

The Monthly Dealer Legal Newsletter compiled by "The Dealer's Law Firm," Myers & Fuller

Venturing Beyond your State to Buy Dealerships

Due diligence is required as state laws can vary

Are you in the dealership buying mode? Will you be searching for stores in more than one state? Buyers face a variety of issues during the dealership acquisition process. If your search takes you across state lines, there are additional considerations that must be addressed. There are 50 possible ways a transaction can be affected by state law, because the contours of the legal relationship between dealer and manufacturer vary widely from state to state. A careful study of what I like to refer to as "jurisdictional considerations" should be an important part of your pre-purchase preparation.

As I pointed out in my last article, the smart buyer of a dealership expands the due diligence inquiry to include a review of applicable factory's dealer network initiatives. If you are venturing beyond your backyard and

into other states, your due diligence inquiry must also include a careful review of the state law of each of the states in which a prospective target dealership is located.

In some states, for example Florida and North Carolina, the dealership appointment criteria that a manufacturer may apply to a proposed transaction is strictly defined by the state dealership franchise protection statute. Such specific standards for the approval of a proposed purchaser of a dealership are intended to keep the focus on the qualifications of the buyer. As a result, the manufacturer, in theory, cannot condition the approval of the transaction on the buyer constructing new facilities, relocating the dealership, or achieving a particular dealer network initiative. In contrast, other states have

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Statutory Protection from Factory Audits

State laws are in place to protect you

Does your state statute protect your dealership from unfair and discriminatory audits? Many, if not most, state statutes do not give dealers adequate protection from unfair or discriminatory audits.

Every factory has the right to audit your dealership's warranty and incentive claims. Virtually every factory, in its sales and service agreement, provides that making "false or fraudulent" statements to the factory is grounds for

termination. Many factories have used this provision in the sales and service agreement to terminate dealers for the filing of claims that the *factory* determines are "false or fraudulent."

One of the most important protections your statute can give you is a definition of "false" and/or "fraudulent." That definition should require actual knowledge and acquiescence of the majority owner and/or the dealer

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Chrysler's Continuing Efforts to Force Exclusivity

Now more than ever Chrysler is feeling good about itself. Inevitably, when a factory believes it is providing good product to its dealers and is gaining market share, it begins to place greater demands on its dealers. In Chrysler's case, that pressure began to be applied in early 2004, when Chrysler sent out letters strongly urging its dealers to consider exclusive Chrysler facilities. In that letter, Chrysler requested a business plan for accomplishing the "undualing" of those non-Chrysler franchises.

When dealers overwhelmingly ignored those letters, Chrysler sent a follow-up letter that was not so nice. In that letter,

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How to Read and Understand a Market Study

Properly defining your market and your performance standard

Last month we began a discussion of the dreaded market studies that all manufacturers conduct from time to time. This month and next month we will discuss what to look for in each section of the market study. While the terminology may vary slightly, the form and substance of all manufacturers' market studies are essentially the same. This is primarily because all manufacturers rely to some degree on Urban Science Applications Inc. (USAI), when conducting the study. USAI, you will remember, is the "sorcerer" the factories use to conjure up their implements of torture.

The first section in most market studies is the "geography or market definition" section. The purpose of this section is to convince you that the factory has conducted an examination of the market and determined that the market is properly defined. This is sometimes true and sometimes not. This section is the first opportunity for you as a dealer to look for yourself to see if the market makes sense to you. Both you and the factory should look at cross sell data to determine if the dealers who are currently in the market are rightfully included in the market. Cross sell data is also analyzed to determine if any fringe dealers are presently selling enough vehicles to be included in the market. Urban Science uses a test (sometimes 30/30, sometimes 40/40 and sometimes arbitrary) to determine if a fringe dealer should be included in the market. You should know what formula your factory uses and see if it is following its own procedures. If a dealer that is not currently included in the market area is now registering whatever the formula requires and the dealers in the market are registering the required percent in the fringe dealer's market, then a recommendation should be (but will not always be) made to include the dealer in the market area. You need to insure the market is properly defined as to the number of dealers if you hope to get a meaningful market study.

If your store is in an area that is experiencing rapid growth, it is quite possible that the study will conclude that a fringe dealer should be included in the market area. With this recommendation comes the need to realign the dealers Area of Responsibility (AOR). Although it may seem counter-intuitive, adding a dealer is normally a good thing. This is because it will result in a smaller AOR for your store and smaller is better because it will be easier for the dealership to meet the standard that the factory uses to judge your sales performance.

That said, you must now carefully analyze the area and make sure that

despite the fact that it was located on the other side of a river that had only one bridge. While the area was closer by air it was impossible to reach by car. The new assignment made it a certainty that the dealer would look bad on the performance scale and insured problems down the road.

If you find any problems with your newly assigned geography, write a letter and complain to the factory. Be very explicit in telling the factory all the information you have. Show how the geography should be assigned to some other dealer. You must respond quickly so as not to be seen as accepting the new geography as correct. By acting quickly you have made a clear statement that you feel the assigned geography is improper and have begun a defense should the factory come to you later with a poor performance letter. If the geography assigned to you is improper (too

"The first section in most market studies is the 'geography or market definition' section. The purpose of this section is to convince you that the factory has conducted an examination of the market and determined that the market is properly defined. This is sometimes true and sometimes not."

any changes to your assigned geography make sense. First, determine that the study has your dealership location and the other market area dealers' locations on the map correctly. As we noted last month, the factories rely on Urban Science's "dealersites" program and it is not infallible.

Next, look at your newly assigned geography to see that it makes sense. In other words, does the area conform to traditional shopping patterns, have you been assigned non-residential areas or are the demographics such that the consumers in your new areas can't afford your product? Also, make sure that your area is not handicapped by geographic barriers such as lakes, mountains, etc. We have seen studies that assigned geography to a dealer

large), you *will never* be able to meet your sales performance requirements. That will *always* put you behind the "eight ball" with the factory.

The second section in the market study is generally the "sales or registration" performance review. Performance can't be reviewed without a standard of review (national average, regional average, zone average, etc.). When reviewing this section, you should determine if the standard has changed. If so, you should determine if the change is beneficial or harmful for your dealership. It is very rare to see a market study which reaches the conclusion that the market is performing up to the factory's standard. Therefore, whether the standard has changed or not, this is the

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Last Man Standing: Consolidation at Big Blue

Three separate divisions now referred to as 'P-B&G'

In the Renaissance Center, where the world's largest manufacturer of automobiles shelters its elite, one can still catch a glimpse of the ghost of Ron Zarella, who many believe was the father of the Oldsmobile discontinuation. That's however, as much as you will see. It appears that the tide which washed the discontinuation of Oldsmobile into these hallowed halls has not receded. Consolidation of models – from which consolidation of brands must inevitably follow – continues.

GM recently announced that it was specializing the models which would be assigned to Pontiac, Buick and GMC franchisees. This is but another way to say that GM continues to consolidate models, brands and ultimately

dealers. Gone are the days when GM attempted to provide a “full array of models” to each of its brand franchisees. The product addendum to

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the GM Dealer Sales and Service Agreement will, we believe, continue to shorten as time passes. What once stood as three separate divisions is now referred to as “P-B&G.” What the GM announcement means, in no uncertain terms, is that “P-B&G” is now a single brand. Any doubts about this were resolved by the stern warning in the announcement, that anyone who cannot combine these three franchises may not survive.

Let it be known that we are not here to judge GM. It is clear that GM believes that continued consolidation, in every business sense, is what the market dictates. GM showed the resolve to consolidate, regardless of sentiment when it axed its oldest brand, the equivalent of sending your grandfather to a nursing home. In

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Market Study, continued from page 2

time to complain to the factory if you do not believe that the standard is fair or achievable. For a standard to be achievable it must have some similarity to your area. A classic example of an improper standard is the Miami, Florida market. Domestic dealers in the the Miami market are at a huge disadvantage due to the high level of Hispanic buyers. GM uses the state average to analyze performance and it has proven to be an impossible hill to climb. Over 70 percent of the Miami market buyers are Hispanic and on average Hispanics buy import branded vehicles. Additionally, Hispanics buy cars and not trucks. GM, Ford, and Chrysler are not big on cars and rely on trucks to carry the day. Using the state average is improper because the rest of the state of Florida is not remotely similar in demographics. Dealers in Tallahassee and Gainesville sell more trucks and fewer cars. Dealers in Tampa, Orlando and Jacksonville are the same. A domestic dealer in Miami will never be able to meet the state average and the state average is, therefore, improper. Making Miami dealers com-

pete directly with dealers from small towns in rural areas which may only have one or two GM linemakes and a Ford and Chrysler store and no import competition, makes the standard impossible to meet. This lack of competition in the rural areas in Florida consistently results in the GM dealers achieving a higher market share than metro Miami dealers. The state standard also does not take into account the unique characteristics of an international city such as Miami, which has a diverse population that prefer imports over domestics.

We have recently been attempting to convince judges, with some success, that in a state such as Florida, that the metro areas should be judged against each other and not against the rural dealers. This problem of being judged by the state standard exists in many states where the same penetration patterns exist. If you have this problem or any problem with the standard by which you are judged, you should make your disagreement known when you respond *in writing* to the market study.

Next month we will continue our discussion on what you should look for in the remaining sections of the market study.

By Daniel E. Myers and Martin Hayes

Article summary

- Carefully analyze the geography assigned to your market.
- Determine if any changes have been made to your AOR and whether the proposed changes make sense.
- Remember when it comes to your AOR bigger is not better.
- Analyze factory standard of review to determine if it is reasonable.
- If the assigned geography or the standard of review is unreasonable, write the factory.

Statutory Protection, continued from page 1

operator in the filing of fraud claims. A dealer should not be terminated because (s)he has a rogue employee who files bogus claims. Once the majority owner or dealer operator discovers an employee has filed bogus claims, (s)he should terminate that employee.

The statute should also prohibit the factory from auditing or charging back claims filed more than one to two years prior to the date of the audit. Any chargebacks by the factory should be based on actual claims that were filed in error. No chargeback should be based on the factory extrapolating unless the dealership agrees to be charged back on that basis.

The statute should prohibit chargebacks based on failure of the dealer to follow the factory's policies and proce-

dures. If the dealer and/or consumer were entitled to be reimbursed/paid by the factory, the factory should be responsible for payment. In other words, dealers should not be charged back for ministerial mistakes or sloppy bookkeeping.

Recently, we have seen a barrage of audits by a number of factories when their obvious intention was to reduce the number of its dealers and/or to recoup moneys due to the factory's poor financial condition. Audits actually designed to insure fair and factual reporting of claims are appropriate. However, in today's atmosphere, it seems more and more factories are using audits as a sword.

*By Loula M. Fuller
& Richard N. Sox, Jr.*

Article summary

- State laws should protect dealers from unfair and discriminatory audits.
- "Fraud" should be clearly defined by the statute.
- Dealer operator must have actual knowledge for "fraud" to exist.
- No audits for claims filed one to two years before the audit.
- Dealers should not be charged back for sloppy bookkeeping.

Consolidation at Big Blue, continued from page 3

fairness, there were tears shed within the "RenCen" the day that decision was announced. GM's legacy and related healthcare costs have taken a toll on the company's bottom line, no one disputes that fact. However, our job is not to defend GM; our job is to make sure that the family of soldiers who have held the front lines and stood watch over the kingdom for GM's generals, namely the dealers, are protected. At the end of the day, without its dealers, there is no GM.

To those who receive this newsletter, we are not without defenses to this new wave of consolidation. This firm, without any question, led the national representation of dealers during the Oldsmobile discontinuation and we learned a lot. The following measures should be commenced by every dealer potentially affected by the P-B&G announcement. Begin charting your volume, expenses, and profitability closer than ever. If possible, obtain a valuation of your dealership now so that it can be compared to the diminishing value into the future. When models do become specialized, be aware and document buyer comments about the available model array, particularly when you don't have a model type a customer desires. Catalogue all GM comments about your market per-

formance as GM's market performance criteria are founded on its ability to provide you a full array of models. Check the language in your next proposed GM DSSA agreement, compare it against your existing agree-

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ment and find out what changes have been made. These changes are harbingers of things to come. Begin petitioning your local GM representative, in writing, about obtaining the other consolidated brands. If GM expects that no one brand can stand on its own, it probably has a plan to consolidate in many markets. In making these requests, inquire about GM aiding, without too many strings, in acquiring these additional brands.

Document any local consolidation of brands that may leave you out of the commercial mix and object in writing when this occurs. If, after all of these events unfold, you simply cannot sustain a viable dealership regardless of dualing, there are very valuable remedies the law permits in such a situation – the same remedies we employed to accentuate the compensation of Oldsmobile dealers. Keep a watchful eye as this play unfolds.

*By W. Douglas Moody and
Richard N. Sox, Jr.*

Article summary

- GM's consolidation of linemakes is sure to continue.
- GM's announcements related to P-B&G will result in three franchises being reduced to one.
- There are valuable remedies available for losing the value of three viable franchises.
- It is critical to chart dealership value, volume, expenses and profitability along with any lost customers due to lack of previously provided product.

Chrysler Forcing Exclusivity, continued from page 1

Chrysler demanded that those dealers undual by a certain date or else. We asked ourselves “or else” what? We encouraged dealers to respond to Chrysler’s letters by saying that Chrysler could not force these dealers to undual. Once a factory approves your franchise lineup by way of a facilities addendum to your dealer agreement, it is stuck with that lineup unless it can show you do not meet reasonable facilities guidelines and in order to come into compliance somebody has to go. On the flip side, a dealer can never add a new franchise to his or her dealership property until either the factory has approved the request or the dealer has successfully challenged the factory’s denial of that request.

Well, Chrysler must have known all along that the “or else” was an empty threat. As far as we know, Chrysler has done nothing in follow-up to that last threatening letter. Instead, it appears to have taken a more subtle and sinister route in accomplishing its goal to have exclusive facilities. Chrysler appears to now be attempting to convince successor dealers that they have to agree to exclusive facilities before being granted approval to become dealer operators.

Chrysler’s ploy comes in the form of a standard letter asking the prospective dealer to sign the bottom of the letter agreeing to its terms. Those terms include acknowledging certain “keys to operating a successful dealership” one of which is “exclusive/adequate facilities.” No prospective should sign this acknowledgement.

Our concern is that the phrase “exclusive/adequate” is ambiguous enough to allow Chrysler to come back and argue that you agree to exclusive facilities and not merely “adequate” facilities. It is unnecessary for a prospective dealer to put him or herself at risk by signing this acknowledgement because in most states Chrysler must review the application of a successor/prospective dealer based upon the qualifications of the dealer candidate. The issue of adequate facilities is a different matter altogether. As mentioned above, you don’t have to provide exclusive facilities as long as your current facilities are adequate based on reasonable standards. In any case, Chrysler cannot tie the debate over whether the dealership facilities are adequate with the successor/prospective dealer’s request to be appointed dealer operator. The only acknowledgement

that successor/prospective dealers should be making is to agree to always maintain reasonably adequate facilities for the sale and service of Chrysler vehicles – nothing more. Beware of Chrysler’s continuing efforts to force exclusive facilities.

By Richard N. Sox, Jr.

Article summary

- Beware of Chrysler’s continuing efforts to force exclusivity.
- Chrysler is attempting to have successor/prospective dealers acknowledge that a successful dealership requires exclusive facilities.
- Chrysler must review a successor/prospective dealer’s application based solely upon the successor/prospective dealer’s qualifications.
- Chrysler cannot force dealers to undual non-Chrysler franchises.

Venturing, continued from page 1

statutes that simply provide that a manufacturer cannot “unreasonably withhold consent” to a proposed transaction. If you are shopping for a Nissan dealership or another franchise where the factory is currently pushing unreasonable facility initiatives, in which kind of state would you rather have your transaction?

In addition to looking at a state’s dealership transfer statute with respect to the appointment criteria, check to see if the statute sets forth a specific time frame in which the factory must respond to a proposal. Some statutes require that the manufacturer respond within 30-90 days after receiving from the seller a notice of sale. Other states set the clock ticking from the time the manufacturer receives a completed application and all requested information. Still other states don’t have any sort of time requirement, so the manu-

facturer can string out a deal as long as it desires. If the transfer statute provides a timeframe in which the manufacturer must respond from receipt of a notice of sale, the factory usually cannot jerk around with a dealer much when it comes to the application process. If the timeframe runs from receipt of a complete application, the definition of “complete” is in the eyes of the beholder. Where there is no prescribed timeframe, manufacturers often slow walk deals – often in an effort to push the purchaser into **agreeing** to a particular network initiative.

If you, as a buyer, are striking out beyond your state lines, be sure to expand the due diligence inquiry. Carefully review the transfer statute of neighboring states to determine which statute is most favorable given your specific circumstances. By gathering this information you minimize the occur-

rence of surprises and maximize your ability to achieve your expansion goals.

By Robert A. Bass

Article summary

- Dealership buyers looking in different states should, as part of due diligence, compare the dealership transfer protections of the states.
- Some state franchise laws set forth specific criteria that limit the factory’s scope of review of a proposed transaction.
- Look for the time frame provisions under the state statute and use them to your advantage.

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