the Myers & Fuller, P.A. report

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Leveling the playing field between automobile dealers and manufacturers for over 20 years.

Inside

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Introducing the Myers & Fuller Report

a newsletter for motor vehicle dealers and associations

Welcome to the second edition of the Myers & Fuller Newsletter. We intend for our newsletter to be published quarterly for use by motor vehicle dealers, dealer associations and their advisors in keeping abreast of challenges facing dealers across the United States.

Myers & Fuller has been representing automobile, truck and motorcycle dealers and dealer associations for over 20 years in disputes with manufacturers and consumers. Our practice includes counseling dealers on matters such as buy-sell transactions, terminations, relocation and addition of competing dealerships, finance and insurance, warranty and sales incentive audits, improper allocation, transfer turndowns, market realignments, internet sales, site control, exclusivity, environmental cleanup and consumer class action lawsuits. In addition to our litigation services, we assist numerous dealer associations in crafting franchise law solutions to the many manufacturer, finance and insurance as well as consumer challenges facing dealers. Lastly, we provide our clients with onsite finance and insurance compliance audits which includes reviewing and recommending changes to processes and forms used at the dealership.

Our goal with the Newsletter is to provide you up-to-date information on new developments in manufacturer initiatives, finance and insurance challenges and consumer claims. We will include articles on broad topics affecting dealers as well as specific discussion on the outcomes of our manufacturer and consumer disputes.

We hope you will find the Newsletter to be a valuable resource. Please do not hesitate to contact us with questions on any topic we cover or with suggestions on how to improve the Newsletter.

Richard N. Sox, Jr.
Managing Partner

News Brief

Dealers and Dealer Associations Push Back Against VW and Audi's New Program

PRIOR TO THE NATIONAL AUTOMOBILE DEALER ASSOCIATION ANNUAL MEETING IN LAS VEGAS EARLIER THIS YEAR, MYERS & FULLER WAS CONTACTED BY A NUMBER OF OUR VW CLIENTS AND DEALER ASSOCIATION CLIENTS QUESTIONING THE LEGALITY OF THE NEWLY ANNOUNCED VW INCENTIVE PROGRAM. This program called for VW to holdback an additional 1% to be paid to the dealer only after certain criteria were met. These criteria included sales performance and facility upgrades. This program looked an awful lot like the Ford Blue Oval program that our partner, Shawn Mercer, successfully challenged as a violation of price discrimination laws. Upon further review, we recommended that VW dealers and Dealer Association executives strongly object to this program as a violation of federal and State price discrimination prohibitions. We assisted our clients in writing letters to VW and in creating talking points to use in discussions with VW officials at the NADA convention.

We are happy to report that VW has backed off of this program and, as we understand it, changed the terms of the program substantially.

Similarly, over the last couple of months, Audi has rolled out its R8 allocation program. The R8 is a hot new vehicle being produced by Audi and which is set for distribution in the next few months. We were shocked to learn that instead of simply allocating these vehicles to its dealers as would be done with any other new model, Audi had informed dealers that in order to receive a "full" allocation of R8s they would be required to, among other things, pay $100,000 to Audi for the privilege. This payment was supposedly to offset training costs, etc.

Again, we assisted several of our Audi clients and Dealer Association clients write letters objecting to R8 allocation program as being a violation of State franchise protections. As a result of the efforts on the part of these dealer and Association executives, Audi has drastically curtailed its requirements for a dealer to receive the new R8.

News Briefs

Impact of the Sale of the Chrysler Division on Dealers

SINCE HEARING OF THE RUMORS THAT THE CHRYSLER DIVISION MAY BE FOR SALE, THE ATTORNEYS AT MYERS & FULLER HAVE BEEN BUSY THINKING AND WRITING ABOUT HOW THIS MAY IMPACT THE DIFFERENT PARTIES INVOLVED. Soon after learning of the potential sale of Chrysler Division, our first thoughts turned to the Chrysler, Dodge and Jeep dealers.

The rumors turned from the sale of the Chrysler Division to a third party to specific discussion that General Motors was in talks to acquire the Division. It became quickly obvious to us that some significant number of dealers could be eliminated in such a transaction. This could be either Chrysler, Dodge and Jeep dealers, General Motors dealers such as Pontiac, Buick and GMC dealers or a combination of the two. There is little chance that General Motors would want to increase the size of its dealer network in these times of downsizing and consolidation of their existing network. Drawing on our experience in representing numerous Oldsmobile dealers after the "discontinuance" of the Oldsmobile linemake, we are advising dealers to, among other things, not make any significant investment in their dealership without obtaining a representation from GM/Chrysler that GM/Chrysler had no intention of eliminating the dealer's linemake in the face of the rumors that GM may purchase the Chrysler Division.

Lastly, we are working with some dealer associations to add legislation that would require that a discontinued dealer be paid fair market value for their franchise unless the new owner continues to honor the dealer's franchise agreement.

Please go to our website at www.dealerlawyer.com to review the alerts and articles referenced above.

Plaintiff's Lawyers Bring Lawsuit Against Most South Carolina New Motor Vehicle Dealers

MYERS & FULLER IS REPRESENTING SEVERAL DEALERS THAT HAVE BEEN NAMED AS DEFENDANTS IN A CLASS ACTION SUIT ALONG WITH ALMOST EVERY OTHER NEW MOTOR VEHICLE DEALER IN THE STATE OF SOUTH CAROLINA RELATED TO THE CHARGING OF DOCUMENTARY FEES. The Plaintiffs' lawyers claim that the placement of such fees on a dealer invoice is deceptive in that it implies that the fee is separate and distinct from the general overhead that car buyers expect to be included in the sticker price for a car and that such placement suggest that the fee is mandatory. The lawyers further claim non-compliance with a state statute regulating the charging of documentary fees.

The South Carolina action comes on the heels of a late 2006 trial court decision in the State of Arkansas, wherein the trial court ruled that the charging of documentary fees by a car dealer amounts to the unauthorized practice of law. That court reasoned that dealerships were being compensated for preparing "legal" documents. Myers & Fuller was not involved with the Arkansas action and believe the opinion is misguided.

Motions to dismiss the South Carolina class action complaint have been filed on behalf of the dealers and a hearing is scheduled during April.

Myers & Fuller, P.A. Dealership Seminar Opportunities

contact us today to schedule or modify one of these seminars for your organization

DEALERSHIP MERGERS & ACQUISITIONS/ SUCCESSION ISSUES

DEALERSHIP MERGERS AND
ACQUISITIONS/SUCCESSION
Duration: 1.5 to 2.5 hours
Content: Discussion of issues surrounding Letters of Intent, Asset & Stock Purchase Agreements, manufacturer franchise application process, and proper succession planning.

A WALK THROUGH THE MANUFACTURER
FRANCHISE APPLICATION PROCESS
Duration: 1 hour
Content: Detailed, step-by-step, walk through of the manufacturer application process involved in buying and selling a dealership.Includes examples of various manufacturer applications and the particular items certain manufacturers look for.

FRANCHISE LAW ISSUES

MAJOR TOPIC REVIEW
Duration: 2 to 3 hours
Content: Review major issues impacting franchises including points of sale, terminations, ownership transfers, management changes, incentive programs, audits, dealership succession, mergers and acquisitions.

FRANCHISE BY FRANCHISE REVIEW
Duration: 1 to 2 hours
Content: Covers latest franchise trends as well as issues covered in MAJOR TOPICS REVIEW as they apply to particular linemakes.
Audience: Most commonly presented to 20 Group meetings.

LEGISLATIVE REVIEW
Duration: 1 to 2 hours
Content: Reviews a specific State's motor vehicle franchise law provisions. Covers both the important provisions which should be taken advantage of by the motor vehicle dealers within the State as well as areas in which the franchise laws could be updated.
Audience: Motor Vehicle Dealer Association directors and board members.

STATE OF THE INDUSTRY
Duration: 1.5 to 2.5 hours
Content: Covers the latest trends in the industry – topic by topic. Focuses on the latest trends in sales incentive programs, facility/image programs and dealer body consolidation programs, etc. Includes recommendations to avoid participation in unreasonable programs and protect the dealer's investment in the franchise.

FINANCE AND INSURANCE ISSUES

INTRO TO KEY F&I CONCEPTS
Duration: 1 to 2 hours
Content: Overview of current industry developments and legal compliance requirements facing dealership F&I departments. Question and answer is an integral part of this presentation.

CONTINUING EDUCATION FOR F&I
(Intermediate/Advanced Level)
Duration: 2 to 3 hours
Content: Overview of key elements of dealership forms as well as a detailed discussion of state and federal laws covering F&I dealership operations. Includes suggestions on improving F&I performance while reducing liability.

COMPREHENSIVE ON-SITE F&I REVIEW
Duration: 7 to 8 hours
Content: On-site comprehensive review of dealership policies and procedures. Sampling review of dealership deal files. Update forms and training for management and staff. Conduct exit meeting with Dealer/Principal to discuss results of review.

The Definition Section by Robert Bass

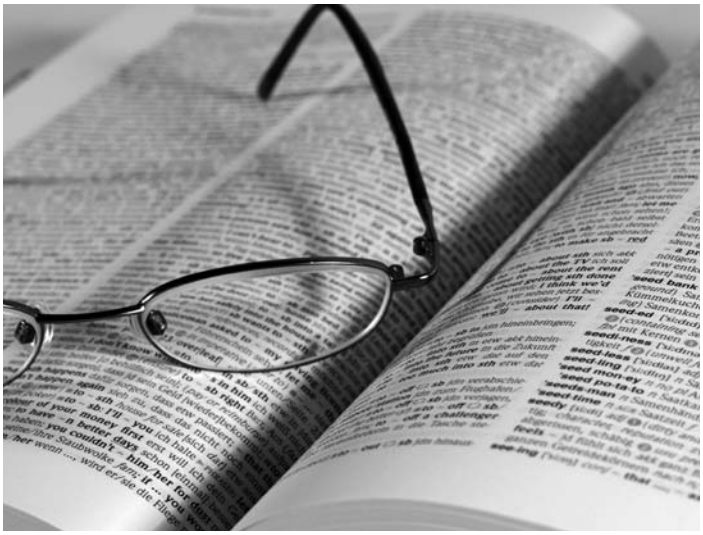
ENGLISH IS A MARVELOUS LANGUAGE, AND FOR THOSE WHO MAKE A LIVING PUTTING WORDS TOGETHER THERE IS AN OPPORTUNITY EACH DAY TO LEARN NUANCES IN THE LANGUAGE THAT WERE NOT PREVIOUSLY KNOWN. This process involves learning to use the right word in the right place. Clear and unambiguous writing is critical; however, it can also be a tremendous challenge. As author and noted language maven Bill Bryson writes in his book Bryson's Dictionary of Troublesome Words, English "is a language where cleave can mean to cut in half or to hold two halves together; where the simple word set has 126 meanings as a verb, 58 as a noun, and 10 as a participial adjective; . . .." Care should be taken not to use a word that means many things to different people depending on the context or circumstances.

If one uses the wrong word in a letter to a friend or business colleague, at best one might lose a little face or at worst, respect. (An old friend of mine used to say "dramatic" when he really meant "traumatic;" he became the brunt of much teasing for that.) Using the wrong word in the wrong place in a contract for sale and purchase of a dealership, however, may cost a party to the contract thousands of dollars or even cause the deal to fail. In many instances, it is not so much that the wrong word is used in an agreement; the problem comes when the right word is subject to numerous interpretations. It is critical for the parties to a buy-sell agreement to nail down the intended meaning of a particular word to successfully achieve the purpose of using that word.

So, how does one overcome these challenges? All well drafted transaction agreements should contain a Definition Section. Not every "defined term," however, goes into the Definition Section. If a particular word that needs defining is located and used only in a single section of the agreement, one can get away with noting the definition in that section. If, however, a particular term is found in several sections of the buy-sell agreement, it should be defined in the Definition Section. An exception to the foregoing: if defining a word takes several sentences and that word is used in only one section of the agreement, for ease of reading it is helpful to define that term in the Definition Section.

Now, as one who may one day be party to a buy-sell agreement, you're probably telling yourself that you'll leave it to your lawyer and advisors to worry about all this structure and format stuff. That is by and large true, but deciding which words go into the Definition Section and which words go into the body of the buy-sell agreement is only part of the game. The real chess match is deciding which words to define and how they are defined.

An asset purchase agreement will almost always provide that the buyer's obligations are conditioned on seller conveying its assets "free and clear of all Encumbrances" – with "Encumbrances" being a defined term. If nothing more is said, that is a buyer friendly approach. From a seller's perspective, not only should encumbrances be defined but there should be a defined term for "Permitted Encumbrances." A seller is rarely able to convey its assets free and clear of all encumbrances. There are almost always encumbrances on assets that haven't fully ripened at the time of closing. Take for example taxes that are not yet due; non-payment will subject those assets to a lien. Accordingly, a seller should make sure there is a definition for "Permitted Encumbrances." This removes the opportunity for the buyer to pull a "gotcha" on the day of closing and open the door for grinding on the deal.



"…the problem comes when the right word is subject to numerous interpretations."

Another phrase that one often sees in a buy-sell is "Material Adverse Change." Buyers will often condition their performance on there not being any Material Adverse Change to the dealership business. This phrase needs to be defined. An astute seller should attempt to minimize the affect of the phrase. For example, changes in the national economy shouldn't constitute a Material Adverse Change. Changes in the dealership business as a result of announcing the sale, such as key employees quitting, should also not constitute a Material Adverse Change. If the dealership suffers an insurable loss, that also should not constitute a Material Adverse Change. Insurance proceeds would allow the buyer to get the benefit of its bargain. Some parties like to quantify "Material Adverse Change" as part of defining the phrase by assigning a dollar amount. Sellers need to look for that phrase and be mindful of its affect on the deal.

A few other examples: "Knowledge" is a word that parties should be careful with. A Buyer will want a broad definition; a seller should prefer a more narrow application of the word. "Ordinary Course of Business" will often be relevant if the seller owns other same-brand stores and it has plans to shuffle its inventories before the closing. A buyer may want a definition that limits that activity.

The importance of the Definition Section is often overlooked by parties to a buy-sell. That can be a huge mistake. One should carefully consider the selection of terms to include in the Definition Section. If a party has particular plans or objectives that affect that process, it should discuss those issues with its attorney. If one does not understand a particular term in an agreement, one should discuss with their lawyer whether a defined term should be created. Active party participation is important if an effective buy-sell is to result. The clear and unambiguous use of words, through defining them, will help bring a transaction to a successful closing.

summary

- *All buy-sell agreements should contain a definition section.*
- *The content of the definition section can affect the allocation of risks between the parties.*
- *Buyers and Sellers should each carefully examine the definition section to see how it affects the deal.*

There is No Slow-Down in Add Points by Richard N. Sox and Loula M. Fuller

WE HAVE NOTICED A MAJOR UP TICK IN THE NUMBER OF NEW AUTOMOBILE IMPORT DEALERSHIPS AND MOTORCYCLE DEALERSHIPS, PARTICULARLY HARLEY DAVIDSON POINTS, BEING ADDED ACROSS THE UNITED STATES. The import dealerships include Honda, Toyota, Hyundai, VW and BMW points in markets that are arguably being more than adequately served by the existing dealers. Not only is such a new dealership sure to take away revenue from the existing dealers but, to add insult to injury, most of the existing dealers are being asked to spend millions of dollars to upgrade and expand their facilities at the same time.

Unfortunately not all States have protection against a manufacturer arbitrarily adding new points. Our experience tells us that having a franchise law that allows an existing dealer to challenge the need for such a new dealership is one of the basic protections which should be found in every State motor vehicle franchise law. The idea is not to prevent a manufacturer from adding a new dealership but to force them to prove that one is necessary.

Every "add point" protection must consist of the following points:

1) a right of an existing dealer to protest any proposed add point;

2) adequate notice of such an add point;

3) a "stay" of the add point during the pendency of a protest; and

4) detailed criteria by which the decision maker can balance the need for the new point with the harm to the existing dealer.

In this article, we will review the first two items. First and foremost, all add point protections should contain a clear definition of what constitutes an add point which can be protested by an existing dealer. This requires a proper definition of an add point. To be of most benefit to dealers, the definition of an add point should be "the opening or reopening of a new point of sale" with an exception for a relocation of an existing dealership such that the existing dealership is moving within some minimum range, say 2 miles, from its original location and/or that the existing dealership is not moving closer to the neighboring same linemake dealer.

An important note related to the definition of an add point is for the drafter to be cognizant of a "back fill" scenario. A backfill scenario is where a dealer relocates to a new location within the 2 mile exception but then has an agreement with the factory to add a dealership at the old location. In many cases, because the new point is within the exception and the old point is beyond the radius allowing a dealer the right to protest the backfill as a new point, the neighboring same linemake dealer just went from 1 competing dealer to 2 without any right to protest. This scenario can be cured by including a provision that says the 2 mile relocation exception only applies if the old location is not reopened for some period of time, say 2 years.

Getting back to the definition of a qualifying add point, the radius around the new point which triggers protest rights must be of a size that truly protects your territory while (it pains me to say this) being reasonable in allowing a factory to add new points in a growing market. One way to accomplish this balance is to have a larger radius, say 20 miles, for an add point in a county of less than 300,000 people while having a smaller radius, something like 13 miles, for a county with more than 300,000 people. It is critical that the radius used be the primary basis for the right of an existing same linemake dealer to protest an add point. It is equally important not to make the existing dealer's "market area" the trigger for a right to protest. This is because in every Dealer Agreement, the factory reserves the right to change your assigned market area at their sole discretion. Thus, a factory lawyer will simply tell the market folks to reduce a dealer's assigned market area in order to accomplish an add point nearby. If the add point is not within the new market area no protest rights will arise.

In addition to the mileage radius criteria for protest rights by a same linemake dealer, we also believe that the ideal State franchise law should include a provision allowing a protest if an existing dealer can establish that during any 12 month period over the last, say 36 months, such dealer or its predecessor dealer made something like 25 percent of its retail sales of new motor vehicles to persons whose registered household addresses were located within a radius of 20 miles or 13 miles, depending on county population, of the add point location. Such a provision has the effect of protecting a dealer whose market is so unique that he/she sell a large portion of their vehicles outside the traditional mileage radius. The dealer's investment is protected by focusing on where that dealer's business derives from instead of simply using the arbitrary mileage criteria.

After nailing down a proper definition of what qualifies as a protestable add point, the next item which your franchise law should contain is an adequate notice provision. The notice of an add point must go to the State department of motor vehicles, or its equivalent, with the specific name of the proposed dealer, the exact address of the proposed opening or reopening of a dealership, the linemake which is proposed to be sold from the location, and all franchised motor vehicles within a radius of say 100 miles. The State department governing motor vehicles should then publish or otherwise put all same linemake dealers on notice of the proposed add point. The State add point protection must then give any same linemake dealer at least 30 days from receipt of such notice to file a protest with the State.

We will discuss the remainder of the crucial add point provision criteria in our next edition.

summary

- *Protection from Factories' adding a dealer to your market is more important now than ever*
- *An add point protection must include an adequate definition of what qualifies as a protestable add point*
- *An add point protection must include an adequate definition of which existing dealers may protest the proposed new dealership*
- *A proper add point provision must include a notice provision which provides all dealers with more than sufficient time to protest the addition of a new dealership.*

More Pay Headed Your Way for Parts and Service?

RECENT FEDERAL COURT RULINGS IN NEW JERSEY AND MAINE COULD HAVE A SIGNIFICANT IMPACT ON DEALERS ACROSS THE NATION WHEN IT COMES TO RETAIL RATE REIMBURSEMENTS FOR PARTS AND LABOR WARRANTY WORK FROM THEIR RESPECTIVE MANUFACTURERS. The issue of retail rate reimbursement for parts and labor, a contentious issue for two decades, recently reappeared on the radar screen. The average dealership loses over $100,000 per year because of factory discounting of warranty rates. Roughly half of the states require manufacturers to reimburse dealerships at a retail rate for labor and parts.

In order to offset the higher warranty reimbursement rates for labor and parts, Ford implemented a "warranty parity surcharge" on all new vehicle invoices. Maine dealers argued that this surcharge by Ford, as well as pending surcharges by other manufacturers, is contrary to the intent of the statute- to require retail rate reimbursement, and would result in higher costs to the consumer. Maine auto dealers argued that there should only be one price for automobile repairs, warranty or customer pay, and that automobile manufacturers should not discount the warranty reimbursement rate paid to dealers for work that, eventually, gets subsidized by non-warranty customers. This ultimately equates to higher costs to consumers.

Maine's legislation amended the state regulatory scheme to prohibit manufacturers from adding state-specific surcharges to wholesale motor vehicle prices in order to recoup the costs of their compliance with retail-rate reimbursement laws. The statute, the only state law that expressly prohibits the additional surcharge by the manufacturer, is designed to protect Maine automobile dealers from the superior bargaining position held by manufacturers with respect to the dealers as well as to protect dealers by requiring that they receive their retail rate. Maine's law, passed in 2003 and upheld by a U.S. appeals court in November 2005, prohibits the surcharges. In May 2006, the U.S. Supreme Court refused to hear the Alliance of Automobile Manufacturers' appeal of the ruling.

New Jersey's law provides that a "motor vehicle franchisor shall reimburse" its franchisee for parts used in warranty repairs at the franchisee's "prevailing retail price," provided that the retail price is not unreasonable. In the New Jersey case, a district court ruled in March 2006, that surcharges imposed by Ford Motor Co. are illegal. The New Jersey court's ruling reaffirmed a similar 1995 ruling prohibiting Ford's dealer parity surcharge. In March, the federal court sided with Garden State dealers, agreeing that such surcharges violate the New Jersey law. U.S. District Judge William Bassler wrote that because of Ford's surcharge policy, "no dealer will be reimbursed for warranty parts at the prevailing retail rate." He compared the surcharges to "a shell game." Ford is appealing the decision in the New Jersey case.

If this trend continues, dealers across the nation may find themselves receiving more for warranty parts and repairs.

summary

- *Maine law expressly prohibits additional surcharge by manufacturer; intended to require manufacturers to pay dealers retail rate for warranty work.*
- *Passed in 2003, upheld by a U.S. appeals court in November 2005 and Supreme Court in May 2006.*
- *New Jersey Law requiring parts reimbursement at prevailing retail price upheld in March 2006; Ford surcharges to offset difference ruled illegal.*

Crafting FACTA Identity Theft Rules

LATE LAST SUMMER SIX FEDERAL FINANCIAL REGULATORY AGENCIES JOINED TOGETHER TO CRAFT LONG ANTICIPATED "RED FLAG" RULES. This latest FACT Act requirement will require various creditors and lenders – including dealers – to develop, implement and monitor a written "Identity Theft Prevention Program." Under the proposed Red Flag Regulations, creditors, such as new car dealers, must have a written Program that is based upon the risk assessment of the creditor and that includes controls to address the identity theft risks identified. This Program must be appropriate to the size and complexity of the creditor and the nature and scope of its activities, and be flexible to address changing identity theft risks as they arise. A creditor may wish to combine its program to prevent identity theft with its information security program, as these programs are complementary in many ways.

The National Automobile Dealers Association is actively representing dealer interests and offered comments on the proposed rule.

The proposed rule requires the dealer's written plan to identify and respond to "red flags" indicating the possibility of identity theft. The proposed rule suggests 31 red flags and requires each creditor to conduct a risk assessment to determine which red flags are relevant to its business.

Similar to the FTC Safeguards Rule, the proposed rule requires staff training and oversight of service providers. It also requires the creditor's Board of Directors to approve the written program and oversee its development, implementation and maintenance. In addition, staff employees who are responsible for implementing the program must report to the Board or senior management at least annually regarding the company's compliance.

Myers & Fuller will keep you advised of the progress of this important rule making procedure.

summary

- *Red Flag Rules proposed; require dealers to develop, implement and monitor a written Identity Theft Prevention Program*
- *Dealership must evaluate current identity theft prevention practices and its understanding of all of the "red flags" of identity theft that apply during a credit transaction.*
- *Dealership must create new policies and train all relevant staff to recognize the applicable red flags and know what actions to take when red flags are found.*
- *Dealership's designated program manager must continuously monitor new identity theft trends and determine the need for applicable updates to the dealership's compliance program.*
- *Once each year, a dealership's designated program manager must provide detailed reports on the compliance program's effectiveness.*

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