport Boulevard, Austin, Texas	4015 Limited Partnership	6728
Regional Offices			
Corpus Christi	602 N. Staples Street, Corpus Christi, Texas	Corpus Christi Regional Transp. Authority	303-7-20538
Dallas	1925 E. Beltline Road, Carrollton, Texas	Purple Tree LLC	7959
El Paso	1227 Lee Trevino Drive, Suite 100, El Paso, Texas	Burnham Properties Ltd.	10263
Fort Worth	2425 Gravel Drive, Fort Worth, Texas	RiverBend Complex LLC	10462
Houston	2110 East Governors Circle, Houston, Texas	Ragsdale-Brookwood Joint Venture	20399
San Antonio	15150 Nacogdoches Road, San Antonio, Texas	Acharya Investments LLC	20537
Waco	2203 Austin Avenue, Waco, Texas	Tony Martin, Trustee	8365

-UNAUDITED-

Schedule of Space Occupied (Continued)

For the Fiscal Year Ended August 31, 2020

Location	Type	Usable Square Footage	FTEs	Cost Per			Contract Period
				Month	Sq.Ft. Per Mo.	Year	
State Owned Buildings							
Camp Hubbard (CH) Complex							
Building, CH 1	Office	71,684	317				
Building, CH 2 (Fiesta Room)	Office	1,102	-				
Building, CH 5	Office	33,134	107				
Building, CH 6	Office	21,216	109				
Regional Offices							
Abilene	Office	1,900	6				
Amarillo	Office	2,538	5				
Austin	Office	3,131	10				
Beaumont	Office	3,000	6				
Huntsville Operations	Office	260	2				
Longview	Office	3,120	8				
Lubbock	Office	2,579	7				
Midland/Odessa	Office	3,618	6				
Pharr	Office	3,500	13				
Wichita Falls	Office	2,665	15				
Total, State Owned Buildings		153,447	611.0				
Leased Space							
Centimeter Warehouse Facility	Warehouse	575	-	-	-	-	09/01/19 - 04/30/23
CPA Warehouse	Warehouse	3,000	-	1,694.74	0.5649	20,336.88	05/01/20 - 04/30/23
Regional Offices							
Corpus Christi	Office	3,141	7	3,777.04	1.2025	45,324.48	04/01/17 - 03/31/27
Dallas	Office	7,865	27.5	10,544.49	1.3407	126,533.88	04/01/20 - 03/31/25
El Paso	Office	3,771	12	4,713.75	1.2500	56,565.00	11/01/17 - 10/31/22
Fort Worth	Office	5,685	26	6,468.75	1.1379	77,625.00	08/01/13 - 10/31/20*
Houston	Office	11,554	39.5	23,723.19	2.0532	284,678.28	11/01/18 - 09/30/24
San Antonio	Office	3,916	16.5	6,818.73	1.7412	81,824.76	09/01/17 - 08/31/27
Waco	Office	2,307	6	3,185.53	1.3808	38,226.36	09/01/15 - 08/31/20**
Total, Leased Space		41,814	134.5	\$ 60,926.22		\$ 731,114.64	
GRAND TOTAL		195,261	745.5	\$ 60,926.22		\$ 731,114.64	

* Fort Worth lease extended at \$7,816.88 per month for 5,685 square feet of occupied space. Contract term is 11/01/20 - 10/31/25.

** Waco lease extended at \$3,780.00 per month for 2,307 square feet of occupied space. Contract term is 09/01/20 - 08/31/25.

-UNAUDITED-

Schedule of Vehicles Purchased

For the Fiscal Year Ended August 31, 2020

<u>Make</u>	<u>Model</u>	<u>Year</u>	<u>Quantity</u>	<u>Purchase Price</u>	<u>Type of Use</u>	<u>Fuel Efficiency In Average Miles per Gallon</u>
Chevrolet	Traverse	2020	2	\$ 49,778.00	Investigations, Audits, Freight and Passenger Transport	22.5
Ford	Escape	2020	2	\$ 39,420.00	Investigations, Audits, Freight and Passenger Transport	30
TOTALS			<u>4</u>	<u>\$ 89,198.00</u>		

-UNAUDITED-

Alternative Fuel Program Status

For the Fiscal Year Ended August 31, 2020

Alternative Fuel Vehicles Received Into Inventory by Fiscal Year

The totals in the chart below represent the number of alternative fuel vehicles received into inventory between September 1 and August 31 of each fiscal year.

Fiscal Year	Type Of Fuel Capability						Total
	Natural Gas (CNG)	Propane (LPG)	Ethanol 85% (E-85)	Gas/Electric Hybrid	Electricity	Biodiesel 20% (B-20)	
2020							0
2019			18		1	1	20
2018			21				21
2017							0
2016			3				3
2015							0
2014			8				8
2013			8				8
2012			6				6
2011							0
2010		6	1	11			18
Totals	0	6	65	11	1	1	84

Texas Department of Motor Vehicles (TxDMV) was created by House Bill 3097, 81st Legislature, Regular Session. The vehicles listed for FY 2010 were part of the transfer from Texas Department of Transportation (TxDOT) when the TxDMV began operations. Twenty-four purchases between FY 2012 and FY 2016 were surplus vehicles bought from the Texas Department of Public Safety. All other new vehicles have been procured via the Comptroller of Public Accounts Term Contract.

Fuel Usage for the Fiscal Year Ended August 31, 2020

Fuel Type	Gallons Used
Unleaded Gasoline	12,237.59
Unleaded for Gas Hybrid	939.51
Diesel	68.56
Ethanol 85% (E-85)	3,049.10
Electricity	71.17
Biodiesel 20% (B-20)	319.36
	Gallons of Gasoline Equivalent (GGe)
Total	16,685.29

-UNAUDITED-

Schedule of Itemized Purchases

For the Fiscal Year Ended August 31, 2020

Vendor Name	Amount	Product Purchased	Justification
<i>Promiles Software Development Corporation</i>	\$ 603,180.00	<i>Programming and Support Services</i> Software/Data Management and Support Services for TxPROS software application	<i>Competing Products Not Satisfactory</i> ProMiles Software Development Corp wrote the source code for the software application and is the only Vendor who can provide support services.
<i>Explore Information Service LLC</i>	250,800.00	<i>Software Maintenance and Support</i> Texas International Registration Plan (TxIRP) software for apportionately registering commercial vehicles operating interstate.	<i>Competing Products Not Satisfactory</i> Explore Information Services wrote the source code for the system and currently supports it as well. As such, they are the only vendor that can supply the services required.
TOTAL PURCHASES	\$ <u>853,980.00</u>		

Published and distributed
by the
Texas Department *of* Motor Vehicles
4000 Jackson Avenue
Austin, Texas 78731

To: Texas Department of Motor Vehicles Board
From: Linda M. Flores, CPA, Chief Financial Officer, Finance & Administrative Services Division Director
Agenda Item: 6.D
Subject: FY 2021 Second Quarter Financial Report (BRIEFING ONLY) – Linda M. Flores, Sergio Rey and Brian Kline

PURPOSE

The TxDMV Board is briefed quarterly on revenue collections and department expenditures. This report contains sections detailing year-to-date status as well as actual versus projections of revenues and expenditures. The year-to-date report includes a section dedicated to the TxDMV Fund and a section with information on Motor Vehicle Crime Prevention Authority (MVCPA) fee collections that support the MVCPA program. An additional section provides information about the impact of costs related to the TxDMV COVID-19 response.

Attached is the Fiscal Year (FY) 2021 financial summary report for the period ending February 28, 2021.

EXECUTIVE SUMMARY

The TxDMV is self-sufficient and supports its expenditures through revenues deposited to TxDMV Fund 0010, except for MVCPA. MVCPA is fully funded through fees deposited to the credit of the General Revenue Fund.

Through the second quarter of FY 2021, the key highlights of the department's revenues and expenditures are:

- The department's total revenue deposits (all funds) were \$859.5 million, a 4.6% decrease compared to the second quarter of FY 2020.
- TxDMV Fund 0010 collections totaled \$69.4 million, a 15.8% decrease compared to second-quarter FY 2020.
- All-fund (General Revenue Fund and TxDMV Fund) obligations (including expenditures and encumbrances) totaled \$115.5 million. This includes expenditures associated with COVID-19 in the amount of \$1.5 million.
- The department collected sufficient revenue through the second quarter of FY 2021 to support its expenditures during the same period.
- The ending **TxDMV Fund 0010** balance at February 28, 2021, was \$154.9 million. Inclusion of encumbrances adjusts the **net balance to \$115.9 million**.

FINANCIAL SUMMARY

TOTAL REVENUES (All Funds)

TxDMV revenue deposits totaled \$859.5 million through the second quarter of FY 2021. This amount comprises:

- \$ 737.72 million for the State Highway Fund (Fund 0006);
- \$ 52.40 million for the General Revenue Fund (Fund 0001); and
- \$ 69.38 million for the TxDMV Fund (Fund 0010).

TxDMV FUND 0010 REVENUES

FY 2021 collections for TxDMV Fund 0010 totaled \$69,382,929. This amount comprises revenues from titles, registered vehicles, license plates, oversize/overweight permits, motor vehicle business licenses, processing and handling fees, and miscellaneous fees.

TxDMV Fund 0010 revenues decreased by 15.8% compared to FY 2020. The decrease in FY 2021 revenues compared to FY 2020 is attributable to the fee waivers and decline in economic activity related to COVID-19.

EXPENDITURES/OBLIGATIONS

Obligations through February 28, 2021, totaled \$115.5 million (\$63.3 million in expenditures and \$52.2 million in encumbrances) for all funds. Significant expenditure categories continue to include salaries, contract services for plate production, printing costs for Vehicle Titles and Registration Division forms, postage, and Data Center Services costs. Included in expenditures is \$2.9 million for contract payments to MyPlates, the specialty-plates vendor. Contract payments to MyPlates are contingent upon revenues collected.

To date the department has incurred \$1.5 million in FY 2021 obligations related to the COVID-19 response. The majority of the cost is related to staff time responding to operational issues, i.e., planning and implementing new policies/procedures, modifying facilities for customer service and disinfecting services.

The FY 2021 budget through February 28, 2021, includes \$10.0 million in unspent balances of FY 2020 appropriations. The primary drivers of the remaining balance include savings from vacant positions, less than anticipated license plate production expenses, and agency reserves. The authority to carry forward the unspent funds from FY 2020 was approved by the Legislature during the 86th regular legislative session.

The FY 2021 capital project budget obligations through February 28, 2021, include expenditures of approximately \$8.5 million and encumbrances of approximately \$9.7 million, for a total obligated amount of \$18.7 million. This includes \$10.9 million in obligations for Data Center Services; \$5.5 million for Automation; and \$920,000 for County Technology. The remaining capital obligations are for agency support for vehicle replacement, technology, and facilities. The FY 2021 capital project budget includes \$17.7 million in funds carried forward from FY 2020; the majority of the carry forward is for the Automation capital budget.

The FY 2021 budget includes continued funding for exceptional items that were approved by the Legislature during the 86th regular legislative session. The exceptional items approved include nine new full-time equivalents (FTEs) and associated funding for the Consumer Relations Division, and twelve new FTEs for the Information Technology Services Division. The Legislature also approved a contingency rider for the implementation of a digital license plate program that included two FTEs for the Vehicle Titles and Registration Division. A contract was awarded in October 2020 to a third-party vendor to provide digital license plate services and public go-live is scheduled to commence in March 2021.

MYPLATES

The current (third) specialty-plates marketing contract executed with MyPlates runs from November 19, 2019, to December 31, 2025, with an option to renew the contract for an additional six-year term. The contract includes a minimum guarantee of \$25 million into the General Revenue Fund from the sale of personalized and non-personalized new vendor specialty plates, as well as 5% of the revenue from the renewal of these plates, during the term of the contract.

General Revenue Fund 0001 deposits associated with the MyPlates contract from November 19, 2019, to February 28, 2021, totaled \$21.0 million. Of the \$21.0 million, \$9.6 million counts toward the \$25 million contract guarantee.

SUMMARY OF THE CUMULATIVE COVID-19 IMPACTS THROUGH THE SECOND QUARTER of FY 2021

It has been one year since COVID-19 has changed the way the Texas Department of Motor Vehicles has provided business to the customers of the state of Texas. Governors proclamations, State economy, Unemployment numbers going up, and February weather are just a few of the events that have taken place that have affected our numbers this past year. Below is a summary of the impacts that have happened through the second quarter of FY 2021.

REVENUE

- The cumulative impact on revenues since the beginning of the COVID-19 event is a loss of \$37.2 million specifically due to fee waivers for delinquent title transfer penalties and certain temporary permits (along with the associated processing and handling fees on the permits). The waiver period will end on April 14, 2021.
- The cumulative impact on revenues since the beginning of the COVID-19 event is an additional loss of \$283.9 million due to a general decline in economic activity during the period.

BUDGET

- TxDMV began providing resources in March 2020 in response to the COVID-19 pandemic. Response activity has continued into FY 2021.
- Total expenses for the prior year FY 2020 related to the COVID-19 response totaled \$1.7 million. Expenses were primarily for staff time dedicated to the response, facility maintenance improvements and cleaning, and the acquisition of personal protective equipment for employees and customers.
- Total FY 2021 obligations for COVID-19 response, from September 2020 through February 2021 was \$1,508,163. The majority of the obligated amount was due to specific facility cleaning contracts that were established for providing COVID-19 cleaning services. The contracts provide cleaning coverage through August 2021. Other costs include employee time devoted specifically to COVID-19 response and temporary contract workers brought in to the Consumer Relations Division to assist with workload.
- The total projected cost impact in FY 2021 for COVID-19 response is estimated at \$2.2 million. The total cost estimate also assumes COVID-19 facility cleaning services will continue through the end of the fiscal year and staff time devoted to the response will continue through June 2021.
- The overall cost of the pandemic including \$1.7 million from FY 2020 and \$2.2 million estimated for FY 21 is a cumulative cost impact of \$3.9 million.



Texas Department of Motor Vehicles

HELPING TEXANS GO. HELPING TEXAS GROW.



2nd Quarter Financial Report
ending February 28, 2021
Fiscal Year 2021



Texas Department *of* Motor Vehicles

HELPING TEXANS GO. HELPING TEXAS GROW.

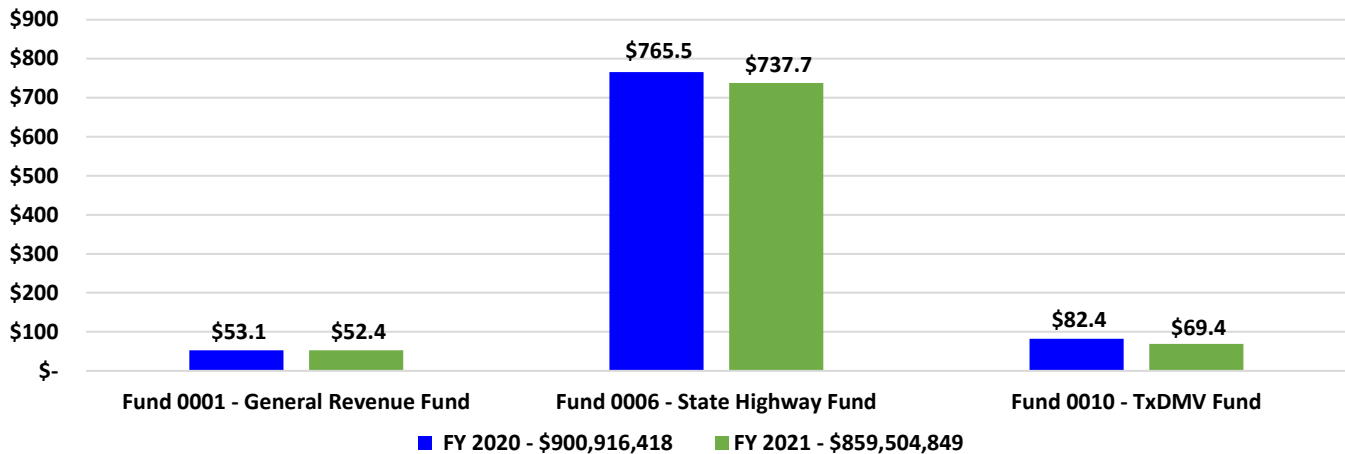
Actual Revenue (All Funds)

September through February FY 2021

Overall Revenue Collections

FY 2020 and FY 2021 Year-over-Year Revenue by Fund

(in millions)



The Texas Department of Motor Vehicles (TxDMV) collected \$859.5 million through the second quarter of FY 2021, which was more than the forecasted amount of \$851.5 million. This was 0.9% more than the projected FY 2021 total, and 4.6% below FY 2020 collections. Through the second quarter, the state experienced a slow but steady growth pattern in almost all sectors with an increase expected in registration and processing and handling fee revenue in the third and fourth quarters as the deferral period draws to a close. Oversize/overweight revenue continues to lag behind FY 2020, but revenue is expected to trend higher later in the current fiscal year. COVID-19 continues to have an effect on the state's economy, including reduced auto sales (which saw an unusual drop due to the February statewide weather conditions) and downward impacts to the oil-and-gas sector as a result of low oil prices.

Revenue collected for all three funds totaled \$859,504,849 through the second quarter of FY 2021. This was a decrease of 4.6% from FY 2020. The amount of revenue collected for each fund in FY 2021 consisted of: Fund 0001, General Revenue Fund, \$52,401,047 (1.2% decrease from FY 2020); Fund 0006, State Highway Fund, \$737,720,873 (3.6% decrease from FY 2020); and Fund 0010, TxDMV Fund, \$69,382,929 (15.8% decrease from FY 2020). These fees include: Motor Vehicle Certificates of Title, Motor Vehicle Registration, Motor Carrier Oversize/Overweight, Motor Carrier Credentialing, Motor Vehicle Business Licenses, Processing and Handling Fee, and miscellaneous revenues.

TxDMV revenue deposits through the second quarter of FY 2021 in each of the three funds did fall short of FY 2020 collections.

FY 2021 versus FY 2020 Year-to-Date Comparison

Year over Year

Revenue Category	Year over Year		% Difference	
	FY 2020 Actual	FY 2021 Actual		
Motor Vehicle Certificates of Title	\$ 42,321,032	\$ 32,812,875	-22.5%	↓
Motor Vehicle Registration	727,512,029	716,173,765	-1.6%	↓
Motor Carrier - Oversize/Overweight	92,670,557	72,550,631	-21.7%	↓
Motor Carrier Credentialing	1,610,901	4,333,173	169.0%	↑
Motor Vehicle Business Licenses	3,849,068	4,014,882	4.3%	↑
Miscellaneous Revenue	6,539,277	5,415,667	-17.2%	↓
Processing and Handling Fee	26,413,553	24,203,854	-8.4%	↓
Total	\$ 900,916,418	\$ 859,504,849	-4.6%	↓

September through February FY 2021 Actuals vs Projections

FY 2021 Actuals versus Projections

Revenue Category	FY 2021 Projections	FY 2021 Actual	% Difference	
Motor Vehicle Certificates of Title	\$ 35,473,146	\$ 32,812,875	-7.5%	↓
Motor Vehicle Registration	700,961,924	716,173,765	2.2%	↑
Motor Carrier - Oversize/Overweight	76,144,162	72,550,631	-4.7%	↓
Motor Carrier Credentialing	4,207,356	4,333,173	3.0%	↑
Motor Vehicle Business Licenses	3,746,697	4,014,882	7.2%	↑
Miscellaneous Revenue	5,591,000	5,415,667	-3.1%	↓
Processing and Handling Fee	25,356,362	24,203,854	-4.5%	↓
Total	\$ 851,480,648	\$ 859,504,849	0.9%	↑

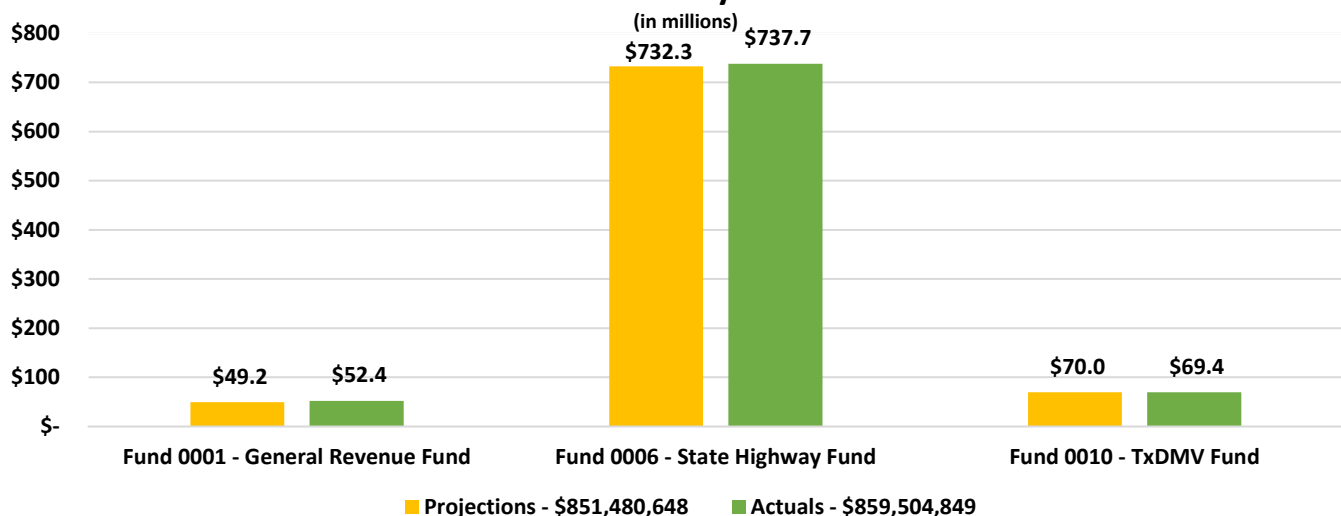
TxDMV collections in the last few months of FY 2020 reflected a pickup in most revenue streams from the lows of April and early May of 2020. This included title fees and motor vehicle business license fees, along with many customers proceeding with renewing registration of their vehicles even with the allowable deferral. Collections are expected to continue rebounding as we progress through FY 2021, including the effect of the fee-waiver and deferral period closing in mid-April. FY 2021 projections shown above were established for board-reporting purposes in the latter part of FY 2020, and include consideration of COVID-19 effects on revenue streams.

Revenues for most categories saw a decline in February due to the week of severe weather in which much less business was performed during that week statewide. However, customer activity is expected to pick up in the third and fourth quarters.

Miscellaneous revenue continues to see a decrease from FY 2020 due to the declining performance of interest rates paid on the TxDMV Fund. These rates have decreased on average from 2.17% in FY 2020 to 0.55% in FY 2021 during the same time period representing a 75% decline in rates.

FY 2021 Actuals vs Projections

Revenue by Fund





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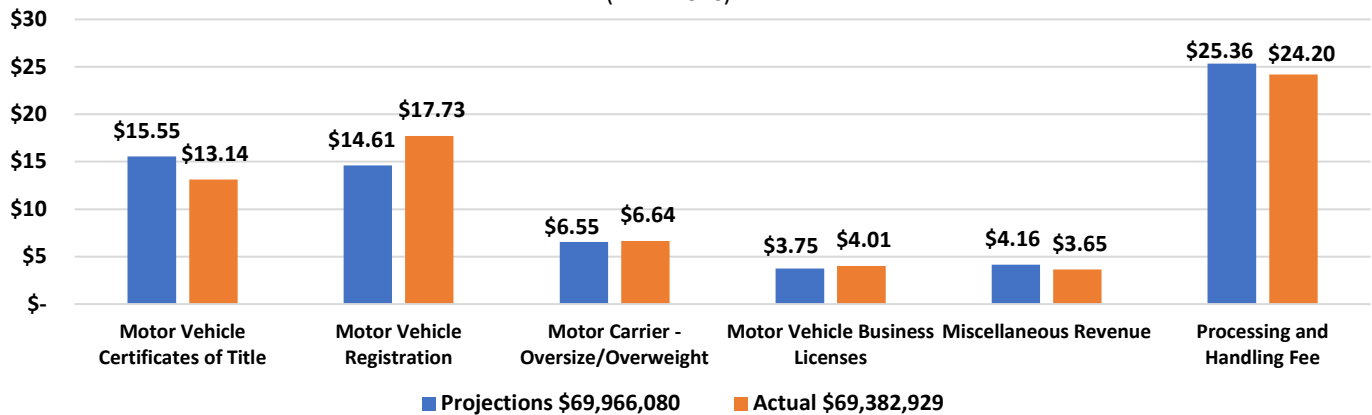
TxDMV Fund 0010 Financial Status Highlights

September through February FY 2021

TxDMV Fund 0010 Highlights

Actuals vs Projections

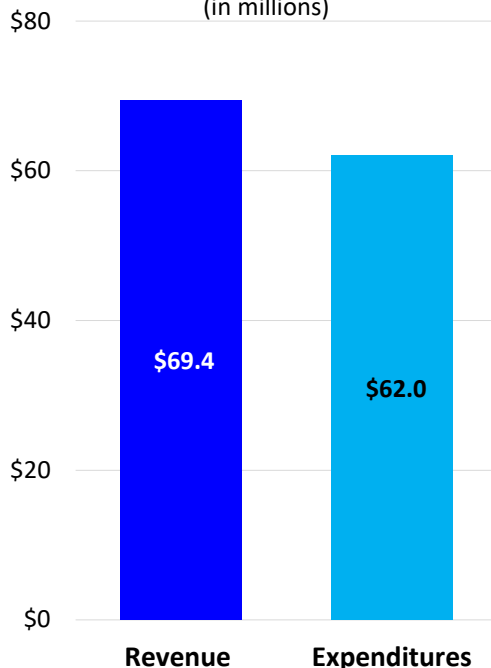
(in millions)



- Overall, TxDMV Fund (0010) revenues were 0.8% below projections through the second quarter of FY 2021. Registration revenue was 21.4% over projections, followed by motor vehicle business licenses at 7.2% over. Miscellaneous revenue was 12.1% under, mostly attributed to lower-than-expected interest rates paid on the TxDMV Fund balance.
- TxDMV Fund revenue collections totaled \$69.4 million, which was 15.8% (\$13.0 million) lower than collections during the same time period of FY 2020. This represented: a 37.3% decrease in title revenue (mostly due to the waiver of delinquent title transfer penalties); a 0.4% decrease in registration revenue; a 19.2% decrease in oversize/overweight revenue; a 4.3% increase in motor vehicle business license revenue; a 29.4% decrease in miscellaneous revenue; and an 8.4% decrease in processing and handling fee revenue.
- TxDMV Fund deposits were below projections by 0.8% (\$583,151) through the second quarter of FY 2021 and currently is expected to meet FY 2021 projections.

FY 2021 Activity-to-date

(in millions)



TxDMV Fund 0010 Balance

	Year-to-date
Beginning Fund Balance	\$ 147,503,099
Fund 0010 Revenue	
Motor Vehicle Certificates of Title	\$ 13,142,455
Motor Vehicle Registration	\$ 17,729,629
Motor Carrier - Oversize/Overweight	\$ 6,638,185
Motor Vehicle Business Licenses	\$ 4,014,882
Miscellaneous Revenue	\$ 3,653,923
Processing and Handling Fee	\$ 24,203,854
Total Revenue	\$ 69,382,929
Fund 0010 Expenditures	
TxDMV Operational Expenditures	\$ 55,652,680
Fringe Benefits	\$ 6,360,558
Total Operational Expenditures	\$ 62,013,238
Ending Fund Balance, Feb 28, 2021	\$ 154,872,790
Adjustment for Encumbrances	\$ 39,013,357
Adjusted Net Cash Balance	\$ 115,859,433



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Motor Vehicle Crime
Prevention Authority

September through February FY 2021

Motor Vehicle Crime Prevention Authority

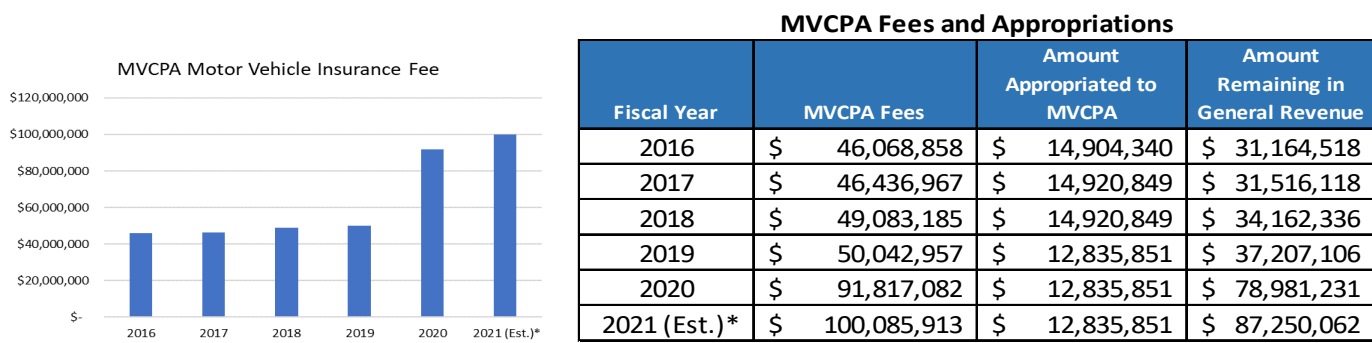
The Motor Vehicle Crime Prevention Authority (MVCPA) has fostered a statewide cooperative network of law-enforcement groups, prosecutors, insurance industry representatives, local tax assessor-collectors, and concerned citizens to combat vehicle theft and burglary through enforcement, prevention, public information, and education initiatives. In addition to providing guidance and oversight, MVCPA awards financial grants to agencies, organizations, and concerned parties in an effort to raise public awareness of vehicle theft and burglary and implement education and prevention initiatives.

The predecessor of the Motor Vehicle Crime Prevention Authority (MVCPA) was established by the 72nd Texas Legislature in 1991 as the Automobile Theft Prevention Authority (ATPA). It was one of the nation’s first statewide efforts to reduce auto theft. The 80th Legislature expanded the ATPA mission to include combating motor vehicle burglary and changed the name to the Automobile Burglary and Theft Prevention Authority. The 86th Legislature changed the name to the Motor Vehicle Crime Prevention Authority and added fraud-related motor vehicle crime to its mission. To better align the operation and improve coordination with the Texas Department of Motor Vehicles (TxDMV), the enabling statute for the MVCPA was codified in the Texas Transportation Code. Under the recodification the MVCPA is required to:

- Collect an annual \$4 fee for every motor vehicle insured in Texas.
- Issue grants to law-enforcement agencies and other statutorily designated groups to combat motor vehicle crime.
- Develop, collect, and monitor performance data on arrests, recovery of vehicles, and cases cleared, as well as other performance measures for motor vehicle crime.
- Report annually, to the Texas Legislature, fiscal and program data.
- Develop a biennial statewide Plan of Operation to combat motor vehicle crime.
- Examine and make determinations for refunds to insurers that overpay the \$4 per vehicle fee.

House Bill (HB) 2048, passed during the 86th Legislature, increased the fee that motor vehicle insurance companies pay per motor vehicle year from \$2.00 to \$4.00. HB 2048 also changed the allocation of the fee revenue to MVCPA from 50% of the \$2.00 fee to 20% of the \$4.00 fee.

The following charts illustrate the six-year trend in the MVPCA motor vehicle insurance fee collections and a comparison of fees collected to MVCPA appropriations.



*2021 Fees are estimated.

	Actual 2018	Actual 2019	Actual 2020	Forecast 2021 (Est.)	Forecast 2022 (Est.)	Forecast 2023 (Est.)
MVCPA Fee	\$ 49,083,185	\$ 50,042,957	\$ 91,817,082	\$ 100,085,913	\$ 100,085,913	\$ 100,085,913



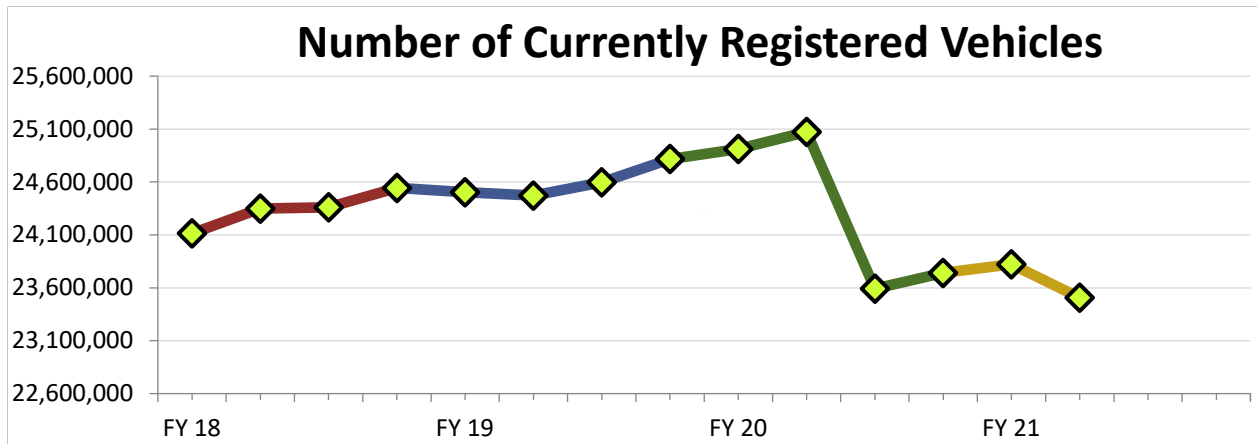
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All Funds (Fund 0001, Fund 0006, and Fund 0010): Title, Registration, Oversize/Overweight, and Processing and Handling Fees

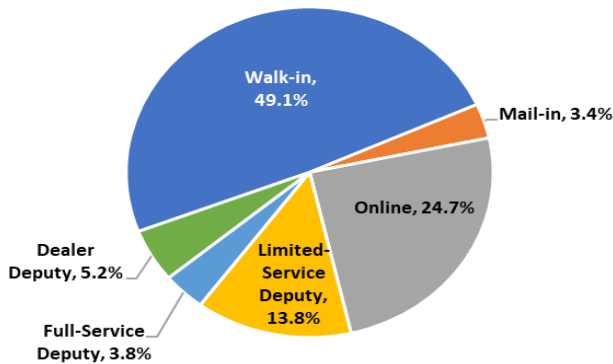
Registration Revenue

- All-funds registration revenue in FY 2021 decreased 1.6% (\$11.3 million) from FY 2020. This is based mostly on the waiver of certain temporary permits and the allowable *deferral* of annual-registration renewals, which will end on April 14, 2021.
- All-funds registration revenue was 2.2% (\$15.2 million) higher than projections. This revenue category met the FY 2021 projection and accounted for 83% of TxDMV revenue through the second quarter. The number of non-exempt registered vehicles went from 25.1 million at the end of February 2020 to 23.5 million at the end of February 2021, a decrease of 1.6 million (6.2%) vehicles. The number of registered vehicles will rebound as the deferral period draws to a close.



Processing and Handling Fee

Transaction Mix from Annual Registrations through the 2nd Quarter

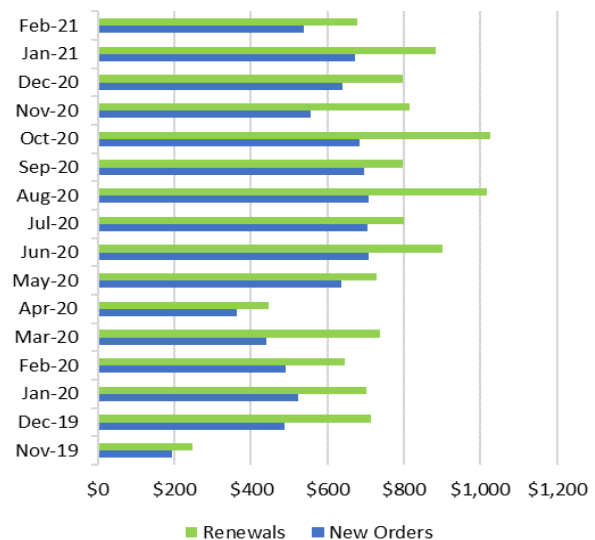


- A plurality (49.1%) of annual-registration transactions year-to-date were processed at county offices. Year-to-date online utilization was 24.7%, a 7.5-percentage-point increase from FY 2020.
- With some county offices closed temporarily, more registration renewals were processed online through the second quarter of FY 2021 than the same period of FY 2020. Through the second quarter, online registrations made up 2.7 million of the 10.8 million FY 2021 transactions versus 1.9 million of the 11.2 million FY 2020 transactions.

Vendor Plates

- General Revenue Fund 0001 deposits associated with the (third) MyPlates contract from November 19, 2019, to February 28, 2021, totaled \$21.0 million, of which \$9.6 million counted toward the contract's \$25 million guarantee.
- Since the effective date of the current contract, new orders made up 43.1% of the Fund 0001 mix, and renewals made up 56.9%.

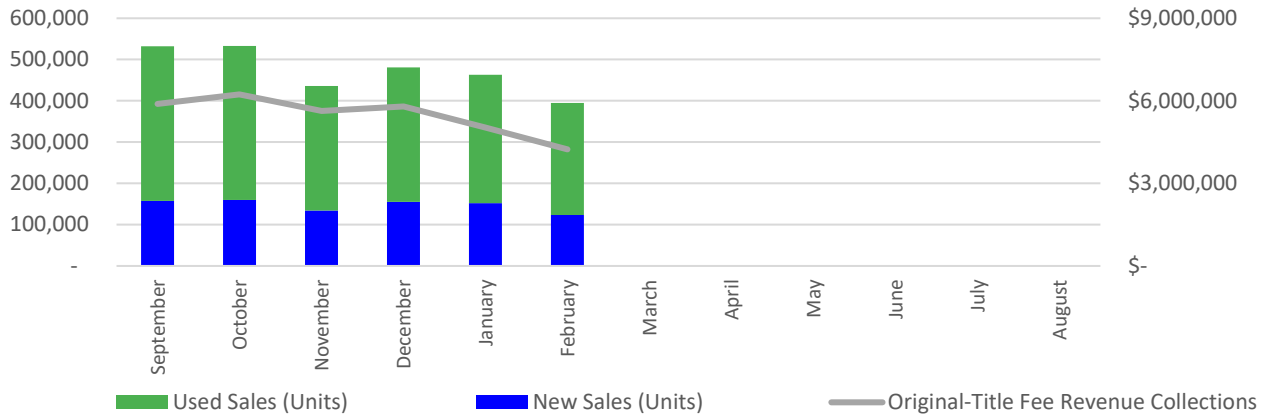
MyPlates Orders (Fund 0001 Portion)
(in thousands)



Motor Vehicle Certificates of Title

- The agency recognized a decrease (from projections) in FY 2021 all-funds title revenue of 7.5% (\$2.7 million) through February FY 2021.

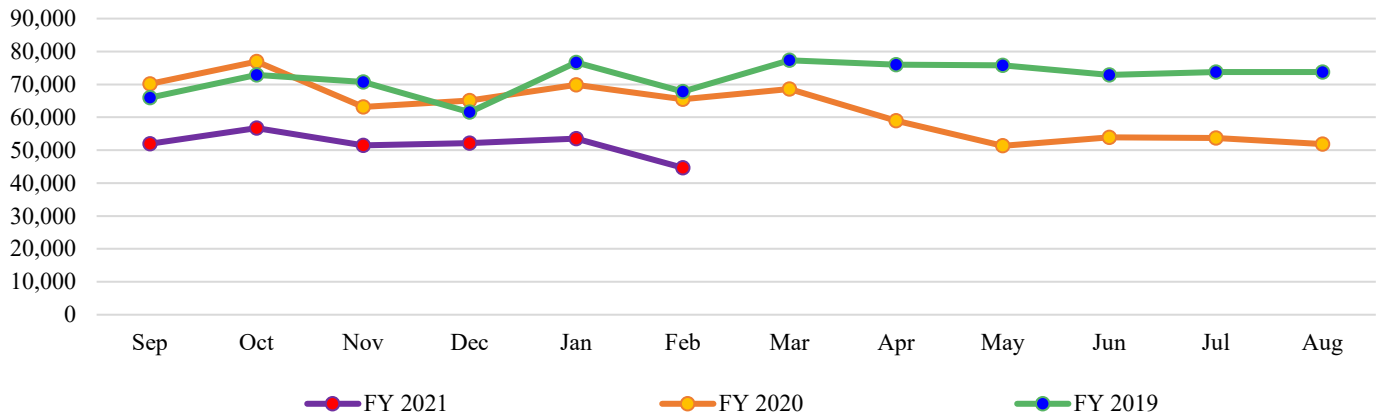
Monthly Auto Sales and Original-Title Fee Revenue Collections



- Revenue from the original-title fee makes up the largest component of certificates of title revenue. In FY 2021, revenue was collected from the issuance of about 3.0 million original titles through the second quarter. This was a decrease of 7.4% from the same time period in FY 2020. Original-title issuance is driven by new- and used-vehicle sales.
- Compared to FY 2020, auto sales in FY 2021 decreased by 5.0%, with used-car sales down 5.8% and new-car sales down 3.1%, all contributing to a year-over-year decrease in revenue.

Motor Carrier Oversize/Overweight

Monthly Oversize/Overweight Permit Issuance



- All-funds oversize/overweight permitting revenue was 4.7% (\$3.6 million) under FY 2021 projections. The number of permits issued in FY 2021 year-to-date was 310,487 compared to 410,786 issued in FY 2020, a decrease of 24.4% (100,299 more permits were issued in FY 2020). Decreased activity in the oil-and-gas sector has had an impact on the issuance of motor-carrier permits, resulting in lower oversize/overweight fee deposits. As a result of recent COVID-19 events and continued lower oil prices, revenue in this category did not meet second-quarter FY 2021 expectations, but is expected to see an uptick in the third and fourth quarters.



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Cumulative COVID-19 Impacts

FY 2021 Financial Impact of COVID-19 Response

- TxDMV began providing resources in March 2020 in response to the COVID-19 pandemic. Response activity has continued into FY 2021.
- Total expenses for FY 2020 related to the COVID-19 response totaled \$1.7 million. Expenses were primarily for staff time dedicated to the response, facility maintenance improvements and cleaning, and the acquisition of personal protective equipment for employees and customers.
- Total FY 2021 obligations for COVID-19 response, from September 2020 through February 2021 was \$1,508,163. The majority of the obligated amount was due to specific facility cleaning contracts that were established for providing COVID-19 cleaning services. The contracts provide cleaning coverage through August 2021. Other primary costs include employee time devoted specifically to COVID-19 response and temporary contract workers brought in to the Consumer Relations Division to assist with workload.
- The total projected cost impact in FY 2021 for COVID-19 response is estimated at \$2.2 million. The total cost estimate also assumes COVID-19 facility cleaning services will continue through the end of the fiscal year and staff time devoted to the response will continue through June 2021.
- The overall cost of the pandemic including \$1.7 million from FY 2020 and \$2.2 million estimated for FY 21 is a cumulative cost impact of \$3.9 million.
- The cumulative impact on revenues since the beginning of the COVID-19 event is a loss of \$37.2 million specifically due to fee waivers for delinquent title transfer penalties and certain temporary permits (along with the associated processing and handling fees on the permits). The waiver period will end on April 14, 2021.
- The cumulative impact on revenues since the beginning of the COVID-19 event is an additional loss of \$283.9 million due to a general decline in economic activity during the period.



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TxDMV Budget

September through February FY 2021**TxDMV Fund 0010**

The beginning budget amount for FY 2021, as approved by the 86th Legislative Session General Appropriations Act, was \$153,007,749. The budget has been modified for the carry forward of unexpended balances from FY 2020 (\$34,915,411 for both capital and operating appropriations) and for benefit costs (\$12,591,000). The current modified budget amount for all appropriations as of February 2021 is \$200,514,600.

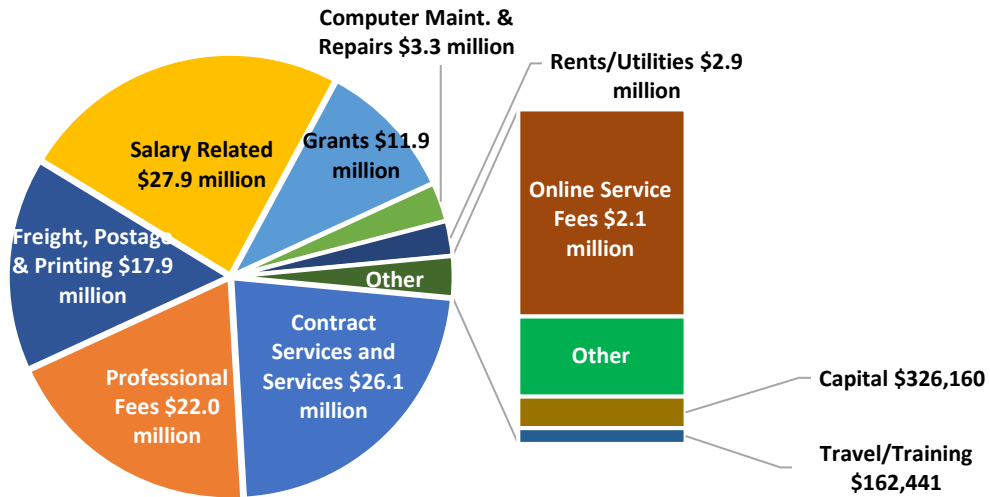
Key components of the FY 2021 budget include:

- Additional full-time equivalents (FTEs) were added for Consumer Relations (9.0 FTEs) and Information Technology Services (12.0 FTEs) beginning in FY 2020 and continuing into FY 2021.
- Capital funding was added for Regional Service Center renovations and upgrades (\$250,000 in FY 2020 and \$250,000 in FY 2021); ITS infrastructure and application improvements (\$1,850,000); and consumer protection and enforcement tracking (\$470,000 in FY 2020 and \$97,500 in FY 2021).
- Funding was also approved in the amount of \$730,000 in FY 2020 and \$1,161,606 to address increases in Statewide Cost Allocation Plan costs. These costs are for legislatively mandated reimbursements to the General Revenue Fund for central services provided by the Comptroller of Public Accounts, such as the maintenance of the statewide financial system used by TxDMV.
- A contingency rider was also approved during the 86th legislative session for implementing a digital license plates program. An appropriation in the amount of \$1.2 million was approved for FY 2020 for two new FTEs in the Vehicle Titles and Registration (VTR) Division and technology costs in the ITS Division. Funding for the FTEs continues in FY 2021. Administrative code rules to establish a digital license plates program have been finalized and a contract with a third-party vendor was approved in October 2020. Public go-live of the Digital License Plate program is anticipated to take place in March 2021.
- Unexpended balances from FY 2020 operating appropriations was authorized to be brought forward to FY 2021 by the legislative approval of a rider in the General Appropriations Act.

September through February FY 2021

- Second-quarter TxDMV obligations for all funds totaled \$115.5 million (expenditures of \$63.3 million and \$52.2 million in encumbrances). Encumbrances are outstanding purchase orders that have been issued for goods and services that will be received and expended in the future.

Second Quarter Obligations by Category - All Funds

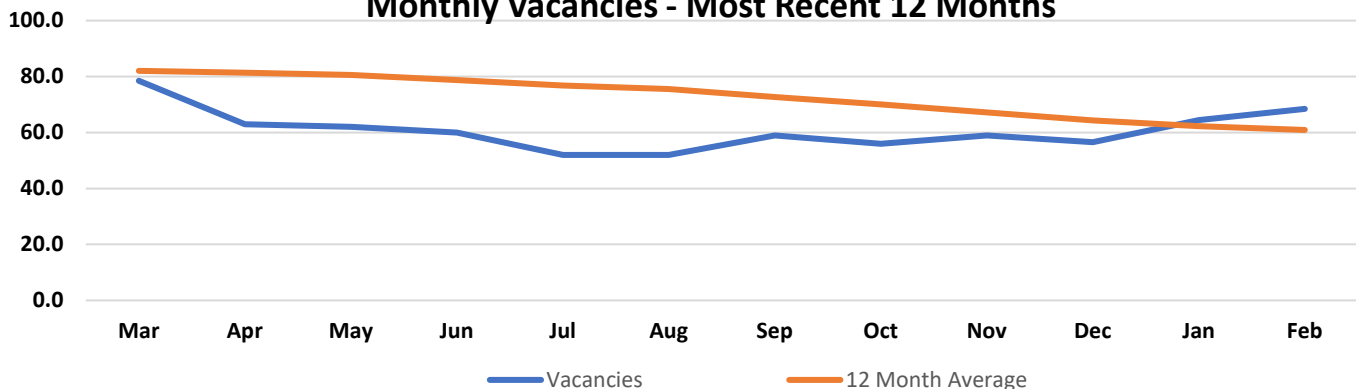


- Major second-quarter obligations in FY 2021 are listed in the chart above. Obligations for freight/postage/printing (primarily postage/printing), contract services, professional fees, salary related, and grants constitute 90% of the department's obligations for the second quarter.
- Printing expenditures are associated with titling and registration forms and imaging costs. Contract services include costs of license plates production, registration decal production, and MyPlates contract obligations. Professional fees are associated with data center services and capital project contractors working on department technology initiatives.

Full-Time Equivalents

- In FY 2020, the approved department FTE count increased from 779 to 802: nine new FTEs for Consumer Relations, twelve new FTEs for Information Technology Services, and two new FTEs for Vehicle Titles and Registration for digital license plates.
- Overall, filled positions have increased from 723.5 FTEs in March 2020 to 733.5 FTEs as of February 2021. Overall staffing since the beginning of FY 2020 has been steadily improving and vacancies have decreased from 78.5 at March 2020 to 68.5 at February 2021.

Monthly Vacancies - Most Recent 12 Months



FY 2021 Highlights

- The FY 2021 budget as of February 28, 2021 was \$200.5 million. This amount included the original baseline total of \$153.0 million as approved by the Legislature during the 86th legislative session; \$34.9 million in funds that were brought forward from FY 2020; and \$12.6 million for benefit costs.
- The baseline total of \$153.0 million provides funding for 802.0 FTEs, ongoing operating costs, and FY 2021 funding for capital projects.
- The \$34.9 million in carry forward funds as of February 28, 2021 is primarily from the continuation of capital projects funded in FY 2020 and continuing into FY 2021. The largest portion of the carry forward is from the TxDMV Automation Project, with a carry forward amount of \$17.7 million.
- The other major driver of carry forward balances is lapsed funds from the FY 2020 operating budget. During the 86th legislative session TxDMV received authority to carry forward any lapsed operating funds from FY 2020 into FY 2021. As of February 28, 2021 the operating carry forward amount was approximately \$10.0 million.
- The operating carry forward will be utilized by TxDMV in FY 2021 to address the continued COVID-19 response as well as other one-time costs as needed.
- The carry forward balance will also be utilized to address one-time facility expenditures related to the late February winter storm.

Capital Budget and Projects

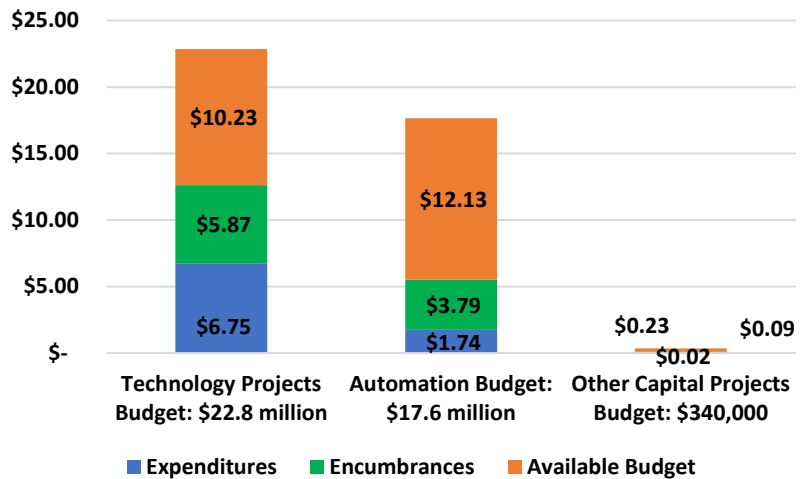
Capital Project Budget Status				
	Revised Budget	Expenditures	Encumbrances	Available Budget
Technology	\$ 22,853,240	\$ 6,751,032	\$ 5,870,953	\$ 10,231,255
Automation	\$ 17,662,680	\$ 1,743,110	\$ 3,787,711	\$ 12,131,859
Other Capital Projects	\$ 340,867	\$ 19,729	\$ 90,864	\$ 230,274
All Capital Grand Total	\$ 40,856,787	\$ 8,513,871	\$ 9,749,528	\$ 22,593,388

Capital Budget Status

The capital budget totals \$40,856,787.

- Including: Expenditures of \$8.5 million, and encumbrances of \$9.7 million, for a total of \$18.2 million in obligations.
- The budget as of the end of the quarter for capital consists of \$17.6 million carried forward from FY 2020 for Automation and HQ Maintenance projects, and \$17.9 million in new appropriations.
- Detailed information on Technology Projects is shown below, and Automation and Other Capital Project information is on the following page.

Second Quarter Capital Budget Status (In Millions)



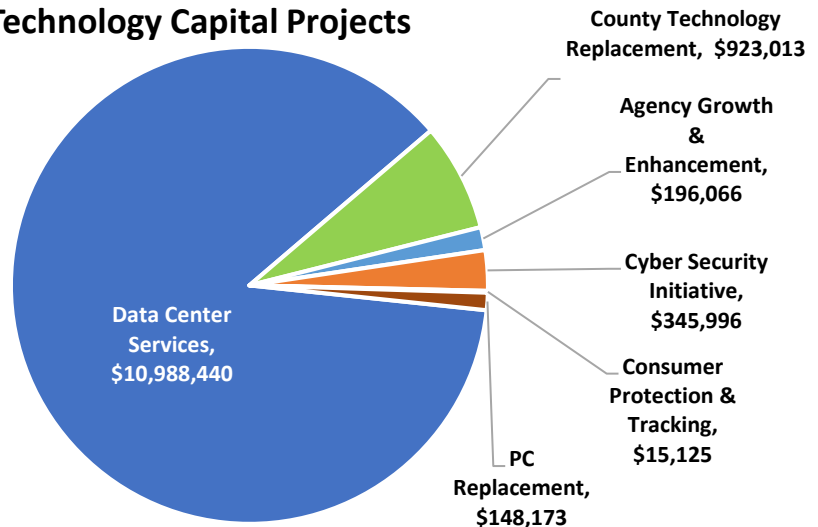
Technology Capital Projects

Technology Highlights

The obligations in the Technology category consist of:

- Data Center Services (DCS), the largest single component of the Technology budget (\$10.9 million), provides management of applications, hardware and technology services for TxDMV.
- The majority of expenditures and encumbrances through February 2021 includes Data Center Services, and toner and technical support for the counties. Obligations in County Technology Replacement and PC Replacement include laptops and desktops for the refresh programs.

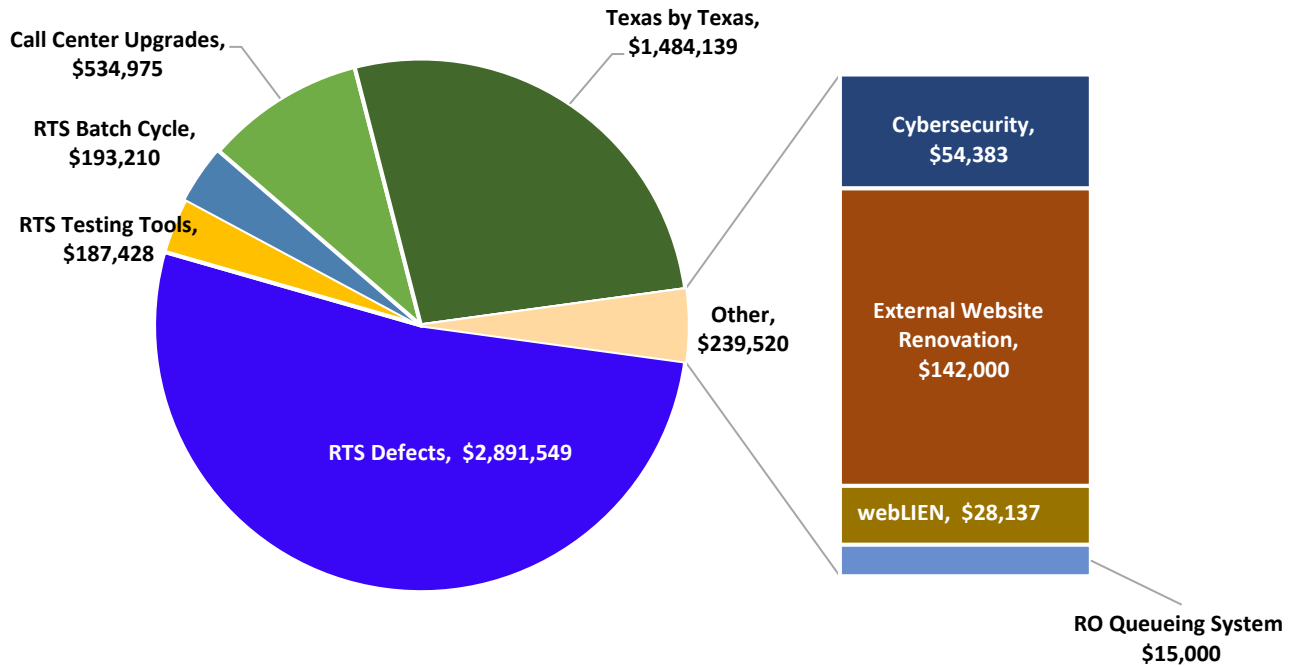
Technology Capital Projects



Financial Summary through the Second Quarter

Automation Capital Projects

Automation Obligations: \$5.5 million



- The TxDMV Automation project consists of \$5.5 million in obligations. The primary obligations as of February 2021 are for Registration and Title System (RTS) defects, Texas by Texas application implementation, and the Call Center Upgrades Project.
- The total Automation budget as of February 2021 is \$17.6 million.
- Approximately, \$4.3 million remains in Unallocated Reserve at the end of February 2021.
- Top IT initiatives upcoming throughout this fiscal year include webLIEN, the County Sandbox and Digital License Plates.
- With PC Replacement funds, desktops are being replaced with laptops for better telecommuting ease.

Other Capital Projects

- Other Capital Projects budget as of February 2021 totals \$340,000. That amount includes \$90,000 for agency vehicles and \$250,000 for regional service center maintenance.
- Funding for agency vehicles will provide for the acquisition of four vehicles in FY 2021.
- The RSC maintenance capital budget will be utilized in FY 2021 for renovations and facility improvements at the Midland-Odessa Regional Service Center.



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Board Meeting Date: 4/1/2021
BRIEFING

To: Texas Department of Motor Vehicles Board
From: Linda M. Flores, CPA, Chief Financial Officer, Finance & Administrative Services Division Director
Agenda Item: 6.E
Subject: FY 2022-2023 Legislative Appropriations Request Update (BRIEFING ONLY) – Linda M. Flores

PURPOSE

To provide a briefing on the Fiscal Year 2022-2023 Legislative Appropriations Request (LAR) and the recommended appropriations as included in the introduced versions of House Bill 1 (H.B.1) and Senate Bill 1 (S.B.1)

EXECUTIVE SUMMARY

The 87th Legislature will establish the Texas Department of Motor Vehicles (TxDMV) two-year appropriations through the passage of Senate Bill 1 (S.B. 1) in May 2021. The department is primarily funded by revenues deposited in the TxDMV Fund 0010, and General Revenue Fund 0001 to fund the Motor Vehicle Crime Prevention Authority (MVCPA).

In January 2021, the House of Representatives and the Senate filed their respective versions of the General Appropriations Act (GAA) House Bill 1 and Senate Bill 1, respectively. Both introduced bills included identical levels of baseline funding for the department totaling \$302.5 million, \$153.8 million in FY 2022 and \$148.7million in FY 2023.

Neither of the introduced bills recommended funding for any of the department's exceptional items requests.

In response to the recommendations of the introduced bills, the department re-prioritized and modified a new exceptional items list. The new list totaled \$36.6 million and was submitted to the Legislative Budget Board.

RIDERS

A rider is a legislative directive or appropriation inserted into the General Appropriations Act following appropriation line items for an agency or in a special or general provision of the act. A rider provides direction, expansion, restriction, legislative intent or an appropriation.

The introduced versions of H.B.1 and S.B.1 include all TxDMV requested riders for FY 2022-2023. These include Unexpended Balance authority for Automation and TxDMV HQ Maintenance capital projects; Unexpended Balance authority for Federal grants and matching funds; and Unexpended Balance authority within the biennium.

METHOD OF FINANCE

All of TxDMV operations and the recommended exceptional item requests would be funded through the TxDMV fund, with the exception of MVCPA. All MVCPA operations and its exceptional item requests would be funded through General Revenue.

H.B.1 AND S.B.1 AS INTRODUCED IN JANUARY 2021

H.B. 1. and S.B. 1 as introduced included a total of \$302.5 million for the department's FY 2022-2023 biennium. The introduced version of the appropriations bill did not include any requested exceptional items. The amount of \$302.5 million included baseline reductions in Automation and MVCPA grant funding.

MODIFIED EXCEPTIONAL ITEMS

The Legislative Budget Board provided TxDMV an opportunity to update their exceptional item requests in January 2021 after the House and Senate budget introduced recommendations became available.

The department modified its list of exceptional items to include nine items totaling \$36.6 million.

Two new exceptional items were included in the January 2021 modifications:

- A request of \$3.1 million to restore Automation capital funding to complete the Web Salvage project
- A request of \$8.5 million to restore MVCPA grant funding

One existing exceptional item from the original LAR submission was modified in the January 2021 update:

- The amount of funds to expand MVCPA grants was revised from \$2.5 million to \$7.3 million, an increase of \$4.8 million based on updated revenue estimates



Texas Department of Motor Vehicles FY 2022 – 2023 Legislative Appropriations Request Update

TxDMV LAR Comparison to HB1/SB1



	TxDMV Request/Full-Time Equivalents (FTEs)	HB 1/SB1 Recommended/Full- Time Equivalents (FTEs)	Difference
Baseline	\$319.3 Million/802 FTEs	\$302.5 Million/802 FTEs	\$(16.8 Million)
Exceptional	\$19.5 Million/11 FTEs	\$ - 0 -	\$(19.5 Million)/11 FTEs
Total	\$338.8 Million/813 FTEs	\$302.5 Million/802 FTEs	\$(36.3 Million)/11 FTEs

- Baseline request reduced by \$16.8 million primarily consisting of reductions in MVCPA grants, Automation capital, DCS capital, and market adjustments
- No exceptional items were recommended.
- Baseline included riders for Unexpended Balance authority for Automation capital and HQ Maintenance, matching funds for Federal grants, and unexpended authority within the FY 2022-2023 biennium

Revised Exceptional Items



TxDMV 2022-23 Exception Item Summary



Priority	Exceptional Items	Original Request				Revised Request			
		FY 2022	FY 2023	Biennial Total	Full Time Equivalents	FY 2022	FY 2023	Biennial Total	Full Time Equivalents
1	Restoration of Automation Funding	\$ -	\$ -	\$ -	-	\$ 3,113,578	\$ -	\$ 3,113,578	-
2	Building 5 Replacement	\$ 6,187,500	\$ -	\$ 6,187,500	-	\$ 6,187,500	\$ -	\$ 6,187,500	-
3	Accounts Receivables System	\$ 3,358,871	\$ 114,087	\$ 3,472,958	2.00	\$ 3,358,871	\$ 114,087	\$ 3,472,958	2.00
4	Complaint Management System	\$ 5,225,712	\$ -	\$ 5,225,712	-	\$ 5,225,712	\$ -	\$ 5,225,712	-
5	Houston RSC Sub-Station	\$ 821,207	\$ 358,912	\$ 1,180,119	4.00	\$ 821,207	\$ 358,912	\$ 1,180,119	4.00
6	Dallas RSC Sub-Station	\$ 613,340	\$ 242,630	\$ 855,970	2.00	\$ 613,340	\$ 242,630	\$ 855,970	2.00
1	Restoration of MVCPA Grant Funding	\$ -	\$ -	\$ -	-	\$ 4,287,508	\$ 4,287,508	\$ 8,575,016	-
2	MVCPA Expanded Coverage	\$ 1,276,641	\$ 1,276,641	\$ 2,553,282	-	\$ 3,550,241	\$ 3,838,642	\$ 7,388,883	-
3	MVCPA Fee Collection Unit	\$ -	\$ -	\$ -	-	\$ 280,000	\$ 280,000	\$ 560,000	3.00
Total, Exceptional Items		\$17,483,271	\$ 1,992,270	\$19,475,541	8.00	\$27,437,957	\$ 9,121,779	\$36,559,736	11.00
Method of Finance									
	General Revenue Fund 0001	\$ 1,276,641	\$ 1,276,641	\$ 2,553,282		\$ 8,117,749	\$ 8,406,150	\$ 16,523,899	
	Texas Department of Motor Vehicles Fund 0010	\$ 16,206,630	\$ 715,629	\$ 16,922,259		\$ 19,320,208	\$ 715,629	\$ 20,035,837	
Total, Method of Finance		\$17,483,271	\$ 1,992,270	\$19,475,541		\$27,437,957	\$ 9,121,779	\$36,559,736	

Modifications to Exceptional Items



Two new exceptional items were added:

- Restoration of Automation Capital funding – to complete the Web Salvage Project
- Restoration of Motor Vehicle Crime Prevention Authority (MVCPA) grant funding

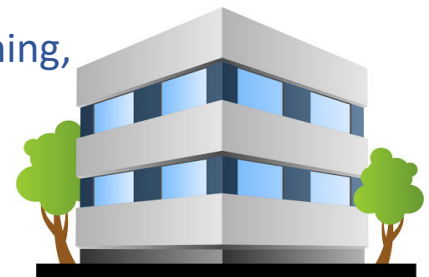
One existing exceptional item was modified:

- Expand MVCPA coverage – the amount was increased by \$4.8 million for the biennium based on updated revenue estimates

TxDMV Headquarters Building Construction



- Texas Facilities Commission determined that it was more cost effective to newly construct rather than repair current structures
- Total Cost: \$65 million based on current assessment estimates
- All costs covered through the TxDMV Fund, regardless of bonding or lump-sum appropriation, no General Revenue is required
- TxDMV is requesting \$6.2 million in the FY 2022-2023 biennium for Planning, Design and Site Preparation
- Construction costs are not being requested in the FY 2022-2023 biennium

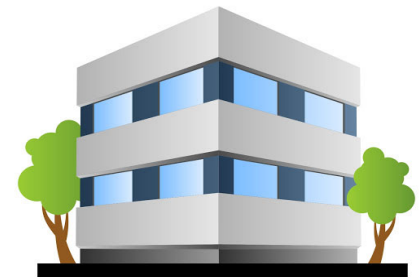


TxDMV Headquarters Building Construction



\$65 million project financing options

- *Option 1:*
 - ✓ Legislature Approval Required
 - ✓ Bonds issued by the Texas Public Finance Authority,
 - ✓ 20-year bonds, 2.5% interest,
 - ✓ Monthly payment of \$344,437; Annual payment of \$4,133,244
 - ✓ Biennial Payment of \$8,266,488
- *Option 2:*
 - ✓ Lump-sum funding request to be considered by the Legislature

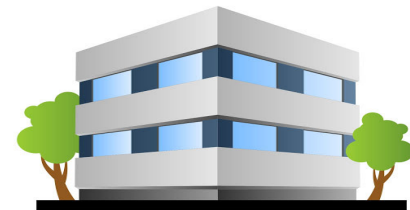


TxDMV Headquarters Building Construction



Texas Public Finance Authority Process

- Steps to request bond funding from the Texas Public Finance Authority (TPFA)
 - ✓ Request legislative authorization through a General Appropriations Act Rider
 - ✓ The Rider will authorize the project, the issuance of revenue bonds, the appropriation of bond proceeds, and the appropriation of lease payments
 - ✓ A resolution adopted by the TxDMV Board authorizing submittal of the request to TPFA
 - A project description, budget, and estimated expenditure schedule must be provided to TPFA
 - ✓ The request must be approved by the TPFA Board



To: Texas Department of Motor Vehicles Board
From: Linda M. Flores, CPA, Chief Financial Officer, Finance & Administrative Services Division Director
Agenda Item: 6.F
Subject: Winter Storm 2021 Impacts to TxDMV Facilities and Regional Service Centers

OVERVIEW

During the week of February 15, 2021, TxDMV operations were impacted by wintry weather, unusually cold temperatures and dangerous roadways. Several offices experienced issues related to a lack of heating and electrical services, as well as water supply.

The following locations were adversely impacted as a result:

- 1) **Austin Regional Service Center** – The Austin Regional Service Center experienced water damage due to two (2) broken water lines. This is a TxDOT facility and TxDOT quickly made repairs that allowed the office to open as planned on Monday, February 22, 2021, without delay.
- 2) **Longview Regional Service Center** – The Longview Regional Service Center experienced some water damage due to a single broken pipe. This is another TxDOT facility and TxDOT again quickly made repairs that allowed the office to open without delay.
- 3) **Austin Headquarters – Camp Hubbard, building 1** – Camp Hubbard, building 1 headquarters operations experienced a fire line rupture that flood several areas of the first floor, primarily impacting the employee lobby entrance, the Lone Star/Board Room and the executive director’s office suite. TxDMV Facilities Services quickly began addressing needs. Water extraction has been completed and repairs are underway to the lobby ceiling and sheetrock and cleaning needs in the executive director’s office. Staff housed in this location have been able to telecommute while work is performed.
- 4) **Austin Headquarters – Camp Hubbard, building 5** – Camp Hubbard, building 5 experienced roof leaks on the second, smaller floor, of the building, which continues to occur with each weather event due to an old roofing system. TxDMV Facilities Services is replacing 150 ceiling tiles and is having the carpet cleaned. Most occupants of this floor have been telecommuting.

FISCAL IMPACT

Our Facilities team continues to assess the buildings and property needs.

Cost Impacts to date:

Item	Cost
County Computer Equipment Replacements*	\$0.00
Water Damage Clean Up	19,265.00
Tree Debris Clean Up	3,600.00
Bottled Water	120.00
Fire Suppression pipe break repairs	3,673.31

Ceiling and Wall Repairs	2,426.66
Floor Repairs	3,391.67
Painting	2,166.67
Building 5 Carpet Cleaning	No Cost
TOTAL	\$34,643.31
*Pending	

No action is required from the Committee on this briefing item.

Impact of Winter Storms on TxDMV Facilities

- **Facilities Update:** All TxDMV facilities, except Camp Hubbard Building 6, opened for on-site staff on Monday, February 22, 2021. The following is a summary of the storm’s impact on TxDMV facilities:
 - *Building 1:* A fire-line ruptured and flooded parts of the first floor, primarily impacting the main lobby entrance, Lone Star Room and executive office. Water extraction, carpet cleaning, and repairs to the fire-line were performed allowing them to be reoccupied. Minor ceiling and wall repairs are still underway as we fully restore the impacted areas.
 - *Building 5:* Due to the current condition of the roof, water leaks continue with each weather event. The carpet was cleaned on March 3rd and approximately 150 ceiling tiles will be replaced.
 - *Building 6:* The water was turned off in the building while TxDOT repaired water damage from broken pipes between the first and second floors. No damage occurred on the fifth floor, which houses the Motor Carrier Division (MCD). MCD staff telecommuted on Monday, February 22nd, and allowed to reoccupy the building February 23rd.
 - *Austin RSC:* The Austin Regional Service Center experienced water damage due to two (2) broken water lines. This is a TxDOT facility and TxDOT quickly made repairs allowing the office to open as planned on Monday, February 22nd, without delay.
 - *Longview RSC:* The Longview Regional Service Center experienced water damage due to a single broken pipe. This is a TxDOT facility and TxDOT quickly made repairs allowing the office to open as planned on Monday, February 22nd, without delay.

Cost Impact as of 03-19-2021

Item	Cost
County Computer Equipment Replacements*	\$0.00
Water Damage Clean Up	19,265.00
Tree Debris Clean Up	3,600.00
Bottled Water	120.00
Fire Suppression pipe break repairs	3,673.31
Ceiling and Wall Repairs	2,426.66
Floor Repairs	3,391.67
Painting	2,166.67
Building 5 Carpet Cleaning	No Cost
TOTAL	\$34,643.31
*Pending	

To: Texas Department of Motor Vehicles Board
From: Roland Luna, Vehicle Titles & Registration Division Director
Agenda Item: 7
Subject: Special Plate Designs

RECOMMENDATION

The Vehicle Titles and Registration Division (VTR) seeks board approval or denial of two plate designs submitted for your consideration. Each plate design is from the marketing vendor, My Plates.

The Texas Criminal Defense Lawyers Association plate is a new plate design and has never been sold before. The Baylor Bears is a redesign of an existing plate.

PURPOSE AND EXECUTIVE SUMMARY

Statutory authority for the board to approve vendor specialty license plates and invite the public's comment on proposed vendor plate designs are in Texas Transportation Code Section 504.851 (g) and (g-1) (1). Statutory authority for a sponsor of a specialty license plate under Texas Transportation Code Chapter 504, Subchapter J, to contract with the private vendor authorized under Texas Transportation Code Section 504.851 for the marketing and sale of the specialty license plate is in Texas Transportation Code Section 504.6011. Statutory authority for the board to approve non-profit organization specialty license plates and invite the public's comment on proposed plate designs are in Texas Transportation Code Section 504.801. The board's approval criteria are clarified in Administrative Codes §217.45 Specialty License Plates, Symbols, Tabs, and Other Devices and §217.52 Marketing of Specialty License Plates through a Private Vendor.

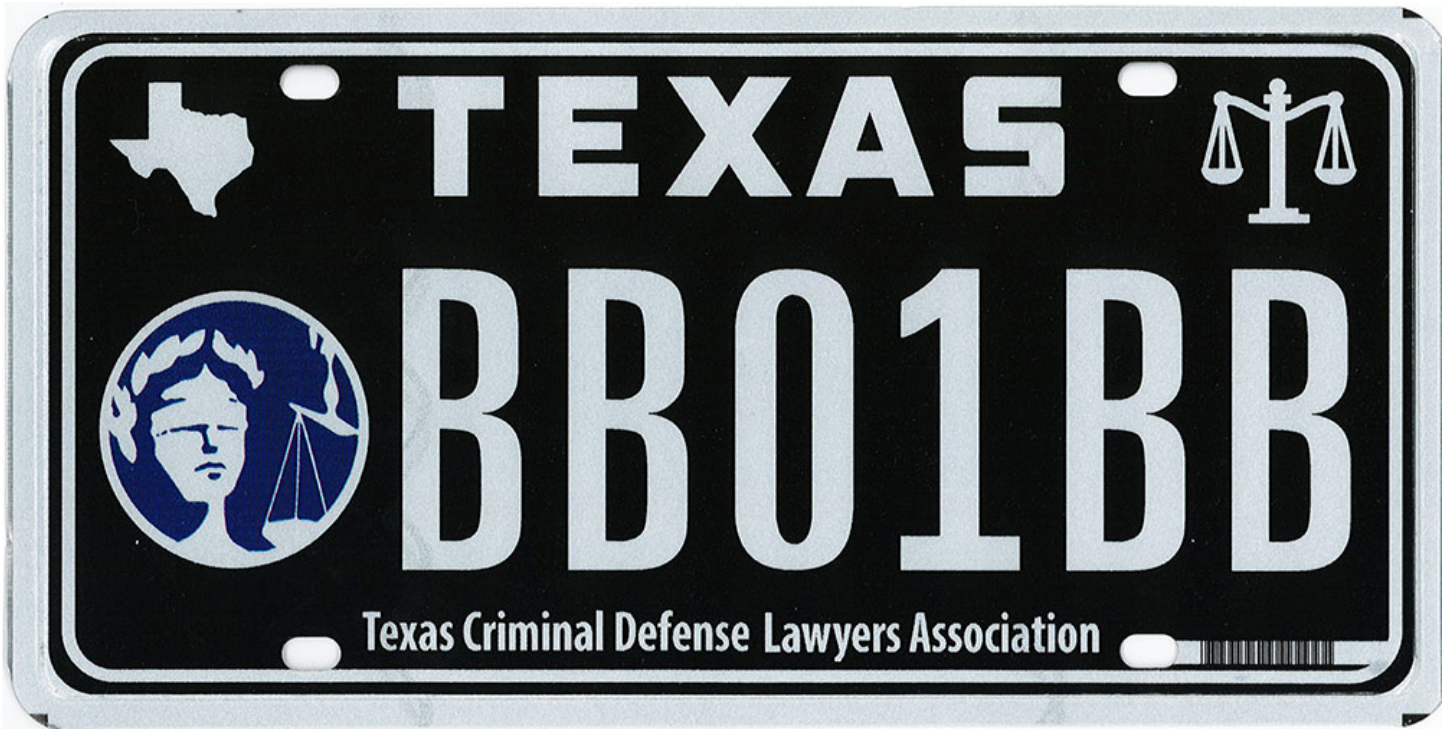
The vendor contract (Statement of Work paragraph #2, *Marketing Services*) specifies that following the board's contingent approval of a plate, the vendor must get at least 200 commitments within six months of the approval for a plate to be produced. (Equally, existing plates must maintain 200 registered to stay in the program.) My Plates' procedure is to first offer a plate to the public to register their interest. Following the board's contingent approval, My Plates then offers a plate online for prepaid orders. My Plates confirms when 200 prepaid orders are achieved. Since March 2014, the board has contingently approved 34 vendor plates. Of the 34, nine did not achieve the required 200 commitments and were not produced.

TxDMV's procedure is to invite comments on all proposed plates ahead of the board's review. The department's intent is to determine if there are any unforeseen public concerns about a plate design. The department publishes a 10-day "like/dislike/comment-by-email" survey, called an eView, on its website. Although the survey counts the public's "likes" and "dislikes," it is unscientific and not used as an indicator of a plate's popularity.

The plate designs were presented to the public in a February 2021 eView. No negative comments were received. The count of the public's "like/dislikes" are below with the designs.

Texas Criminal Defense Lawyers Association	New	
133 people liked this design and 66 did not		
Baylor Bears	Current	Redesign
176 people liked this design and 98 did not		

Texas Criminal Defense Lawyers Association (New)



Baylor Bears (Redesign)

Redesign



Current Design



Vehicle Titles and
Registration Division
Special Plates Unit (6FTEs) 01/21



VTR Director
Roland D. Luna, Sr.

APR. 2021



New Specialty Plates in March



SLP AVAILABLE 506
MILITARY AND DV 190
RESTRICTED USE 51
STATE SPECIALTY 139
VENDOR SPECIALTY 126



CHARITY

	LINKED	UNLINKED	TOTAL
1. ANIMAL FRIENDLY	8,280	373	8,653
2. CONSERVATION: HORNED LIZARD	6,682	268	6,950
3. STATE OF THE ARTS	5,314	189	5,503
4. CONSERVATION: BLUEBONNET	4,529	209	4,738
5. CONSERVATION: WHITE-TAILED DEER	3,257	153	3,428
6. TEXAS A & M UNIVERSITY	2,600	54	2,654
7. BIG BEND	2,078	160	2,238
8. CONSERVATION: LARGE MOUTH BASS	1,920	121	2,041
9. NATIVE TEXAN	1,917	192	2,009
10. TEXAS TECH UNIVERSITY	1,883	67	1,950



VENDOR

	LINKED	UNLINKED	TOTAL
1. CLASSIC BLACK	38,452	8,548	47,000
2. LARGE STAR WHITE/BLACK	38,207	8,180	46,387
3. TEXAS BLACK 1845	16,199	4,068	20,267
4. LONE STAR BLACK	10,243	3,516	13,759
5. CARBON FIBER	6,495	1,527	8,022
6. LONE STAR BLK/SILV	4,063	1,234	5,297
7. TEXAS VINTAGE BLACK	3,771	1,010	4,781
8. T FOR TEXAS BLACK	3,631	1,546	5,177
9. TEXAS A&M (MAROON)	3,631	607	4,238
10. WHITE	3,242	829	4,071

TOP 10



MILITARY

1. DISABLED VETERAN	197,566	4,427	201,993
2. DV U.S. ARMY	42,909	897	43,806
3. DV U.S. MARINE CORPS	21,533	431	21,964
4. DV U.S. AIR FORCE	19,011	382	19,393
5. DV U.S. NAVY	16,010	316	16,326
6. PURPLE HEART	14,400	379	14,779
7. DV BRONZE STAR MEDAL	12,589	219	12,163
8. U.S. MARINE CORPS	11,751	412	12,163
9. MERITORIOUS SERVICE MEDAL	11,307	499	11,806
10. U.S. ARMY	10,264	450	10,714

SPECIAL PLATES UNIT CUSTOMER SERVICE FY 2021

26,948

10,538

0

7,058

1,440

3

2,083

Personalized Plate
Applications Reviewed
(10% Declined)

Telephone Calls

Walk-in
Customers

Emails

Refunds

Public Information
Open Records

Correspondence
(Including Plate
Applications)

To: Texas Department of Motor Vehicles Board
From: Caroline Love, Government & Strategic Communications Division Director
Agenda Item: 8
Subject: 87th Legislative Session Update

RECOMMENDATION

Briefing Only.

PURPOSE AND EXECUTIVE SUMMARY

This briefing will cover the key dates for the 87th Legislative Session, as well as the responsibilities of the Government & Strategic Communications Division as it relates to the department's review and analysis of legislation, coordination of the department in legislative hearings and meetings, and providing updates to department leadership and the TxDMV Board.

FINANCIAL IMPACT

None.

BACKGROUND AND DISCUSSION

The Government & Strategic Communications Division will be providing regular updates throughout the session on the status of legislation impacting the department. The discussion will also include an overview of legislation filed containing components of TxDMV Board Recommendations to the 87th Legislature, including:

- [HB 3514](#) (Canales): Miscellaneous clean-up and non-substantive changes including Lemon Law and MVCPA updates to reflect current practices.
- [HB 3531](#) (Martinez): All title, registration and license plates recommendations included. Titling and registration include efficiency measures with processing transactions, license plates language is clean-up in nature.
- [HB 3532](#) (Martinez): Conforming size and weight references to federal statutes and general motor carrier clean up provisions (SB 1815), cleaning up current county oversize/overweight bond requirements (SB 1814).
- [HB 3533](#) (Martinez): Increase of dealer bonds for used car dealers only, from \$25,000 to \$50,000.
- [HB 4276](#) (Thompson, E.): Provides the TxDMV Board with rulemaking authority on limiting the number of temp tags a licensed dealer can issue (SB 1816).
- [SB 15](#) (Nichols): Includes several data protection measures, including the TxDMV Board recommendation to require an entity no longer eligible to receive the data to not retain any previously obtained data.
- [SB 1814](#) (Seliger): Clean-up of county oversize/overweight permits to no longer require a bond, but to maintain and provide list of permits issued to counties where permit is used (included in a portion of HB 3532 as well).
- [SB 1815](#) (Seliger): Conforming size and weight references to federal statutes and general motor carrier clean up provisions (included in a portion of HB 3532 as well).
- [SB 1816](#) (Seliger): Provides the TxDMV Board with rulemaking authority on limiting the number of temp tags a license dealer can issue (4276), clarifies temp tags/permits must be displayed in the rear license plate area (included in a portion of HB 3531 as well).
- [SB 1817](#) (Seliger): Provides title processing efficiencies for motor vehicles with insurance claims (included in a portion of HB 3531 as well).

Board Policy Documents

Governance Process (10/13/11)

Strategic Planning (10/13/11)

Board Vision (4/7/16)

Agency Boundaries (9/13/12)

Texas Department of Motor Vehicles TxDMV Board Governance Policy

1. PURPOSE

The directives presented in this policy address board governance of the Texas Department of Motor Vehicles (TxDMV).

2. SCOPE

The directives presented in this policy apply to the TxDMV Board and TxDMV agency personnel who interact with the Board. The TxDMV Board Governance Policy shall be one that is comprehensive and pioneering in its scope.

3. POLICY

3.1. TxDMV Board Governing Style

The Board shall govern according to the following general principles: (a) a vision for the agency, (b) diversity in points of view, (c) strategic leadership, providing day-to-day detail as necessary to achieve the agency vision, (d) clear distinction of Board and Executive Director roles, (e) collective decision making, (f) react proactively rather than reactively and with a strategic approach. Accordingly:

- 3.1.1. The Board shall provide strategic leadership to TxDMV. In order to do this, the Board shall:
 - 3.1.1.1. Be proactive and visionary in its thinking.
 - 3.1.1.2. Encourage thoughtful deliberation, incorporating a diversity of viewpoints.
 - 3.1.1.3. Work together as colleagues, encouraging mutual support and good humor.
 - 3.1.1.4. Have the courage to lead and make difficult decisions.
 - 3.1.1.5. Listen to the customers and stakeholders needs and objectives.
 - 3.1.1.6. Anticipate the future, keeping informed of issues and trends that may affect the mission and organizational health of the TxDMV.
 - 3.1.1.7. Make decisions based on an understanding that is developed by appropriate and complete stakeholder participation in the process of identifying the needs of the motoring public, motor vehicle industries,

and best practices in accordance with the mission and vision of the agency.

- 3.1.1.8. Commit to excellence in governance, including periodic monitoring, assessing and improving its own performance.
- 3.1.2. The Board shall create the linkage between the Board and the operations of the agency, via the Executive Director when policy or a directive is in order.
- 3.1.3. The Board shall cultivate a sense of group responsibility, accepting responsibility for excellence in governance. The Board shall be the initiator of policy, not merely respond to staff initiatives. The Board shall not use the expertise of individual members to substitute for the judgment of the board, although the expertise of individual members may be used to enhance the understanding of the Board as a body.
- 3.1.4. The Board shall govern the agency through the careful establishment of policies reflecting the board's values and perspectives, always focusing on the goals to be achieved and not the day-to-day administrative functions.
- 3.1.5. Continual Board development shall include orientation of new Board members in the board's governance process and periodic board discussion of how to improve its governance process.
- 3.1.6. The Board members shall fulfill group obligations, encouraging member involvement.
- 3.1.7. The Board shall evaluate its processes and performances periodically and make improvements as necessary to achieve premier governance standards.
- 3.1.8. Members shall respect confidentiality as is appropriate to issues of a sensitive nature.

3.2. TxDMV Board Primary Functions/Characteristics

TxDMV Board Governance can be seen as evolving over time. The system must be flexible and evolutionary. The functions and characteristics of the TxDMV governance system are:

- 3.2.1. Outreach
 - 3.2.1.1. Monitoring emerging trends, needs, expectations, and problems from the motoring public and the motor vehicle industries.
 - 3.2.1.2. Soliciting input from a broad base of stakeholders.

3.2.2. Stewardship

3.2.2.1. Challenging the framework and vision of the agency.

3.2.2.2. Maintaining a forward looking perspective.

3.2.2.3. Ensuring the evolution, capacity and robustness of the agency so it remains flexible and nimble.

3.2.3. Oversight of Operational Structure and Operations

3.2.3.1. Accountability functions.

3.2.3.2. Fiduciary responsibility.

3.2.3.3. Checks and balances on operations from a policy perspective.

3.2.3.4. Protecting the integrity of the agency.

3.2.4. Ambassadorial and Legitimizing

3.2.4.1. Promotion of the organization to the external stakeholders, including the Texas Legislature, based on the vision of the agency.

3.2.4.2. Ensuring the interests of a broad network of stakeholders are represented.

3.2.4.3. Board members lend their positional, professional and personal credibility to the organization through their position on the board.

3.2.5. Self-reflection and Assessment

3.2.5.1. Regular reviews of the functions and effectiveness of the Board itself.

3.2.5.2. Assessing the level of trust within the Board and the effectiveness of the group processes.

3.3. Board Governance Investment

Because poor governance costs more than learning to govern well, the Board shall invest in its governance capacity. Accordingly:

3.3.1. Board skills, methods, and supports shall be sufficient to ensure governing with excellence.

- 3.3.1.1. Training and retraining shall be used liberally to orient new members, as well as maintain and increase existing member skills and understanding.
 - 3.3.1.2. Outside monitoring assistance shall be arranged so that the board can exercise confident control over agency performance. This includes, but is not limited to, financial audits.
 - 3.3.1.3. Outreach mechanisms shall be used as needed to ensure the Board's ability to listen to stakeholder viewpoints and values.
 - 3.3.1.4. Other activities as needed to ensure the Board's ability to fulfill its ethical and legal obligations and to represent and link to the motoring public and the various motor vehicle industries.
- 3.3.2. The Board shall establish its cost of governance and it will be integrated into strategic planning and the agency's annual budgeting process.

3.4. Practice Discipline and Assess Performance

The Board shall ensure the integrity of the board's process by practicing discipline in Board behavior and continuously working to improve its performance. Accordingly:

- 3.4.1. The assigned result is that the Board operates consistently with its own rules and those legitimately imposed on it from outside the organization.
 - 3.4.1.1. Meeting discussion content shall consist solely of issues that clearly belong to the Board to decide or to monitor according to policy, rule and law. Meeting discussion shall be focused on performance targets, performance boundaries, action on items of Board authority such as conduct of administrative hearings, proposal, discussion and approval of administrative rule-making and discussion and approval of all strategic planning and fiscal matters of the agency.
 - 3.4.1.2. Board discussion during meetings shall be limited to topics posted on the agenda.
 - 3.4.1.3. Adequate time shall be given for deliberation which shall be respectful, brief, and to the point.
- 3.4.2. The Board shall strengthen its governing capacity by periodically assessing its own performance with respect to its governance model. Possible areas of assessment include, but are not limited to, the following:
 - 3.4.2.1. Are we clear and in agreement about mission and purpose?

- 3.4.2.2. Are values shared?
- 3.4.2.3. Do we have a strong orientation for our new members?
- 3.4.2.4. What goals have we set and how well are we accomplishing them?
- 3.4.2.5. What can we do as a board to improve our performance in these areas?
- 3.4.2.6. Are we providing clear and relevant direction to the Executive Director, stakeholders and partners of the TxDMV?
- 3.4.3. The Board Chair shall periodically promote regular evaluation and feedback to the whole Board on the level of its effectiveness.

Texas Department of Motor Vehicles Strategic Planning Policy

1. PURPOSE

The directives presented in this policy address the annual Strategic Planning process at the Texas Department of Motor Vehicles (TxDMV).

2. SCOPE

The directives presented in this policy apply to the TxDMV Board and TxDMV agency personnel who interact with the Board. TxDMV Strategic Planning Policy attempts to develop, document and expand its policy that is comprehensive in its scope in regards to the strategic planning process of the Board and the Department beyond that of the state strategic planning process.

3. POLICY

3.1. TxDMV Board Strategic Planning

This policy describes the context for strategic planning at TxDMV and the way in which the strategic plan shall be developed and communicated.

- 3.1.1. The Board is responsible for the strategic direction of the organization, which includes the vision, mission, values, strategic goals, and strategic objectives.
- 3.1.2. TxDMV shall use a 5-year strategic planning cycle, which shall be reviewed and updated annually, or as needed.
- 3.1.3. The 5-year strategic plan shall be informed by but not confined by requirements and directions of state and other funding bodies.
- 3.1.4. In developing strategic directions, the Board shall seek input from stakeholders, the industries served, and the public.
- 3.1.5. The Board shall:
 - 3.1.5.1. Ensure that it reviews the identification of and communication with its stakeholders at least annually.
 - 3.1.5.2. Discuss with agency staff, representatives of the industries served, and the public before determining or substantially changing strategic directions.

-
- 3.1.5.3. Ensure it receives continuous input about strategic directions and agency performance through periodic reporting processes.
 - 3.1.6. The Board is responsible for a 5-year strategic plan that shall identify the key priorities and objectives of the organization, including but not limited to:
 - 3.1.6.1. The creation of meaningful vision, mission, and values statements.
 - 3.1.6.2. The establishment of a Customer Value Proposition that clearly articulates essential customer expectations.
 - 3.1.6.3. A Strengths, Weaknesses, Opportunities and Threats (SWOT) Analysis, to be updated annually.
 - 3.1.6.4. An assessment of external factors or trends (i.e., customer needs, political factors, economic factors, industry trends, technology factors, uncertainties, etc.)
 - 3.1.6.5. Development of the specific goals and objectives the Department must achieve and a timeline for action.
 - 3.1.6.6. Identification of the key performance indicators to measure success and the initiatives that shall drive results.
 - 3.1.6.7. Engage staff at all levels of the organization, through the executive director, in the development of the strategic plan through surveys, interviews, focus groups, and regular communication.
 - 3.1.6.8. Ensure the strategic planning process produces the data necessary for LBB/GOBPP state required compliance while expanding and enhancing the strategic plan to support the needs of the TxDMV. The overall strategic plan shall be used as a tool for strategic management.
 - 3.1.7. The Board delegates to the Executive Director the responsibility for **implementing** the agency's strategic direction through the development of agency wide and divisional operational plans.
-

Texas Department of Motor Vehicles TxDMV Goals and Objectives

1. PURPOSE

The information presented in this policy addresses the goals and key objectives of the Board of the Texas Department of Motor Vehicles (TxDMV) as they relate to the mission, vision, and values of the TxDMV.

2. SCOPE

The scope of this policy is to define the desired state the TxDMV Board is working to achieve. This policy is designed to be inspirational in outlining the desired state of the agency that supports the TxDMV Board vision and meeting agency goals.

3. TxDMV MISSION

To serve, protect and advance the citizens and industries in the state with quality motor vehicle related services.

4. TxDMV VISION

The Texas Department of Motor Vehicles sets the standard as the premier provider of customer service in the nation.

5. TxDMV VALUES

To earn the trust and faith of all citizens of Texas with transparency, efficiency, excellence, accountability, and putting stakeholders first.

- 5.1. **Transparency** – Being open and inclusive in all we do.
- 5.2. **Efficiency** – Being good stewards of state resources by providing products and services in the most cost-effective manner possible.
- 5.3. **Excellence** – Working diligently to achieve the highest standards.
- 5.4. **Accountability** – Accepting responsibility for all we do, collectively and as individuals.
- 5.5. **Stakeholders** – Putting customers and stakeholders first, always.

6. TxDMV GOALS

6.1. GOAL 1 – Performance Driven

The TxDMV shall be a performance driven agency in its operations whether it is in customer service, licensing, permitting, enforcement or rule-making. At all times the TxDMV shall mirror in its performance the expectations of its customers and stakeholder by effective, efficient, customer-focused, on-time, fair, predictable and thorough service or decisions.

6.1.1. Key Objective 1

The TxDMV shall be an agency that is retail-oriented in its approach. To accomplish this orientation TxDMV shall concentrate the focus of the agency on:

- 6.1.1.1. Delivering its products and services to all of its customers and stakeholders in a manner that recognizes that their needs come first. These needs must be positively and proactively met. TxDMV works for and with its customers and stakeholders, not the other way around.
- 6.1.1.2. Operating the agency's licensing and registration functions in a manner akin to how a private, for-profit business. As a private, for-profit business, TxDMV would have to listen to its customers and stakeholders and implement best practices to meet their needs or its services would no longer be profitable or necessary. Act and react in a manner that understands how to perform without a government safety net and going out of business.
- 6.1.1.3. Simplify the production and distribution processes and ease of doing business with the TxDMV. Adapting and maintaining a business value of continuous improvement is central to TxDMV operations and processes.
- 6.1.1.4. All operations of the TxDMV shall stand on their own merits operationally and financially. If a current process does not make sense then TxDMV shall work within legislative and legal constraints to redesign or discard it. If a current process does not make or save money for the state and/or its customers or stakeholders then TxDMV shall work within legislative and legal constraints to redesign or discard it. TxDMV shall operate as efficiently and effective as possible in terms of financial and personnel needs. Divisions should focus on cost savings without sacrificing performance. Division directors are accountable for meeting these needs and applicable measures. All division directors are collectively responsible for the performance of TxDMV as a whole.
- 6.1.1.5. Focus on revenue generation for transportation needs as well as the needs of its customers.
- 6.1.1.6. Decisions regarding the TxDMV divisions should be based on the overriding business need of each division to meet or provide a specific service demand, with the understanding and coordination of overarching agency-wide needs.

- 6.1.1.7. Developing and regularly updating a long-range Statewide Plan describing total system needs, establishing overarching statewide goals, and ensuring progress toward those goals.
- 6.1.1.8. The TxDMV shall establish a transparent, well-defined, and understandable system of project management within the TxDMV that integrates project milestones, forecasts, and priorities.
- 6.1.1.9. The TxDMV shall develop detailed work programs driven by milestones for major projects and other statewide goals for all TxDMV divisions.
- 6.1.1.10. The TxDMV, with input from stakeholders and policymakers, shall measure and report on progress in meeting goals and milestones for major projects and other statewide goals.

6.2. GOAL 2 – Optimized Services and Innovation

The TxDMV shall be an innovative, forward thinking agency that looks for ways to promote the economic well-being and development of the industries it serves as well as the State of Texas within the legislative boundaries that have been established for the agency.

6.2.1. Key Objective 1

The TxDMV shall achieve operational, cultural, structural and financial independence from other state agencies.

- 6.2.1.1. Build the TxDMV identity. This means that TxDMV shall make customers aware of what services we offer and how they can take advantage of those services.
- 6.2.1.2. Build the TxDMV brand. This means that TxDMV shall reach out to the stakeholders, industries we serve and the public, being proactive in addressing and anticipating their needs.
- 6.2.1.3. Determine immediate, future, and long term facility and capital needs. TxDMV needs its own stand-alone facility and IT system as soon as possible. In connection with these needs, TxDMV shall identify efficient and effective ways to pay for them without unduly burdening either the state, its customers or stakeholders.
- 6.2.1.4. All regulations, enforcement actions and decision at TxDMV shall be made in a timely, fair and predictable manner.

6.2.2. Key Objective 2

Provide continuous education training on business trends in the industry with a particular emphasis on activities in Texas.

6.2.3. Key Objective 3

Provide continuous outreach services to all customers and stakeholders to access their respective needs and wants. This includes helping frame legislative or regulatory issues for consideration by other bodies including the legislature.

6.2.4. Key Objective 4

Examine all fees to determine their individual worth and reasonableness of amount. No fee shall be charged that cannot be defended financially and operationally.

6.3. GOAL 3 – Customer-centric

The TxDMV shall be a customer-centric agency that delivers today's services and decisions in a positive, solution-seeking manner while ensuring continuous, consistent and meaningful public and stakeholder involvement in shaping the TxDMV of tomorrow.

6.3.1. Key Objective 1

The TxDMV shall seek to serve its customer base through a creative and retail oriented approach to support the needs of its industries and customers.

6.3.2. Key Objective 2

The TxDMV shall develop and implement a public involvement policy that guides and encourages meaningful public involvement efforts agency-wide.

6.3.3. Key Objective 3

The TxDMV shall develop standard procedures for documenting, tracking, and analyzing customer complaint data. Successful problem resolution metrics should be monitored to support continuous improvement activities that shall permanently improve customer facing processes.

6.3.4. Key Objective 4

The TxDMV shall provide a formal process for staff with similar responsibilities to share best practices information.

6.3.5. Key Objective 5

The TxDMV shall provide central coordination of the Department's outreach campaigns.

6.3.6. Key Objective 6

The TxDMV shall develop and expand user friendly, convenient, and efficient website applications.

6.3.7. Key Objective 7

TxDMV shall timely meet all legislative requests and mandates.

Agency Operational Boundaries as Defined by Department Policies of the TxDMV Board (Board)

The Board is responsible for the policy direction of the agency. The Board's official connection to the day-to-day operation of the Texas Department of Motor Vehicles (TxDMV) and the conduct of its business is through the Executive Director of the TxDMV (ED) who is appointed by the Board and serves at its pleasure. The authority and accountability for the day-to-day operations of the agency and all members of the staff, except those members who report directly to the Board, is the sole responsibility of the ED.

In accordance with its policy-making authority the Board has established the following policy boundaries for the agency. The intent of the boundaries is not to limit the ability of the ED and agency staff to manage the day-to-day operations of the agency. To the contrary, the intent of the boundaries is to more clearly define the roles and responsibilities of the Board and the ED so as to liberate the staff from any uncertainty as to limitations on their authority to act in the best interest of the agency. The ED and staff should have certainty that they can operate on a daily basis as they see fit without having to worry about prior Board consultation or subsequent Board reversal of their acts.

The ED and all agency employees shall act at all times in an exemplary manner consistent with the responsibilities and expectations vested in their positions. The ED and all agency employees shall act in a manner consistent with Board policies as well as with those practices, activities, decisions, and organizational circumstances that are legal, prudent, and ethical. It is the responsibility of the ED to ensure that all agency employees adhere to these boundaries.

Accordingly, the TxDMV boundaries are as follows:

1. The day-to-day operations of the agency should be conducted in a manner consistent with the vision, mission, values, strategic framework, and performance metrics as established by the Board. These elements must not be disregarded or jeopardized in any way.
2. A team-oriented approach must be followed on all enterprise-wide decisions to ensure openness and transparency both internally and externally.
3. The agency must guard against allowing any financial conditions and decision which risk adverse fiscal consequences, compromise Board financial priorities, or fail to

show an acceptable level of foresight as related to the needs and benefits of agency initiatives.

4. The agency must provide timely, accurate, and honest information that will afford the Board, public, stakeholders, executive branch and the legislature the best ability to evaluate all sides of an issue or opportunity before forming an opinion or taking action on it. Any information provided that is intentionally untimely, inaccurate, misleading or one-sided will not be tolerated.
5. The agency must take all reasonable care to avoid or identify in a timely manner all conflicts of interest or even the appearance of impropriety in awarding purchases, negotiating contracts or in hiring employees.
6. The agency must maintain adequate administrative policies and procedures that are understandable and aid in staff recruitment, development and retention.
7. The agency must maintain an organizational structure that develops and promotes the program areas from an enterprise-wide perspective. No organizational silos or sub-agencies will be allowed. We are the TxDMV.
8. The agency must empower its entire staff to deliver a positive customer experience to every TxDMV customer, stakeholder or vendor to reduce their effort and make it easier for them to do business with the TxDMV.
9. The agency must at all times look to flattening its organizational structure to reduce cost as technology advances allow.
10. Agency staff shall anticipate and resolve all issues timely.
11. The agency must maximize the deployment and utilization of all of its assets – people, processes and capital equipment – in order to fully succeed.
12. The agency must not waste the goodwill and respect of our customers, stakeholders, executive branch and legislature. All communication shall be proper, honest, and transparent with timely follow-up when appropriate.
13. The agency should focus its work efforts to create value, make sure that processes, programs, or projects are properly designed, budgeted and vetted as appropriate with outside stakeholders to ensure our assumptions are correct so positive value continues to be created by the actions of the TxDMV.
14. The ED through his or her staff is responsible for the ongoing monitoring of all program and fiscal activities and providing information to the Board to keep it apprised of all program progress and fiscal activities. This self-assessment must result in a product that adequately describes the accomplishment of all program

goals, objectives and outcomes as well as proposals to correct any identified problems.

15. In advance of all policy decisions that the Board is expected to make, the ED will provide pertinent information and ensure board members understand issues/matters related to the pending policy decision. Additionally, the ED or designee will develop a process for planning activities to be performed leading up to that particular policy decision and the timeframe for conducting these planning activities. It is imperative that the planning process describes not only when Board consideration will be expected but also when prior Board consultation and involvement in each planning activity will occur.
16. In seeking clarification on informational items Board members may directly approach the ED or his or her designee to obtain information to supplement, upgrade or enhance their knowledge and improve the Board's decision-making. Any Board member requests that require substantive work should come to the Board or Committee Chairs for direction.
17. The agency must seek stakeholder input as appropriate on matters that might affect them prior to public presentation of same to the Board.
18. The agency must measure results, track progress, and report out timely and consistently.
19. The ED and staff shall have the courage to admit a mistake or failure.
20. The ED and staff shall celebrate successes!

The Board expects the ED to work with agency staff to develop their written interpretation of each of the boundaries. The ED will then present this written interpretation to the Board prior to discussion between the Board and ED on the interpretation. The Board reserves the right to accept, reject or modify any interpretation. The intent is that the Board and the ED will come to a mutually agreeable interpretation of agency boundaries that will then form the basis of additional written thought on the part of the ED and staff as to how these boundaries will influence the actions of the agency.