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

More Factory Horrors Stories

Plus, tips on how to avoid becoming one

In our ongoing discussion of horror stories, we've noticed three key trends that are creating horror stories for dealers in their dealings with factories:

1. Trusting the word of a zone manager that a potential buy/sell deal will meet factory approval is dangerous for dealers.

2. Factories are changing the metrics they use to evaluate existing stores—part of an effort by financially and sales-troubled factories to either eliminate small dealers or consolidate metro-area stores.

3. Up-and-coming factories are working to maintain high, average volume levels at stores and eliminating smaller, rural dealerships.

The underlying message for you is that you *must* be aware of your rights under state laws to ensure you don't fall prey to any of these trends.

Here is an example of a horror story that touches on the key trends. The horror story resulted from the dealer assuming that the factory would approve (as it should have) a buy-sell. The dealer sold his interest in two dealerships and relocated to a new city to take over another dealership. After arriving and completing the negotiations, the factory turned down the purchase because of the performance of one of the dealership line-makes at the stores from which the dealer had just divested.

The dealer was fortunate to have purchased the store in a state that allows a potential buyer to protest a turndown that was unlawful. (At the time of this writing there are only a handful of states that provide protections for a scorned purchaser.) We filed a protest and were able to negotiate a settlement that will allow the dealer to be approved as the dealer operator.

During the application process, in this case, the parties were led to believe by zone managers that the applications were going to be approved and the dealers relied, to their detriment, on these representations.

One recommendation to alleviate this problem: Document conversations with factory employees in writing. Even if the application states that you can not rely on representations from factory employees, the statements are much harder for the factory to deny when you have written a letter confirming statements by factory employees.

You can accomplish this by writing a simple letter to the zone manager or other factory employee memorializing the agreements reached in your discussion. Conclude the letter by stating that if there is anything in the letter that the factory employee does not agree with, then the factory employee should respond in writing immediately.

If the employee is being untruthful and/or making representations without proper authority, then you will force the employee to admit this and you can address the issue prior to investing more time and money. We recently assisted a purchaser in writing a "confirmatory" letter which resulted in a previously turned down buy-sell ultimately being approved.

In previous issues, we've also described horror stores that resulted from factories changing dealers' areas of responsibility in an apparent attempt to set up stores for failure. Recently, a dealer who had threatened to file suit to

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THIS ISSUE

Tips to Ensuring an Organized Buy-Sell

Attorneys are responsible for well-crafted document

A comprehensive, well-organized and clearly drafted agreement for the purchase and sale of a motor vehicle dealership is critical to achieving a successful transaction.

Business people often cringe at the thought of having to review and examine a lengthy agreement, but it is very important that the buyer and seller of a dealership understand their agreement, as set forth in a written document. Clarity and organization will go a long way toward making it easy for the parties to understand both the

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***Horror Stories,** continued from page 1*

protect her rights received a Notice of Default letter after the factory began judging the dealer on market share penetration instead of sales effectiveness. The factory also doubled the size of the dealer's PMA.

When we analyzed the dealership's sales figures, we determined that the dealership was selling as many vehicles as 50 percent of the dealers in the region and was one of the top performers in customer satisfaction. Of course, we immediately prepared a letter to the factory documenting our positive interpretation of the dealership's sales performance. The purpose? If the factory moves to terminate, we have documentation that the factory manipulated the manner by which it judged the dealership's performance to punish the dealer for choosing to protect its rights under state law.

Unfortunately, the factories have agendas that are not in many dealers' best interests. It's ever-more critical to know the factories' plans when you are attempting to purchase or sell a dealership—as well as the state laws that provide you protection from becoming a horror story.

by Martin Hayes, Esq. and Dan Myers, Esq.

Article summary

- Prevent your buy-sell from becoming a horror story by writing a confirmatory letter to memorialize any oral representations from zone managers or factory employees that you rely on concerning factory approval of the buy-sell.
- Know your state laws and the protections they afford.
- Pay close attention to any changes that the factories make in how your sales performance is evaluated.

OSHA/ADA Regulatory Update

Right to Know training, demo drives merit compliance attention

It appears that the federal Occupational Safety and Health Administration has been stepping up compliance inspections of dealerships.

Myers & Fuller has received reports from the field indicating that OSHA is taking an interest in auto dealerships and their service garages. According to OSHA, the most often cited standard, by far, at dealerships and service garages is failure to properly conduct Employee Right-To-Know training. In one northern state, OSHA issued 24 training citations to dealers and service facilities during the most recent one-year reporting period. The citations resulted in more than $7,000 in fines.

"In one northern state, OSHA issued 24 training citations issued to dealers and service facilities during the most recent one-year reporting period."

OSHA also issued numerous citations under standards relating to personal protective equipment, respiratory protection and eye protection.

Dealers should have hand controls available for test drives

Would your store be able to accommodate a customer with disabilities who requests a test drive of a new vehicle?

That scenario resulted in a dealer getting criticized this past summer for refusing to install hand controls in a vehicle to enable the customer to take the test drive. Our reading of federal Americans with Disabilities Act (ADA) regulations suggest that you should provide those accommodations, or you could risk negative publicity or even fines for failing to do so.

Under the ADA, dealerships are considered "sales establishments" and therefore the "public accommodations" ADA calls for do apply. Sales establishments may not discriminate on the basis of disability when providing goods and services. To prevent discrimination, the ADA provides that sales establishments must remove barriers to the accessibility of their goods and services if removal is "readily achievable."

In the case of motor vehicle dealers, the United States Department of Justice (DOJ) issued an interpretation back in 1998 in response to an inquiry by General Motors. The DOJ Opinion Letter suggested that providing hand controls for test drives was a "readily achievable" accommodation. The Justice Department stated that an experienced mechanic generally takes only 10 to 15 minutes to install hand controls.

A dealership that has trained mechanics on site during showroom hours likely could provide hand-controlled cars for a customer to test drive without any advance notice. The customer would simply have to wait for a short amount of time for the mechanic to install the controls on the car the customer desired to drive. In the case where a mechanic is not on site and available whenever a dealership showroom is open to customers, then hand-controlled test drives might only be readily achievable after some limited, legitimate amount of notice.

The issue does not arise often, but when it does, dealers are advised to try and comply with a request. Information on particular control systems is readily available on the Internet.

For more information about the Americans With Disabilities Act and OSHA requirements for dealerships, please contact Myers & Fuller attorneys Robert Byerts or Shawn Mercer.

by Robert Byerts, Esq.

Article summary

- OSHA takes closer look at dealership Right to Know training.
- ADA regs require accommodations to enable test drives.

Franchise Law Protections

Restrictions on additional points of sale

As we continue our series on critical provisions to be contained in a state's franchise law protections, we begin to look at protections from factories adding a same linemake dealership within your market area. In this age of continuing additions of dealerships by manufacturers (despite what many claim is an interest to reduce their dealer body), these restrictions are critical in protecting the investment you have made in your dealership.

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

1. the right for an existing dealer to protest any proposed add point;

2. adequate notice of such an add point;

3. a "stay" of the add point while a protest is pending; and

4. detailed criteria by which a decision-maker (administrative judge, for example) 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.

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 the relocation of an existing dealership (such that the existing dealership is moving within some minimum range, say two miles, from its original location and/or not moving closer to a neighboring dealer with the same linemake).

The definition of an add point should also cover a "back fill" scenario. This occurs when a dealer relocates to a new location within the two mile exception but then has an agreement with the factory to add a dealership at the old location. In many cases, the new point lies within the exception and the old point lies beyond the radius that allows a dealer the right to protest the backfill as a new point. In this situation, the neighboring same linemake dealer just went from having just one competing dealer to having two — without any right to protest. This scenario can be cured by including a provision that says the two mile relocation exception only applies if the old location is not reopened for some period of time, say two years.

• The radius around the new point that triggers protest rights must be of a size that truly protects your territory while (it pains us 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 serves as the primary basis for the right of an existing same linemake dealer to protest an add point. It is equally important to avoid making 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 its 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.

• The last consideration for a proper add point statute is a provision that allows a protest if an existing dealer can establish he/she gleaned a significant amount of sales to customers registered within a 20-mile radius (or 13-mile radius, depending on population) of the add point during any 12-month period over the last, say 36 months. The dealer would need to demonstrate that he/she or a predecessor made something like 25 percent of the dealership's retail sales of new motor vehicles to persons whose registered household addresses were located within that zone. This provision has the effect of protecting a dealer whose market is so unique that he/she sells a large portion of their vehicles outside the traditional mileage radius. The dealer's investment is protected by focusing on the area where the dealer does business 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 that 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 the dealership, the linemake motor vehicle dealerships 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.

by Richard N. Sox, Jr., Esq. and Loula M. Fuller, Esq.

Article 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.

Your Role in Reducing Identity Theft Risks

Complying with the FTC's Final Disposal Rule

The Federal Trade Commission ("FTC") has issued a rule that requires dealers to properly dispose of consumer reports and records derived from consumer reports.

The Final Disposal Rule took effect June 1, 2005 as part of the federal government's effort to reduce the risk of identity theft that is created by the improper disposal of consumer information. The Rule is part of the Fair and Accurate Credit Transactions Act ("FACT Act") of 2003.

So what are the obligations for you?

First some definitions:

Consumer information is defined as "any record about an individual, whether in paper, electronic, or other form, that is a consumer report or is derived from a consumer report." This definition includes a compilation of such records, but it does not include information that does not identify individuals, such as aggregate information or blind data.

"The FTC believes compliance with its Disposal Rule would add 'few, if any, additional compliance costs.'"

Disposal of consumer information occurs when you discard or abandon it, or sell, donate or transfer the information to any medium (including computer equipment) where it is stored.

Now, for a look at specifics for your store. The FTC states that any person who maintains or otherwise possesses consumer information for a business purpose must properly dispose of such information "by taking reasonable measures to protect against unauthorized access to or use of the information in connection with its disposal."

Here are examples of reasonable measures you should use to guide your compliance efforts:

- Burning, pulverizing or shredding papers containing consumer information so they cannot practically be read or reconstructed;
- Destroying or erasing electronic media containing consumer information so that it cannot be read or reconstructed;
- After due diligence, entering into (and monitoring compliance with) a contract with a records disposal company that requires it to dispose of your consumer information in accordance with this Rule. Note that the owner of the consumer information and the disposal company are both responsible for its proper disposal;
- Identifying consumer information (so it can be protected) when providing it to a records disposal company, another service provider or an affiliate;
- Incorporating proper procedures for disposing of consumer information into your written information security program, which is required for business that must comply with the FTC's Safeguards Rule.

[Note: While the Rule requires the proper disposal of consumer information, it does not affect the time period you must retain the information for business, regulatory or other purposes. Therefore, the rule does not change record retention requirements for documents containing consumer information.]

These examples of reasonable measures are illustrative only and are not exclusive or exhaustive methods (or "safe harbors") for complying with the rule. The reasonable measures you must adopt at your dealership should include educating your employees on the proper disposal of consumer information. The reasonable measures standard for disposal provides some flexibility in determining how to comply with the rule based on an circumstances at individual businesses.

The FTC believes compliance with its Disposal Rule would add "few, if any, additional compliance costs" beyond those associated with complying with its Safeguards Rule. The FTC is assuming, of course, that such entities currently have appropriate policies and procedures in their information security program to properly dispose of consumer information.

Compliance costs may be greater for entities not already subject to the FTC Safeguards Rule, since these entities may not have in place appropriate procedures for disposing of consumer information. This may apply to many medium and heavy duty truck dealers since the Safeguards Rule only applies to business entities that obtain information about individuals who obtain a financial product or service primarily for personal, family or household purposes.

In summary, all dealers must review and revise their records disposal procedures as necessary to assure compliance with the final disposal rule of the FACT Act. Compliance questions should be directed to your legal advisor.

The full text of the FTC disposal rule is available at www.ftc.gov/0s/2004/11/041118disposalfrn.pdf. Other Fact Act developments are posted at www.ftc.gov/os/statutes/fcrajump.htm.

by Shawn D. Mercer, Esq.

Article summary

- Dealers must comply with the FTC's Disposal Rule (part of the Fair and Accurate Credit Transaction Act), which addresses how to dispose of documents and data containing consumer information.
- The Rule requires following reasonable standards for educating employees about records disposal, and ensuring vendors understand their obligations.
- Disposal Rule compliance should not create significant additional compliance costs for dealers who already comply with the FACT act.

Organized Buy-Sell, continued from page 1

economic as well as legal aspects of their transaction.

Lack of understanding can lead to problems at closing when a party faces the reality of what was agreed to and is now unhappy with the resulting terms of the agreement. Surprises usually are not a good thing in a transaction. Buyers and sellers are more likely to review a well-drafted, organized and unambiguous contract, and such an agreement is more likely to result in a successful closing.

Here are pointers on how to craft a cogent buy-sell contract:

The opening: The opening of a buy-sell contract should contain an accurate description of the transaction, which would include the identity of each party and summary of the proposed transaction. Is the deal an asset purchase transaction? Have the parties agreed to a sale and purchase of stock? In the case of a multi-line seller, is the seller's entire portfolio of brands the subject of the transaction or is only a single franchise being sold? After the closing, does the buyer plan to operate the dealership in its existing location or will the buyer relocate the franchise? These questions need to be addressed in the agreement.

"An organized and clear agreement will aid in each party's review of the contract and understanding of the parties' respective obligations, burdens, benefits and risks."

Addressing shareholders: Obviously, in a stock purchase transaction, the shareholders are going to be listed as a party; the shareholder is the seller of the shares and thus must agree to the terms of the agreement. In an asset purchase context, sellers (i.e., the dealership operating entity) will often try to keep the shareholders off the agreement. Not surprisingly, shareholders want to avoid personal liability and continue to enjoy the benefits of limited liability by making only the selling corporation liable for breaches of the transaction document. Buyers will want to carefully discuss this issue with their counsel. Nothing is worse than turning to a corporation for indemnification and learning the company has been dissolved. Though I will cover this issue in the future when discussing indemnifications, a buyer of assets should strive to include the seller's shareholders in the agreement, or look for alternative ways to secure seller's indemnity obligations.

Allocating risks: Having identified the parties to the transaction, described the nature of the transaction and briefly explained buyer's plans for the dealership after the transaction, a buy-sell agreement should then set forth the allocation of the parties' respective risks.

In addition to addressing the individual issues above, each buy-sell agreement should contain a minimum of the following parts:

(1) a definition section;
(2) a detailed description of the transaction, that is, what specifically is being sold and purchased;
(3) the purchase price section, which details the pricing of each of the items being sold, as well as any prorations and allocations to which the parties agree;
(4) a section describing any deposit being posted by the buyer and its disposition;
(5) a section setting forth the date and place of closing and providing for any post-closing agreements between the parties;
(6) a section enumerating each parties' respective contingencies for performing;
(7) the deliveries that are to be made at closing by each party should be clearly described in its own section;
(8) sections setting forth the warranties and representations of the seller and buyer;
(9) an indemnification section;
(10) a section containing various sub-agreements between the parties that relate to the transaction;
(11) a section providing for the termination of the agreement and disposition of the deposit; and
(12) a section containing miscellaneous terms (sometimes called boilerplate).

Of course, each transaction is unique and other sections may have to be included depending on the circumstances of the deal.

The drafting of each buy-sell should begin with a framework or skeleton that contains each of the sections just described. Organized in that fashion, the parties will have a comprehensive outline from which to work as they fill in the terms of the agreement. Clearly, some of the terms will be identical from deal-to-deal, but no buy-sell agreement should have a twin brother or sister; each agreement should stand on its own as a clear and unambiguous expression of the parties' agreement with respect to the particular transaction.

An organized and clear agreement will aid in each party's review of the contract and understanding of the parties' respective obligations, burdens, benefits and risks. When each party to a buy-sell transaction understands its rights and obligations, the less likely there will be any problems at closing and the more likely the transaction will be a success.

by Robert A. Bass, Esq.

Article summary

- A seller and buyer must understand what they are agreeing to in a buy-sell contract.
- Each buy-sell agreement should begin by identifying the parties and describing the proposed transaction.
- Buyers should discuss with their legal counsel the need to include the seller's shareholder(s) in the buy-sell agreement.
- A well-constructed buy-sell agreement should contain a number of sections, each of which address an important component of the transaction.

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