

1 NEW MOTOR VEHICLE BOARD
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CERTIFIED MAIL

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STATE OF CALIFORNIA
NEW MOTOR VEHICLE BOARD

In the Matter of the Protests of)	
HARBOR CITY ENTERPRISES, INC.,)	Protest No. PR-874-87
dba HARBOR CITY HARLEY,)	
HARLEY-DAVIDSON OF WESTMINSTER,)	
INC.,)	Protest No. PR-875-87
Protestants,)	
vs.)	<u>ORDER ADOPTING PROPOSED</u>
HARLEY-DAVIDSON, INC.,)	<u>DECISION AS MODIFIED</u>
Respondent.)	

TO: Margaret S. Henry, Esq., Patricia Takata, Esq.
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1 PAGE THIRTY-THREE OF THE Proposed Decision of
2 Administrative Law Judge in the above-entitled matter is hereby
3 modified to include the following:

4 e) There is no determination that the amount
5 Harley-Davidson pays the Protestants for parts used in the
6 performance of warranty work is reasonable.

7 As modified, the Proposed Decision is hereby adopted by
8 the New Motor Vehicle Board as its Decision in the
9 above-entitled matter.

10 This Decision shall become effective forthwith.

11 IT IS SO ORDERED THIS 29th day of November, 1988.

12 NEW MOTOR VEHICLE BOARD

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14
15 By Robert J. Beckus
16 ROBERT J. BECKUS
Vice-President

17 A. A. Pierce, Director, DMV
18 John Lancara, Acting Program Manager
19 Occupational Licensing, DMV

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STATE OF CALIFORNIA
NEW MOTOR VEHICLE BOARD

In the Matter of the Protests of)

Protest No. PR-874-87
Protest No. PR-875-87

HARBOR CITY ENTERPRISES, INC.,
dba HARBOR CITY HARLEY,

Protestant,

PROPOSED DECISION

vs.

HARLEY-DAVIDSON, INC.,

Respondent.

and

HARLEY-DAVIDSON of
WESTMINSTER, INC.,

Protestant,

vs.

HARLEY-DAVIDSON, INC.,

Respondent.

PROCEDURAL BACKGROUND

1. By letter dated February 18, 1987, Protestant Harbor City Enterprises, Inc., dba Harbor City Harley (Harbor City) filed a protest with the New Motor Vehicle Board (Board) pursuant to California Vehicle Code section 3065¹.

¹ All references are to the California Vehicle Code unless otherwise noted.

2. By the same letter dated February 18, 1987, Harley-Davidson of Westminster, Inc., (Westminster) also filed a protest pursuant to section 3065.

3. The Board assigned Protest Number PR-874-87 to the protest of Harbor City and Protest Number PR-875-87 to the protest of Westminster. Due to the existence of similar facts relating to the two protests the Board ordered the protests consolidated for purposes of hearing.

4. A hearing was held before Robert S. Kendall, Administrative Law Judge of the Board, commencing on November 16, 1987, and ending on February 25, 1988.

5. By agreement of the parties the record of the hearing remained open to receive additional evidence from the Protestants. The additional evidence from the Protestants was received on June 9, 1988. The parties requested additional time to submit closing briefs. The last brief was received by the Board on June 30, 1988.

6. Westminster and Harbor City were represented by Margaret S. Henry of Rosner, Owens, Nunziato and Henry. Harley-Davidson was represented by Allen S. Resnick of Paul, Hastings, Janofsky and Walker.

ISSUES PRESENTED

7. Whether Harley-Davidson adequately and fairly compensates the Protestants for labor and parts used to fulfill Harley-Davidson's warranty obligations;

A. Whether the *hourly compensation* rate that Harley-Davidson pays the Protestants for performance of warranty work is reasonable.

B. Whether the *time* allowed to perform warranty work is reasonable.

C. Whether *other conditions* of the warranty obligations are reasonable.

D. Whether the amount Harley-Davidson pays the Protestants for *parts* used in performance of warranty work is reasonable.

Section 3065 provides, in relevant part, as follows:

3065(a). Every franchisor shall properly fulfill every warranty agreement made by it and adequately and fairly compensate each of its franchisees for labor and parts used to fulfill such warranty when the franchisee has fulfilled warranty obligations of repair and servicing and shall file a copy of its warranty reimbursement schedule or formula with the board. The warranty reimbursement schedule or formula shall be reasonable with respect to the time and compensation allowed the franchisee for the warranty work and all other conditions of such obligation. The reasonableness thereof shall be subject to the determination of the board; provided that a franchisee files a notice of protest with the board. (emphasis added)

FINDINGS OF FACT

A). Whether the *Hourly Compensation Rate* That Harley-Davidson Pays the Protestants for Performance of Warranty Work Is Reasonable. {Section 3065(a)}

8. Beginning with all 1980 model year vehicles, Harley-Davidson has reimbursed its dealers for warranty labor at 100% of the dealer's certified retail labor rate as claimed by each dealer.

9. Harley-Davidson dealers may recertify their retail labor rate once each calendar year by submitting a new Certificate of Retail Labor Rate.

10. Harley-Davidson has never refused to pay a dealer in accordance with the dealer's certified rate.

11. The average retail labor rate among Harley-Davidson dealers nationwide is approximately \$30 per hour. The average retail labor rate is higher in California, and in many dealerships it is in excess of \$40 per hour. Westminster currently charges \$49.50 per hour, and Harbor City charges \$45.00 per hour. These are the rates Harley-Davidson pays to these dealers for warranty labor.

Facts Relating to Warranty Work on Harley-Davidson
Motorcycles at Harbor City and Westminster

12. Both Westminster and Harbor City give warranty work top priority. They have never refused to perform warranty work.

13. Expert witnesses were called in behalf of Harley-Davidson and the Protestants to testify as to the profitability, or lack thereof, of each dealership's service department in regard to warranty work. The experts reached opposite results.

14. This diametrically opposed testimony is recognized as expert opinion only, and is not binding on the trier of fact. Both experts used, for all practical purposes, the same dealer generated accounting figures; both used generally accepted accounting principles, but arrived at opposite conclusions based

on differing methodology. Because the expert opinions expressed contradict each other, neither opinion is relied upon by the finder of fact in the decision reached hereafter.

15. Harbor City's retail labor rate is \$45.00 per hour. On non-warranty service work, it also charges an additional 5% of the cost of labor (maximum \$10 per repair order) for shop supplies and miscellaneous expenditures. This amounts to an effective labor rate of \$47.75 on retail service of 4.4 hours or less. Harbor City does not reflect the 5% surcharge in its retail labor rate certification to Harley-Davidson.

16. Beginning on August 1, 1986, Westminster certified to Harley-Davidson that Westminster's retail labor rate was \$49.50 an hour. Harley-Davidson paid Westminster at that rate for warranty labor performed despite the fact that Westminster's actual retail labor rate was \$48.00 per hour. Westminster subsequently corrected its certified rate.

17. The actual amount of legitimate warranty labor compensation paid by Harley-Davidson to Westminster is not ascertainable because, during certain periods in question, Westminster was reimbursed for an unascertained number of warranty claims submitted for motorcycles that did not, in fact, require or receive warranty repair. In some instances, Westminster personnel would sell custom, and other parts, and/or perform non-warranty repairs for retail customers and submit warranty claim forms which charged Harley-Davidson for the labor expense to install these parts. Harley-Davidson unknowingly,

and in reliance on the certification on the claim form, would pay for this work when in fact no warranty work was required, or performed, on these motorcycles.

18. Westminster also submitted, and was paid by Harley-Davidson, for claim forms which on their face appeared legitimate but in fact were for off-road racing carburetors the installation of which violated California and federal emission control standards. Harley-Davidson at the time these warranty claims were submitted and paid, was unaware of the impropriety of the warranty claims and the true nature of the parts being installed.

19. Westminster's current retail labor rate is \$50 per hour which is the amount Harley-Davidson reimburses Westminster for warranty labor. In addition, Westminster charges non-warranty retail customers 6% of the cost of labor (maximum \$25 per repair order) to cover shop supplies and miscellaneous items. Thus, Westminster charges retail customers at an effective rate of \$53 per hour for labor for the first 8.3 hours of labor per repair order. Westminster did not include the 6% surcharge in its retail certification rate to Harley-Davidson.

B). Whether the Time Harley-Davidson Allows
Protestants to Perform Warranty Work Is Reasonable.
{Section 3065(a)}

20. Harley-Davidson has 630 dealerships nationwide and maintains a uniform national policy covering warranty reimbursement.

21. Harley-Davidson's warranty for new vehicles extends for 12 months from the date of purchase. A purchaser can take his vehicle to any franchised Harley-Davidson dealer in the United States for warranty work although he is encouraged to take the vehicle to the selling dealer.

22. The total amount of compensation payable on a warranty claim for labor is determined by the time allowed for the repair, as established by a flat rate, multiplied by the dealer's certified retail labor rate.

23. Harley-Davidson has created and published a flat rate manual which is distributed to all its dealers. The dealers use this manual for both retail and warranty work. A flat rate is a set amount of time assigned by Harley-Davidson to perform a particular mechanical or electrical repair or adjustment. Time is calculated in six-minute increments, or 1/10th of an hour. Prior to the introduction of flat rates in the mid-1970's, Harley-Davidson solicited its initial estimates for the times needed to accomplish each repair or adjustment from its dealers through phone contacts and field visits by service representatives.

24. Harley-Davidson updates and revises its flat rate times on a continuing basis. Changes in the flat rate are applied to current warranty claims being processed, but are not reflected in the manual until it is re-issued for the new model year. Revisions occur in response to product changes as well as from requests from dealers who demonstrate that a given time is

inadequate to effect the repair. The 1986 flat rate manual contained 446 changes from the 1985 manual. Seventy-four per cent of these changes were increases in the times allotted to perform specific warranty repairs.

25. Harley-Davidson's Milwaukee headquarters maintains a service and repair facility which is set up like a service department of a typical motorcycle dealership. Factory mechanics review the flat rate times by performing regular repair and maintenance of Harley-Davidson company vehicles in the facility.

26. When establishing or performing a review of a flat rate operation, Harley-Davidson factory mechanics perform the particular job twice to ensure the completeness and accuracy of the time allocation. The first operation is not timed and is used primarily by the mechanic in order for him to become familiar with the procedure. The time adopted in the manual results from performance of the second procedure. The factory mechanics who perform the flat rate operation round-off upward the actual time clocked to the nearest tenth of an hour. Stop watches are not used and the mechanics do not attempt to "race the clock" to shorten the flat rate time.

27. In contrast to many dealerships, Harley-Davidson factory mechanics perform the flat rate operations using only hand tools, rather than power tools.

28. Proposed flat rate times are rounded up to allow a factor for diagnosis, obtaining parts and tools, road testing, and for completing the claim forms. Harley-Davidson establishes

its flat rate times on the basis of 80% mechanic efficiency, i.e., the assumption that 80% of the mechanic's available time is spent on hands-on tool use performing the actual repairs.

29. The speed and accuracy with which a mechanic can perform within a flat rate time is dependent upon his skill, product knowledge and training.

30. Because the climate of Southern California is conducive to year-round motorcycle usage, a higher percentage of full-time riders need year-round, rather than seasonal service. This results in the Southern California dealers generally being able to retain employees on a year-round basis more so than dealers in other areas of the country.

31. At least six months is required for a qualified mechanic to become accustomed to the operations of a given dealership and achieve maximum efficiency. Harbor City has had a high turnover rate of employees. During the fiscal year ending April 30, 1987, seventeen different individuals were employed in the Harbor City service department as mechanics, service writers, or service manager. Other than the service manager, only one employee, a mechanic, was employed for the full twelve months during fiscal year 1987. No other person in the service department was employed for more than six months, and five mechanics and two service writers were employed for two months or less.

32. Each Harbor City mechanic spends approximately one hour of non-billable time per day moving motorcycles out of and back into the shop. On the average, the Harbor City mechanics

bill only 4.1 hours per day or 54% of the billable time available to them in a working day.

33. Westminster lacks adequate, handy storage space for motorcycles waiting for repair, or that have been repaired. Mechanics often have to move as many as six vehicles in order to get to the motorcycle that is to be worked on next. A significant loss of the mechanics' productive billable time results from this activity.

34. In lieu of road tests, Harbor City uses a dynamometer to test repaired motorcycles and to diagnose those needing repair. Use of the dynamometer is intended to reduce the potential for accidents which can and have occurred during road tests.

35. Because of this method of testing, Harbor City has sometimes experienced difficulty in diagnosing mechanical problems. It takes more time for Harbor City mechanics to diagnose and locate specific problems because road tests are the most efficient means to diagnose mechanical problems.

36. On estimates given to retail customers, Harbor City's Service Manager routinely doubles the flat rate time to provide for possible unforeseen or unanticipated later problems, and to avoid follow-up telephone calls to the customer when it is found that more time will be needed.

37. Suggested time adjustments to Harley-Davidson's flat rate manuals were submitted by the Protestants to Harley-Davidson. The proposals were prepared by Jim Wismer the

Westminster owner, his service manager Dennis Arrout, and by Harbor City's service manager Edward Pynn. Each manual had flat rate times allowed for certain warranty repairs lined out, and new proposed times substituted to indicate the actual times each of the three individuals had concluded were needed to perform the tasks.

38. No evidence was offered by the Protestants to demonstrate why it was not possible to complete any or all of these specific tasks cited within the times established by Harley-Davidson. No evidence was offered that actual timed tests under shop conditions had been conducted concerning the challenged procedures to justify the new suggested times. The new proposed flat rate times set out by the Protestants are estimates based wholly on the mixed expert/lay opinion of each proponent. Protestants offered no direct evidence to support their contentions that additional time was needed for completion of the specific jobs challenged. No evidence was presented that Protestants conducted controlled, supervised tests duplicating the methodology used by Harley-Davidson which would demonstrate that Harley-Davidson's methodology was flawed, self-serving or in any manner illogical, or not achievable.

39. The total additional time claimed by Wismer, Arrout and Pynn in their opinions, expressed as a percentage of total

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time in the flat rate manual, is indicated below.

Additional Percentage of Flat Rate Time Allegedly
Required to Perform Repairs

<u>Motorcycle Model</u>	<u>Westminster Wisner</u>	<u>Westminster Arrout</u>	<u>Harbor City Pynn</u>
BJL	8.7%	2.6%	20.2%
BHL/BKL	8.6%	7.3%	21.0%

40. The amount of increased flat rate times requested by Pynn at Harbor City includes additional time to check other potential problems that do not ordinarily arise directly in connection with the particular job code in question. Harbor City does not charge retail customers separately for administrative or diagnostic time.

41. Approximately one-third of the flat rate times marked as inadequate by Wisner of Westminster had not been performed as warranty work by Westminster on either 1986 or 1987 model year motorcycles, nor during the last 30 months prior to the protest. Approximately one-quarter of the flat rate times marked for increases had been used only once by Westminster in warranty repairs.

42. Of the flat rate times marked by Pynn at Harbor City, approximately one-half had never been claimed for warranty work, and approximately one seventh had been used only once for either 1986 or 1987 model year motorcycles in the last thirty months prior to the protest.

43. On January 1, 1986, Harley-Davidson's warranty policy was changed to give an additional .1 hour (six minutes) labor credit on all warranty claims with a cumulative labor total of .3 hours (18 minutes) or less. The credit is applied automatically whenever a claim of .3 hours or less is submitted, and is identified on the credit memo as administrative time.

44. While it is Harley-Davidson's stated policy not to allow this additional credit on subsequent claims of .3 hours or less for repairs performed on the same vehicle within one week, in practice Harley-Davidson has paid the additional .1 hour of credit regardless of the number claims submitted for the same vehicle within a one week period.

45. As of February 1988, Westminster and Harbor City had received the automatic .1 hour administrative labor credit a total of 166 and 93 times respectively. Based on current labor rates of both dealers this represents an additional compensation of \$821 to Westminster and \$418 to Harbor City.

46. Harley-Davidson maintains a procedure for dealers to request permanent changes in flat rate times. Dealers may request an increase in existing flat rates, or establish a new flat rate for a job not currently covered in the flat rate manual, by submitting a factory form setting out the reasons for the particular change.

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C). Whether Other Conditions of the Warranty Obligation are Reasonable. {Section 3065(a)}

47. Harley-Davidson has authorized at least ten factory individuals to grant additional warranty credits when requested by a dealer for a specific warranty problem. These include technical specialists, technical instructors, field service representatives, service managers and the director of service. The Harley-Davidson technicians are required to give reasonable consideration to the additional time requested.

48. When the technician determines that the challenged flat rate time is adequate, he is required to explain the reasons why he so concludes, and attempt to provide the dealer's mechanic with a better procedure or methodology to follow in order to perform the repair within the established flat rate time. In these situations, Harley-Davidson ordinarily gives the dealer a time credit on the specific warranty claim to compensate for the time spent by the mechanic in dealing with the factory concerning the problem.

49. Harley-Davidson maintains a procedure by which additional labor compensation can be claimed in the event a mechanic is unable to perform an operation within the flat rate time or because of a problem peculiar to a specific warranty repair to a vehicle. The dealer, or service manager, may telephone the factory to request additional compensation, or alternatively, may request the increase on the warranty claim form, explaining in detail the specific problem and why extra time was required in the special circumstances.

50. The Harbor City service manager conceded that factory personnel are reasonable and fair in granting additional warranty labor compensation.

51. Both Westminster and Harbor City have received extra compensation for specific warranty claims through phone requests and by requests made on warranty claim forms. Extra compensation in one instance was given to Harbor City because of a warranty repair that was misdiagnosed by a Harbor City mechanic.

52. Westminster has received additional compensation for warranty work caused by mechanic's error. In one instance, a Westminster mechanic ruined an engine while attempting to perform warranty work. Not only did Harley-Davidson pay for the unsuccessful repairs, Harley-Davidson also authorized and paid for a new replacement engine which was necessitated by Westminster's improper repairs.

53. Harley-Davidson's general policy is to reject dealer warranty claims over one year old. However, in February 1985, Harbor City claimed and received warranty credit on warranty claims that originated in 1983. Westminster has also received additional compensation for warranty claims submitted past the one year deadline.

54. Harbor City and Westminster claimed and received total additional credits of 35.8 and 96.6 labor hours, respectively, for warranty labor compensation for 1984 and 1985 motorcycles. The amounts below set out the extra amounts claimed and received

beyond regular warranty compensation claims paid:

	<u>HARBOR CITY</u>		<u>WESTMINSTER</u>	
	<u>Hours</u>	<u>\$\$</u>	<u>Hours</u>	<u>\$\$</u>
1984 model year	17.6	797.00	68.5	3390.75
1985 model year	<u>18.2</u>	<u>819.00</u>	<u>28.1</u>	<u>1390.95</u>
Total	35.8	1616.00	96.6	4781.70

55. Warranty reimbursements paid to the Protestants by Harley-Davidson compared to the national average for the 1985 model year were as follows.

	<u>Parts % of National Average</u>	<u>Labor % of National Average</u>	<u>Labor Hours Per Unit % of National Average</u>
Harbor City	130	254	162
Westminster	314	601	350

56. During the most recent fiscal years for which figures were presented Harbor City received total warranty reimbursements of \$9,887, and Westminster received \$22,141. The \$1,616 and \$4,781 of additional compensation shown in Finding 54 thus represent approximately 16% (Harbor City) and 21% (Westminster) respectively of the total warranty compensation received by the Protestants.

57. Harley-Davidson's Los Angeles and Orange County dealer network received additional warranty labor credits totaling 193.4 labor hours for 1984 models and 176.8 labor hours for 1985 model year motorcycles. This equals a total of 370.2 labor

NUMBER OF WARRANTY ADJUSTMENTS AUTHORIZED BY HARLEY-DAVIDSON

DEALER	1984 MODEL YR.	1985 MODEL YR.	1986 MODEL YR.	TOTAL
Harbor City	1	2	7	10
Westminster	14	8	7	29
<u>LA COUNTY</u>				
- Canoga Park	1	3	3	7
- Culver City	1	2	7	10
- Glendale	6	4	6	16
- Inglewood	-	1	-	1
- Lancaster	-	-	-	-
- Palmdale	-	1	-	1
- Rosemead	5	3	10	18
- Van Nuys	1	7	5	13
- Whittier	4	1	-	5
<u>ORANGE COUNTY</u>				
- Fullerton	8	1	5	14
- Santa Ana	0	1	5	6
<u>NATIONAL</u>	1725	1545	1846	5116

59. Harley-Davidson maintains technical service schools in Milwaukee and in Phoenix. Harley-Davidson pays for room, board and tuition for the two week program, but does not pay for travel expense, or employee salary.

60. Under the terms of the franchise agreement, each dealer is obligated to employ at least one full-time mechanic who has attended either of the Harley-Davidson technical service schools within the past 3 years. Dealers are encouraged by Harley-Davidson to send as many service personnel as possible to the schools. Harbor City's service manager is the only Harbor City employee who has attended the school. Because his attendance was in 1982, Harbor City is not in compliance with its franchise requirements.

61. At Westminster, Wismer is the only person who has attended a Harley-Davidson technical school. However the last time he attended was in 1972. Wismer concedes that the service school would be of benefit to his mechanics and to the dealership, but he has refused to send his mechanics to the school. One Westminster mechanic was not permitted by Wismer to attend the school even though he offered to use his own vacation time, as well as provide his own transportation to and from Phoenix.

62. Harley-Davidson provides an in-house service training program at no cost to dealers. The program consists of microfiche, audio tapes, and video tapes and provides a means to update mechanics on product changes, new mechanical procedures, specific tool usage, and trouble shooting new problems.

63. Approximately 540 dealers nationwide, or 85% of the Harley-Davidson dealer network, participate in the program. Dealers who participate in the program also are afforded the opportunity to send their mechanics to a service school every second year, rather than every third year under the regular franchise requirements.

64. Harley-Davidson regularly schedules one-day local schooling seminars in Southern California to update mechanics and service managers on recent mechanical developments, recurring problems, and the latest repair procedures. Both Harbor City and Westminster service personnel attend these seminars.

65. Harley-Davidson has developed a program to assist dealers in increasing and upgrading service department efficiency and profitability. Over 250 dealers in the United States have participated voluntarily in the program, including every dealer in California except two. Harbor City is one of the two which declined to participate.

66. As part of the program, a dealership service department efficiency percentage is calculated by analyzing each dealership's service operation for certain criteria and by dividing the actual number of mechanic hours billed by the billable hours available. The resulting efficiency number, expressed as a percentage, is a significant indicator of the level of service and efficiency provided by a dealer's service department, and has been found to correlate with the service department's profitability, or lack thereof.

67. The Harley-Davidson representatives conducting the program attempt to increase the total amount of available time a dealer can "bill" customers for its mechanic's labor. From national results, Harley-Davidson found that dealers whose service department maintained high levels of Harley-Davidson school training, regular and special tools, and an efficient and well organized shop layout, generally show a service department profit. Dealers whose service department efficiency numbers fall within the 70-80% range tended to accomplish both regular and warranty repairs within the flat rate time established by the factory.

68. Inasmuch as Harbor City did not participate in the profitability program, it is not possible to determine its efficiency number.

69. Westminster participated in the Harley-Davidson program in June 1985 and February 1987. Its efficiency numbers were calculated to be 60% and 72% respectively.

70. Two Northern California Harley-Davidson dealers had their service departments efficiency analyzed under the same program as Westminster. The Sacramento dealer's efficiency percentage was calculated to be 72-74% and the Stockton dealer maintained a 70% efficiency rating. These dealers had profitable service departments and their mechanics were able to perform service and warranty repairs within the flat rate times in approximately 80-90% of the jobs done. Both these dealerships' mechanics were factory trained pursuant to the requirements of the Harley-Davidson franchise agreement.

D) Whether the Amount Harley-Davidson Pays for Parts Used in Performance of Warranty Work Is Reasonable. {Section 3065(a)}

71. Harley-Davidson reimburses its dealers for warranty parts used in warranty work at dealer cost plus 10%. Dealer cost is the price of the part to the dealer as listed in the most current Harley-Davidson price book regardless of when the part was purchased by the dealer from Harley-Davidson.

72. In 1984, Harley-Davidson established a special task force for the specific purpose of resolving problems which had arisen in its relationship with its California dealers. The task force was composed of Harley-Davidson management personnel and representatives of both the northern and the southern California Harley-Davidson dealers' associations. The task force, at the request of several participating dealers, investigated the issue of warranty reimbursement for parts to determine whether 10% over dealer cost was adequate to reimburse dealers for parts required by them to perform warranty work.

73. Harley-Davidson subsequently issued its task force report to all California dealers. The report concluded that, on average, California dealers incur the following costs related to warranty parts:

<u>Freight</u>	<u>Inventory</u>	<u>Handling</u>
2.9%	5%	1%

As Harley-Davidson pays its dealers 10% above the dealer cost of the part, Harley-Davidson concluded that these figures leave an additional 1.1% for the dealer to apply to general overhead and administrative costs. The dealer organization disputed these conclusions. No evidence was offered that the dealers thereafter submitted figures to establish why their organizations disagreed with Harley-Davidson's estimates, or that established other figures as a basis for cost allocations.

74. Westminster failed to establish a more precise figure for its costs of handling parts, including warranty parts. Westminster does not include in its financial statements figures showing its cost of unpacking and shelving because of the owner's conclusion that the actual costs thereof are not material enough to justify the extra bookkeeping costs each month to generate such figures.

75. Westminster sells genuine Harley-Davidson parts to its employees at dealer cost plus 10%. Employees were told that the 10% over dealer cost was necessary to recover costs of shipping, handling and stocking. The employees were also informed that the dealership broke even and did not lose money on parts sold to them at cost plus 10%.

76. It is not possible to ascertain accurately the actual amount, or total volume of genuine Harley-Davidson parts used in warranty work by Westminster because Westminster regularly and routinely used non-Harley-Davidson after-market parts in warranty work, despite the requirement that only genuine

Harley-Davidson parts be used. Westminster, in such instances, routinely submitted warranty claim forms for reimbursements which showed genuine Harley-Davidson parts numbers despite its use of non-Harley-Davidson parts. Harley-Davidson had no knowledge of this practice and unwittingly paid the claims as submitted. These after-market parts generally cost the dealer less than genuine Harley-Davidson parts, and therefore Westminster's margin on warranty parts overall is higher than if genuine Harley-Davidson parts had been used.

77. Harley-Davidson's policy is that parts orders totaling less than \$50 ordinarily carry a \$10 surcharge. However, the surcharge is waived if the order is for warranty work, or needed for a vehicle which is inoperable due to the unavailability of a part.

78. Harley-Davidson reimburses dealers for lubricants only when they are contaminated as a result of the defect which necessitated the warranty repair. Both Harbor City and Westminster have received substantial warranty reimbursements for fluids and lubricants despite their contentions to the contrary. Often replacement lubricants have been added by Harley-Davidson to Harbor City's and Westminster's warranty claims when the dealerships failed to claim for them and to do so would have been proper.

79. In some instances, when high-demand parts ordered for warranty work are not readily available, Harley-Davidson will authorize the dealer to use as a replacement, the next highest

assembly and will reimburse the dealer for the parts and labor involved.

80. Dealers can further reduce Harley-Davidson's estimated 7.9% freight and inventory costs for warranty parts by using Harley-Davidson's policy developed to encourage large parts orders from its dealers. This program, referred to as "Free Freight", is applicable to all parts orders of \$495 or more. Harley-Davidson ships the orders freight prepaid to a major flight center, such as Los Angeles International Airport. Free Freight applies whether or not the parts ordered are shipped from different locations or are shipped sequentially because of back orders or shortages. The dealerships must arrange and pay for moving the freight from the airport, thus incurring some expense for freight costs.

81. The majority of parts ordered by both Westminster and Harbor City are shipped by Harley-Davidson under the Free Freight program.

82. Harley-Davidson also provides a "Trade Acceptance" program whereby Harley-Davidson dealers can further lower parts costs. Under the program, dealers are encouraged to place large orders for parts and accessories early each year with payment deferred for as long as seven months. No finance charges are incurred by the dealer in the interim. Early payment entitles a dealer to discounts of up to 7%. Trade Acceptance orders also qualify for the Free Freight program.

83. Harley-Davidson dealers who take advantage of the maximum 7% Trade Acceptance program discount and order parts which subsequently find their way to warranty work are thus reimbursed for those warranty parts at dealer cost plus 17% rather than dealer cost plus 10%.

84. Harbor City's Trade Acceptance orders generally have consisted of 50% mechanical parts ("hard parts") with the balance in accessories. Westminster also orders a substantial volume of hard parts under Trade Acceptance.

85. Harley-Davidson also extends a 2% net 15 days parts order discount. If dealers make payment on parts orders within 15 days of the receipt of the invoice, they can take a 2% discount. If this program is used, dealers are reimbursed in the amount of 12% above the actual cost of such parts later used in warranty work.

86. Harbor City attempts to take advantage of the 2% net 15 days program as often as possible. There was no evidence presented as to Westminster's participation in this program.

87. Harley-Davidson absorbs the excess cost in instances where the cost of freight for shipping very large parts, such as frames or fairings, may exceed the 10% over dealer cost reimbursement figures. In these special cases Harley-Davidson compensates the dealer for the 10% over dealer cost and also reimburses the dealer for the actual difference between the cost of freight for the large part and the dollar amount represented by the 10%.

Facts Relating to Other Benefits to Dealers
in Connection With Performance of Warranty

88. Performance of warranty work provides dealers additional opportunities to sell accessories and custom parts to new owners. Westminster sells large quantities of chrome accessories to its customers when their motorcycles are in the shop for warranty repairs. It is the experience of dealers that customers who return for warranty service will often purchase additional products such as clothing and motorcycle accessories while waiting for their repairs to be completed.

89. Both Harbor City and Westminster concede they benefit from warranty work because of the potential for sale of custom parts and accessories to warranty customers.

Facts Relating to Motorcycle Industry
Standards for Warranty Reimbursement

90. The Japanese manufacturers, (Honda, Kawasaki, Suzuki and Yamaha) control 97% of U.S. motorcycle sales. Harley-Davidson accounts for approximately 1% of the U.S. motorcycle market.

91. Kawasaki, Suzuki and Yamaha reimburse their dealers for parts used in warranty work at dealer cost plus 10%.

92. Honda reimburses its dealers for warranty parts at dealer cost plus 25%. Honda dealers carry larger parts inventories due to the large numbers of models produced by Honda. Honda parts and motorcycle models change constantly and

have a lower percentage of interchangeability between model years generally than its competitors. Harley-Davidson parts have a higher degree of interchangeability between models than Japanese motorcycles. Harley-Davidson dealers can service the full range of Harley-Davidson motorcycles from a relatively small parts inventory.

93. The Honda parts book has 710 pages with each page listing approximately 180 line items. The Harley-Davidson parts book has 174 pages listing approximately 120 line items per page.

94. Honda, until 1987, refused to pay its dealers more than \$40 an hour for warranty labor. This policy was maintained regardless of the dealer's prevailing labor rate.

95. Suzuki and Yamaha consider various criteria, including the dealer's retail labor rate, to establish the warranty reimbursement rate. The Suzuki criteria includes the amount and method used to pay the productive service personnel and the prevailing labor rate in the dealer's geographical area. Various other criteria, including training of mechanics, could affect the Suzuki warranty reimbursement rate. Requests from Suzuki dealers for increases in their warranty labor rate must meet Suzuki's hourly warranty labor rate policies. Suzuki also verifies each change in the warranty labor rate by sending out a technical advisor to the dealership. In order to be approved, a Yamaha dealer's rates must be competitive as compared to other Yamaha and non-Yamaha dealers in the area.

96. Only Kawasaki reimburses dealers for warranty labor at each dealer's retail labor rate in the same manner as Harley-Davidson.

97. In 1987, J. D. Power and Associates conducted a Dealer Attitude Survey designed to compare how motorcycle manufacturers were perceived by their dealer organizations. The survey, which was sent to 4,300 motorcycle dealers across the country, included four questions expressly addressing warranty reimbursements. Dealer reaction was sought in connection with:

- 1) labor rate allowance for warranty work,
- 2) parts rate allowance for warranty work,
- 3) fair settlement of warranty claims, and
- 4) prompt payment of warranty claims.

98. Each dealer rated each of the brands sold by it on a four point scale using only one of the following four answers:

- 1) very acceptable,
- 2) somewhat acceptable,
- 3) somewhat unacceptable, and
- 4) very unacceptable.

All responses were scored and all scores were weighted to compensate for differences in sampling response size and to adjust for the differences in size of each manufacturer's dealer network.

99. In the survey Harley-Davidson dealers gave Harley-Davidson an average score that fell between "very acceptable" and "somewhat acceptable" for the warranty labor

rate allowed. There was far more dealer satisfaction with Harley-Davidson's labor rate allowance on warranty work than there was dealer dissatisfaction.

100. In terms of parts allowance for warranty work, Harley-Davidson dealers generally were more satisfied than dissatisfied with Harley-Davidson's allowance. Harley-Davidson scored slightly higher in this category than the Japanese manufacturers.

101. In the category of "fair settlement of warranty claims and prompt payment of claims," Harley-Davidson dealers rated Harley-Davidson significantly higher than every Japanese brand. Harley Davidson dealers found Harley-Davidson's policy in these two areas were far more than "somewhat acceptable".

102. In addition to the four warranty questions, the J. D. Power survey included three questions regarding issues that are indirectly related to warranty reimbursement in that the questions tend to reflect the level of support from the factory to the dealers in connection with warranty and other service work. These questions dealt with:

- (i) service training seminars/schools,
- (ii) technical support to service department, and
- (iii) usefulness of service manuals.

In each of these three categories, Harley-Davidson dealers rated Harley-Davidson significantly higher than every Japanese line dealer rated his manufacturer.

Facts Related to Harbor City and Westminster
Service Departments

103. Service department efficiency at Westminster has been adversely affected by an inadequate supply of replacement parts on hand. In some instances, Westminster mechanics have had as many as ten to twelve repair orders pending, or partially completed, because parts were not available. On some occasions up to fifty percent of the warranty repair orders at Westminster could not be completed because parts were out of stock or were on order, or back order. This is true even though Westminster used significant amounts of after-market parts in its repairs and in some instances used non-Harley-Davidson parts in warranty repairs.

104. Financial constraints have also affected the efficiency and productivity of Westminster's mechanics in that the dealership's service department lacks detailed organization, is inadequate in some respects, and lacks certain specialized tools.

105. Some of Westminster's financial constraint is caused by low working capital. In the past this problem has caused Westminster to postpone or delay the ordering of parts and to reduce the quantity of parts ordered and stocked.

106. In recent years, Westminster has had problems meeting its past due accounts payable to Harley-Davidson for parts orders. On at least one occasion, it has been put on a special credit hold program whereby parts orders are released on a

C.O.D. basis only when Harley-Davidson receives part payment of some of the past due parts accounts.

107. Westminster sells genuine Harley-Davidson parts and accessories at retail prices in excess of Harley-Davidson's suggested retail prices. This practice is common with many Harley-Davidson dealers.

108. Normal practice in the motorcycle industry generally is to carry an average annual parts and accessories inventory equal to approximately 40% to 60% of the cost of sales of parts and accessories during that year. The Harbor City parts and accessories inventory for the fiscal year ending April 30, 1987 was 76% of the cost of sales. The Westminster parts and accessories inventory for the fiscal year ending December 31, 1986 was 25% of the cost of sales.

109. Neither Harbor City nor Westminster provided any evidence of capital expenditures or fixed costs incurred solely for the purpose of enabling them to perform warranty work. There was no evidence that either dealership had to set up extra service bays, or procured extra supplies, tools or personnel, or made any direct or indirect fixed expenditures in order to fulfill warranty requirements.

DETERMINATION OF ISSUES

Protestants have failed to establish that Harley-Davidson does not adequately and fairly compensate the Protestants for labor and parts used to fulfill Harley-Davidson's warranty obligations in that:

a) Protestants have failed to prove that the *hourly compensation* paid by Harley-Davidson is not reasonable;

b) Protestants have failed to prove that the *time* allowed to perform warranty work is not reasonable;

c) Protestants have failed to prove that the *other conditions* of the warranty obligation are not reasonable;

d) Protestants have failed to prove that the amount Harley-Davidson pays the Protestants for *parts* used in the performance of warranty work is not reasonable.

The following decision is respectfully submitted:

The protests are overruled.

I hereby submit the foregoing which constitutes my proposed decision in the above-entitled matter, as a result of a hearing held before me on the above dates and recommend adoption of this proposed decision as the decision of the New Motor Vehicle Board.

Dated: August 29, 1988



ROBERT S. KENDALL
Administrative Law Judge
New Motor Vehicle Board