The Wheels of Justice
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Consider Including Arbitration Clause In Your Deals

You could prevent class action suits

Your dealership may wish to consider including an arbitration agreement as a part of your deal documents. The use of an agreement that only requires one party to elect arbitration, that prohibits class actions and that allows small claims types of actions is suggested.

The Federal Arbitration Act was passed by Congress in 1925. The act was originally intended to apply only to large corporations, but has been expanded to include small businesses and individuals as well. On account of the Federal Arbitration Act, courts tend to favor arbitration over trials in the United States. Most states also have a strong public policy favoring arbitration.

Generally, if a customer signs a contract, the customer is under a duty to read it, and will be bound by its terms, unless the customer can show that he or she was willfully misled or misinformed by the other party. Absent such misrepresentations, the customer will likely be held to have signed the contract with full knowledge of the contents thereof, making an arbitration clause enforceable, so long as the terms are otherwise reasonable.

Some dealers are opposed to including arbitration agreements in their deals for various reasons, including the belief that inclusion of such an agreement suggests from the start that the business relationship with the customer may have problems. Other dealers subscribe to the belief that they should not require consumers to arbitrate disputes when dealers fought

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Follow Your State's Franchise Act

Don't squander your hard-fought-for protections

Last issue, I pointed out the importance of examining and comparing state franchise laws as part of a buyer's pre-purchase preparation. Having picked a particular state in which to purchase a dealership, the emphasis must then turn to complying with that state's franchise laws. Failure to do so can result in substantial adverse consequences.

Every year I get a handful of phone calls from dealers selling their dealerships which have either had the factory reject a buy-sell proposal or are struggling to get the factory to provide an approval to a proposed buy-sell. After listening to their stories, the first inquiry I always make of them is, "so tell me about the statutory notice of sale you sent to the factory." This is usually followed by a long pause of silence. As I probe further, I often learn that the seller and buyer simply mailed to the

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THIS ISSUE

Another Franchise Discontinuance, Another Deception

DaimlerChrysler Vans recently announced, without fanfare, that the Freightliner Sprinter van would no longer be distributed to those select Freightliner dealers who made hefty investments in the product. The announcement was not a total surprise, after participating Freightliner dealers had financially committed to the product, the news began to slip out little by little. However, the first preliminary announcement was made by Freightliner LLC, not DCV. This was no coincidence. We view it as an apology of sorts. The total loss of credibility with a dealer body is a hard thing to mend.

On July 18, 2002, FLLC's president sent a global letter to all Freightliner dealers sell-

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How to Read and Understand a Market Study, Part II

This month we look at performance and demographic sections

Last month we began our analysis of sections of a market study by examining the first two sections: *Geography* and *Standard of Review*. This month we continue the analysis by reviewing the *Performance* and *Demographic* sections. As we have pointed out in past issues, all market studies are essentially the same because all manufacturers rely to some degree on Urban Science Applications, Inc. ("USAI") a.k.a., the Evil Empire.

The next section in a market study analyzes *Performance* in the defined market by the previously defined standard. To accomplish this, USAI will prepare a Retail Product Popularity Report which breaks a manufacturer's vehicle offerings into competitive segments and analyzes how each of the segments is doing against the competition. USAI would like to have you believe that this type of analysis takes into consideration all the differences in each and every market as they relate to demographics and buyer preference. Don't be fooled on this issue; they do not. Segmentation is better than nothing but only marginally. The analysis is done by taking the number of registrations in the competitive sets (segments that are similar) and multiplying by the manufacturer's expected penetration standard (the highest market share they can find). The result of this calculation is the number of expected registrations that the manufacturer determines should be sold in the market area. If the number of actual registrations is less than expected registrations, then your market area will show a net loss to expected registrations and may foreshadow a determination that some *market action* such as adding an additional point or relocating a dealer may be necessary. (We have reviewed hundreds of these studies and never once have we seen a conclusion that the manufacturer's product or marketing is the reason for the alleged short fall. Neither have we ever seen a study that concluded that the buyer preferences did not favor the factory products.)

It is really important for you to look carefully at these calculations and insure they make sense. Look at the standard they use to determine expected registrations and also the segments the factory decides its product competes with. We have seen 300 series BMW products in the same segment with Kia products. Look closely and don't just take the factory's word for it.

Next, the performance analysis will include an 8 1/2 glossy showing where the retail registrations are located on a map. They do this to set the stage for a finding of lost opportunity or lost sales. The green areas represent census tracts (areas) that exceed the expected registration standard and the red tracts equal lost sales. These gain/loss maps will be used to analyze whether areas around your dealership(s) are performing up to the manufacturer's standard. They use red and green to get you, the dealer, thinking how bad a performer you are and to insure that you are conditioned to accept any suggestions (add point or relocation) they propose. Don't bite!

> **"We have reviewed hundreds of these studies and never once have we seen a conclusion that the manufacturer's product or marketing is the reason for the alleged short fall."**

The next section is the *Demographic* section which analyzes growth and/or decline in the study area. This analysis includes a look at population changes, household changes and average household income in the study area. This section is very important and will allow you to determine whether your primary market area is declining or growing in population and/or households. They again use colors (green is growth, yellow is decline). Look to see how your area is forecasted to look in the future. One of the tricks of the trade for the factories is to show a forecast of growth for a market. We have seen market studies that showed growth in certain census tracts in one year and decline in others. Clearly the information is only as good as the forecaster and is good for only one year. The factories would like you to believe the forecast came down from the mountain. It doesn't! It will, however, help you to determine if the households in your primary market area can afford to buy your vehicles and whether growth is predicted. No growth generally means that no market change can be supported. That is good for you, bad for them. Pay attention to the household income that the manufacturer determines is the minimum amount of income that a household needs to buy your product. Ask for a buyer profile of who your customer really is. All factories compile this type of data and know the age, income, education and marital status of the buyers of each and every model. If you ask for it and they provide the information (about a 50-50 proposition) you can then use the demographic analysis against them if threatened by an add point or a relocation. If the purpose of the study is to add a dealership, manufacturers have been known to use a household income that is entirely too low for the consumer to be able to afford your vehicles. Keep 'em honest.

This section will also look at sales patterns which show where sales are registered relative to each of the same line make dealers and how fast sales volume drops off as you go farther away from your dealership (intra-brand competition). They, the factories, place the registrations in the census tract in which the actual customer resides but they do it randomly. That is to say the registrations are accurately placed in the right census tract but not necessarily in the right location within the census tract. We have seen instances where a census tract only had households in one small portion of the census tract but the registrations where spread across the entire tract. This gives a false appearance of where people

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Franchise Discontinuance, continued from page 1

ing the Sprinter that a committee, known as the EAC, had voted to dual brand the Sprinter product as the Dodge Sprinter and that Freightliner dealers likely would be phased out in 2006. If you recall, keeping spirits high and allaying anger, this letter promised that all Freightliner dealers would be treated fairly and that the financial investments of each Freightliner dealer would be recognized. DCV followed with the same theme shortly thereafter. FLLC knew that this entire transaction had turned out to be a sham and that the best and most aggressive of its dealers had been used as so many mules to plow the new US market for DaimlerChrysler AG ("DCAG").

So ask yourself now, how many affected dealers have been treated fairly and how many have had their financial investments recognized and compensated? We have not found the first one. The Sprinter, for Freightliner dealers was a bust all the way around. It now appears the entire transaction was suspect and that once the US market was opened, Freightliner dealers were sent packing while others reaped the benefits of their hard work. DaimlerChrysler needed a seasoned dealer body with commercial and individual customers to introduce the Sprinter into the US market. The obvious choice was the Freightliner dealer body. FLLC then proceeded to "sell" the Sprinter concept to its dealers; FLLC touted the incredible success of the product in Europe and told Freightliner dealers that the market for this product would eventually match the US market for heavy-duty commercial trucks. No one ever mentioned Dodge, dual branding or the prompt elimination of Freightliner dealers now abandoned after performing the hardest task assigned, opening the US market.

After the sales pitch was made, FLLC demanded that select dealers heavily invest to ensure that the Sprinter had its own showroom, sales personnel and technicians. The impression left by FLLC was clear – Freightliner dealers would sell the Sprinter as a Freightliner branded product and would eventually see its market expand geometrically. FLLC made it clear that investment for the long haul was required. No one balked at this opportunity. Who would?

At the eleventh hour, after all participating Freightliner dealers had irrevocably committed to the product, the announcement came that DCV would be substituted as the "new" distributor for the Sprinter Van. FLLC knew this would not raise any eyebrows as other Freightliner products had in the past been distributed by companies other than FLLC. This, we believe, was by design. What the Freightliner dealer body did not know is that DCV was literally thrown together at the last minute, created from nothing, to substitute for FLLC. Why? The answer is simple. This action was taken to insulate and separate by substituting a company on which the ink had barely dried on its Delaware corporate papers. We believe the facts will show that DCV is but a shell, without a glimmer of substance.

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However, this "corporate" insulation was not sufficient. DCV and FLLC wanted more protection from the conduct that had transpired, particularly since the real distribution plan would quickly be revealed. Therefore, every Freightliner dealer who had invested to obtain the right to sell the Sprinter was informed that in order to obtain an agreement to sell the Sprinter, and this requirement was not negotiable, the dealer had to sign a "release." This was not any standard release; it was created especially to insulate FLLC and DCV for any misconduct they may have committed in selling the Sprinter opportunity to the Freightliner dealer body. The release forgives any act, whether it is fraud, deceit or even criminal in nature. We believe this to be the single most revealing act that demonstrates these folks knew, and knew well, that someone's goose had been plucked clean. FLLC even went so far as to demand a second set of releases when its 2003 dealer agreement was presented to its dealer body. All of this was shrewd, but very transparent.

There is not enough room here to print all of the findings our investigation has uncovered. Suffice to say, it appears to be an ugly overall picture and some mighty good people appear to have been taken advantage of. There are alternatives to simply accepting the dictated outcome from DCV. In many states, there are specific laws that protect dealers from this kind of slick maneuvering. In other states, there are laws that prohibit one business from taking outright advantage of another. If you have not been treated fairly or your investment has not been recognized, contact your dealer lawyer.

by Richard N. Sox, Jr.

Article summary

- Freightliner dealers were used to open the US market.
- DCV was a shell used to deceive dealers.
- Under franchise laws the affected dealers have a right to receive the fair value of their franchises.

Follow Your State's Franchise Act, continued from page 1

factory the buy-sell contract with nothing more. My follow-up inquiry is whether the seller's attorney checked the factory notice requirements under the dealership transfer provisions of the state franchise act. Again, this is often followed by another pause of silence.

In the last two months, I have received a greater number of such phone calls than usual. In several cases, neither the seller nor buyer had any clue about the notice of sale requirements under the state franchise laws. This left them with little or no power under state franchise laws to get the factory to approve the particular transaction or expedite the factory's decision on the proposed transaction. Seller and buyer must take time to understand and comply with the notice of sale requirements contained in the transfer provisions of the seller's state franchise laws. The statutory notice of sale is a critical part of the dealership transaction process and must not be overlooked, because in most instances, a proposed transaction will not enjoy statutory franchise protections unless the parties to the transaction have followed the transfer provisions of the franchise act to the letter.

There are essentially two types of statutory requirements found in state franchise laws. One is straightforward – the seller must provide notice to the factory of a proposed sale of a franchised dealership or transfer of a franchise. Under this type, the notice can usually be satisfied by a simple letter from the seller to the factory, and, arguably, merely sending a copy of the executed buy-sell agreement to the factory is sufficient.

The other type of notice can be much more involved. Many state franchise acts require that the seller's notice of sale include information about the ownership of the proposed buyer. Specifically, the seller must identify the name and address of each owner of the buyer as well as a statement of the ownership's relevant retail motor vehicle experience and a personal financial statement of each owner.

In the buy-sell agreements I prepare for clients, I take special care to include a provision in the agreement that allocates among the parties the statutory notice of sale responsibilities. In states that require personal financial and business experience statements, my agreements require the seller to prepare a simple letter that identifies the name and address of the buyer and makes reference to enclosures containing the financial and business experience information of the buyer. The seller sends this letter to the buyer, who then encloses with the letter the business and financial information and sends off the notice to the factory by overnight carrier (or the required carrier under the transfer statute). When the factory receives it, the notice should look like it came from the seller. The reason for the notice's circuitous route to the factory is that most buyers typically do not want to share with the seller their financial position.

"Take special care to include a provision in the agreement that allocates among the parties the statutory notice of sale responsibilities."

Why is the statutory notice of sale so critical? Many transfer statutes require the factory to approve or reject a proposed transaction within a particular period of time or the proposal is deemed approved as a matter of law. As a result, factories are required to respond within a specified period of time and cannot pepper the seller and buyer indefinitely with requests for more information. Transfer statutes also often set out specific standards by which the factory is governed in undertaking its consideration of a proposed transaction. For example, the transfer statute may provide that if the proposed buyer has good moral character, relevant retail market experience, and adequate financial wherewithal, the factory must approve the transaction and buyer. Unless the parties specifically comply with the statutory notice of sale requirements, the transaction likely will not be covered by the transfer statute and the factory's review of the transaction will not be subject to the statute, and, as a result, the parties will not enjoy what may be substantial franchise protections.

Preparing and delivering a properly prepared notice of sale to the factory must be a team effort. Seller and buyer must, with their respective attorneys, review the franchise transfer statute requirements and make sure that they comply with the statutory notice of sale.

by Robert Bass

Article summary

- Research the statutory notice requirements under the franchise act governing the transfer of a franchised dealership.
- Follow the requirements to the letter.
- All parties to the transaction must work together in preparing a notice that complies with the transfer provisions of the seller's state franchise act.

Market Study, continued from page 2

live and how a sales pattern relates to the "real world." Remember registrations (one dot equals one registration) are placed randomly in census tracts or zip codes and not in the exact location of the registration so keep an eye out for unusual spreads of the dots. They are later going to take these randomly placed dots and pretend that they are real and then try to tell you how well you are doing in two mile circles going away from your dealership. This is not only disingenuous it is ridiculous. But they have gotten away with it for years. Know it is fiction and act accordingly.

Next month we will analyze the remaining sections of the market study. Remember, be careful when you look at a market study. If you believe that the recommended market action will negatively impact your dealership write your manufacturer and tell them that you disagree with the recommendation and any other conclusions reached by the market study that make no sense or that you know can not be supported by sound science. Ask for the buyer profiles, look at the geography assigned to you and think about what you are looking at. If it doesn't make sense to you it probably doesn't make sense.

By Martin Hayes and Dan Myers

Article summary

- Performance problems identified in a market study are always dealer related.
- The demographic section can provide insight into your area of responsibility if you ask the right questions.
- Ask your manufacturer for a buyer profile of who your customer really is.
- If you disagree with any conclusions in the market study write your manufacturer.

Include Arbitration Clause, continued from page 1

so hard to avoid arbitration with their manufacturer or distributor through an exception to the Federal Arbitration Act.

However, there are various benefits of arbitration for consumers. According to the National Arbitration Forum,[1] independent studies have shown that:

- Arbitration is approximately 36 percent faster than a lawsuit;
- Arbitration is less expensive for consumers; [2]
- Ninety-three percent of consumers using arbitration found it to be fair;
- Individuals prevail at least as often in arbitration as in lawsuits.

Arbitration agreements are generally enforceable so long as the existence of the arbitration agreement is clearly disclosed to the customer and provided that the terms are not unreasonable. Examples of unfair provisions which can make arbitration clauses vulnerable include: requiring customers to keep arbitration decisions secret; charging excessive arbitration fees; forcing consumers to use a particular arbitration firm; requiring the loser of an arbitration dispute to pay attorney's fees; and forbidding punitive damages even in cases of egregious misconduct.

Dealers often ask what happens if a customer refuses to sign an arbitration agreement. The concept of "freedom of contract" provides that the dealership cannot force someone to arbitrate. The customer can merely shop elsewhere. If a dealer elects to utilize an arbitration clause, the dealer should uniformly require all customers to sign the arbitration agreement. Failing to use an arbitration clause in all agreements could lead to problems with enforcing other arbitration agreements.

The greatest potential benefit of arbitration for a dealer is the ability to prohibit class action lawsuits. Plaintiff's lawyers are much less inclined to bring a single action against a dealership when there is not the possibility of a class action payday.

Dealership arbitration agreements should also include a provision that does not prohibit all court litigation. It is suggested that consumers be allowed to bring individual claims against a dealership in a small claims court forum. Dealers also wish to reserve their self-help remedies to the extent allowed by law. Further, either party should be able to request arbitration. A choice of more than one arbitration firm should also be offered.

Agreements should provide that arbitration is not mandatory unless one party expressly requests it. Such a provision allows a matter to proceed in court if the parties so choose.

We are operating in an era of class action lawsuits. Though no strategy is guaranteed, consistent use of an enforceable arbitration agreement that purports to prohibit class action participation is a good step in the right direction.

[1] *National Arbitration Forum Empirical Studies & Survey Results 2004 (www.arb-forum.com).*

[2] *For example, the American Arbitration Association limits consumers' fees to $125 in cases that involve claims of $10,000 or less. When claims exceed $10,000, the fee is $350.*

by Shawn D. Mercer

Article summary

- Courts favor arbitration over litigation.
- Arbitration is more cost effective than litigation in a consumer lawsuit against the dealership.
- Arbitration clauses are generally enforceable unless they include unfair provisions.
- Arbitration will help in avoiding class action litigation against your dealership.

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