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

The Rest of the Story

How the factory evaluates you

Our last newsletter addressed the importance of knowing the geography you are assigned by the factory. This month we will talk about how the factory controls your market share by playing games with the standard of review. The standard of review is the area the factory uses to evaluate your retail sales penetration. Some factories use the national average, others use the state average while others use a regional or district average. You should be aware of the average they use and if you think it is inappropriate you should write them a letter and tell the factory why.

I am sure you have noticed that we advocate writing letters whenever you see something that is not right or concerns you. We can't stress enough how important it is for you to put the factory on notice whenever you see a potential problem. It not only helps with your factory/dealers communication, but it also builds a written record of concern in case you ever need to defend yourself. Why do you care? **If you are ever accused of being a poor performer and the paper trail is made up solely of correspondence from the factory, YOU WILL LOSE!** Factories are great at notifying you of changes whenever they occur. They do this to put you on notice of the change and to act like they gave you a chance to respond. If you don't respond you accept the change and silently agree that the change is appropriate.

A classic example of this is the way GM changed the standard of review from the national average to the state average. What is the big deal you may ask? **State average will be impossible for all the dealers in a state to achieve.** In fact only about half will achieve it!

continued on page 2

Legislative Initiatives

Updating your state law regularly

The federal government and virtually every state have laws that purportedly give the dealers protection against wrongful termination of their dealer agreement. The federal government passed the Dealer Day in Court ("DDCA") back in the 1950s for the express purpose of protecting dealers' investments from factory overreaching by wrongful termination. The DDCA proved to be ineffective because, in order for the dealer to prevail, the dealer had to prove that the manufacturer was illegally "coercing" the dealer. The "coercion" standard has sometimes required the dealer to prove actual malice on the part of the manufacturer. Needless to say – the DDCA was ineffective for its stated purpose and state legislatures began passing laws to protect the dealers from wrongful termination.

Most state laws do not include the element of "coercion"– yet many (if not most) remain ineffective. WHY? There are two primary reasons: 1. There is no "automatic stay," allowing the dealer agreement to remain in full force and effect throughout the litigation, including all appeals; 2. There is no right to sell the dealership throughout the litigation, including all appeals.

continued on page 4

THIS ISSUE

Important Issues to be Covered in a Stock Transaction

Are the sales of dealerships using a stock or merger transaction (rather than through the use of an asset purchase transaction) on the upswing? In the last several months, I have discussed the structure and application of stock transactions with several dealers, and in the last nine months, I have participated in three deals of that nature. Are stock sales of dealerships returning to the forefront? If so, what is the importance of this trend to you as a dealer?

Having the choice, most parties to a buy-sell transaction, be it an automobile dealership or other type of business, prefer the asset purchase route; however, where a dealership is a c-corp with substantial built-in gains, LIFO issues, or saddled

continued on page 3

The Rest of the Story, *continued from page 1*

Florida is a great example of this problem. Florida is a long narrow state that has the majority of its dealers located in seven major metro markets. If you are located in Miami, Fort Lauderdale, West Palm, Tampa, Orlando, Jacksonville or Pensacola you have a vastly different competitive atmosphere than dealers in say Perry, Chiefland and Snowflake. We all know that the larger metro markets have at least one of every linemake represented and in most cases more than one. If you are a Chevrolet dealer in Tampa (Tampa/St. Petersberg) you have at least five or six other Chevrolet dealers to compete with plus the same number of Ford, Chrysler and Dodge dealers. Toyota, Honda, Hyundai, Nissan, BMW and all the other import brands have several dealerships also. Obviously competition in the metro markets is crowded and intense. **Crowded, intense competitive markets are not the place to achieve high retail market share.** Go to a small, rural market and you may find a Chevrolet, Cadillac, Pontiac, Buick, GMC dealership (located in one building) competing with a Chrysler/Dodge (one building) and Ford store. There are no Lexus or Mercedes, no Toyota or Honda stores. This type of market consistently results in the local dealer achieving much higher retail market share than the dealers in the metro markets. This is not just true in Florida. Go to other states like Mississippi, Montana, Arkansas and Texas and you will see that the same penetration pattern exists. What this means in the real world is that the state average is not a reasonable standard for all the dealers in a particular state. If you are in the rural area with little competition you will have a higher market share than the dealer located in the metro fighting a multitude of competition.

We have looked at the market share results for Chevrolet dealers in Florida for years and the metro dealers market share is almost always lower than the market share achieved by the rural dealers. GM knows this and still holds the dealers to a standard that it knows is not reasonable. The reason GM does this is to be able to claim that the metro dealers are not doing their job. If the metro dealers are not doing their job then GM is justified in adding additional dealerships into the metro markets.

Nissan uses a regional average as its standard of review. I am familiar with a situation where a dealer in a state with 10 other Nissan dealers got the hook for failing to meet the regional average. All the dealers in the state were assigned to the same district and only one dealer in the district could meet the regional average. Does this sound like a reasonable standard of review? The stories go on and on.

We have been telling you for the past few years that all the factories have network initiatives that may or may not include you. **Each factory knows how many dealerships it wants to have and who it wants to own them.** If you are not one of the chosen few then the bullseye is on your back and the arrow the factory may use is the failure to meet the minimum sales requirement contained in the sales and service agreement. That minimum sales requirement must be both reasonable and achievable. If you see that the standard you are being judged by is not reasonable then it is your job to sit down, write a letter, and tell the factory, **BEFORE THE FACTORY TELLS YOU.**

By Daniel E. Myers & Martin Hayes

Article summary

- Know how the factory evaluates your sales and registrations performance
- Know the standard of review (national, state, regional, district or something else)
- Let the factory know if you think the standard is inappropriate and why
- Take your yearly evaluations to heart and respond to them each time you are given a poor report card

The Legacy of the Oldsmobile

Discontinuance – Pontiac, Buick and the Sprinter Van Franchises

Were Bob Lutz' refreshingly honest comments admitting that GM would consider discontinuing a linemake such as Buick or Pontiac a surprise to you? If so, it is time to be a realist. December 12, 2000 was the date of the landmark announcement that GM would be terminating the Oldsmobile linemake. Since that time, we at Myers & Fuller have been warning dealers that other GM linemakes, as well as other manufacturer linemakes, could be next. Indeed, most recently we have seen the Sprinter Van dealers notified that their linemake is slated for termination by Chrysler. Like Oldsmobile dealers these dealers are being offered an insultingly small financial assistance package which Chrysler is using to obtain the Sprinter Van dealer's agreement to release Chrysler of all liability associated with the termination of the linemake.

A lot can be learned from our battle with GM on behalf of numerous Oldsmobile dealers. Through our representation of some 30 Oldsmobile dealers who pulled the trigger on suing GM to obtain the rightful value of their franchise we learned that GM sees the Cadillac and Chevrolet linemakes as their "bookend linemakes." **All other linemakes are on a short rope.** Proof of that is to take a quick look at the orchestrated demise of Oldsmobile in comparison to, for example, recent changes to the Buick lineup. Over the years that preceded the fateful day of the Oldsmobile termination announcement, GM systematically did away with Oldsmobile's stalwart models. First it was the 98, then the Cutlass and finally the Aurora. In exchange for these histor-

ically successful models GM used Oldsmobile as a guinea pig to test out sleeker new designs in the Alero and the Intrigue. Ultimately, GM has utilized portions of these designs in other linemakes. What has GM done with Buick over recent years? The traditional form of the Regal has been discontinued. The Riviera is in the scrap heap. In exchange are sleek new models. This could just be a coincidence but I wouldn't bet the farm (or the franchise) on it.

GM's evolving approach to its franchise lineup makes perfect sense from its point of view. The imports, especially Toyota, are kicking GM's butts. When GM looks at how Toyota is doing it, it finds that its competitors have a much more focused vehicle lineup. GM has to ask itself – how many different ways can a factory design a four door sedan or SUV? If you are willing to spend big bucks on totally separate raw materials and production capacity then the answer is many different designs, but, GM long ago decided it could not afford to do that. The result has been shared and overlapping designs among the various linemakes. Hence, the inability to compete against more focused competition. It is only natural for a manufacturer like Toyota to be more cost efficient when it has less than 10 models to focus on while a manufacturer like GM has dozens of vehicles across its linemakes.

The reality of the situation is that GM's decision to discontinue another linemake or two makes good business sense to GM. Every one has their opinion as to which linemake, if any, should be terminated. What is important for all dealers to understand is that **legally a manufacturer of a product in the United States cannot be forced to continue to supply that product to its franchisees** even in the case where there is a franchise agreement that grants rights to the franchise for some specific period of time. What we believe a manufacturer cannot do, however, is walk away from those franchisees without paying them the going-concern value of the franchise which has unilaterally been taken from them. Every state's automobile franchise law provides that **you as a dealer have the**

continued on page 5

Important Issues to be Covered in a Stock Transaction, continued from page 1

with other unfavorable tax burdens, a stock transaction may be the best, if not the only viable way for a dealer to sell the dealership.

I have preached for some time to our clients about the **importance of a buyer expanding the due diligence inquiry to include (i) an analysis of the existing relationship between the target dealership and the factory and (ii) an analysis of the dealer network initiatives the factories are imposing on the particular franchises held by the target dealership.** Those sermons were most often in the context of asset purchase transactions. The importance of a buyer expanding the due diligence inquiry becomes all the more critical when it comes to a stock transaction.

It is elementary that in a stock transaction the target dealership generally will continue to be bound by all its contractual obligations and be held responsible for its past actions and performance under its agreements and contractual relationships (unless otherwise specifically agreed to by the parties). That is, the sale of the dealership's stock to a new owner does not relieve the dealership of its then existing contractual obligations or from liability, past or future, to which it may be exposed. As a result, a buyer of stock becomes, albeit indirectly, responsible for complying with factory requirements that were previously imposed upon the dealership. Thus, it is critical to obtain copies of any "side agreements" (agreements other than the dealer sales and service agreement) entered into by the seller. In addition to obtaining copies of any such agreements, because some dealers don't keep the best records, it will be very important to include a representation in the stock purchase agreement that the seller has provided all side agreements to the buyer. As a buyer you would hate to find out that your dealership is subject to an exclusive use or other type of site control agreement. If the buyer doesn't carefully analyze that issue prior to entering into the stock purchase agreement, there may be unpleasant surprises.

A buyer who is considering a stock purchase should pay close attention to the factory's dealer network initiatives (many of which are and will be outlined and discussed in this newsletter) that may affect the target dealership. Consult professionals who are familiar with the initiatives. Whether it is a stock purchase or an asset purchase, buyers should build a team of professionals who are familiar with the initiatives, can analyze the impact upon the dealership, and examine the legality of the initiatives in light of applicable state and federal motor vehicle dealer franchise laws.

By Robert Bass

Article summary

- Stock purchase agreement as versus asset purchase agreements are becoming more prevalent
- In a stock purchase of a dealership the buyer is exposed to all pre-existing liability associated with the dealership
- Important to analyze the existing relationship between the dealership and manufacturer
- Important to analyze the dealer network initiatives the factories are imposing
- Buyer may be responsible for any side agreement entered into with the factory by the selling dealer

Legislative Initiatives, continued from page 1

If your state statute does not provide the dealers with these rights, then a dealer under threat of termination cannot risk his/her entire investment by going to court to find out if the proposed termination is "wrongful."

States like West Virginia (that passed these amendments to the termination section of its law this 2005 legislative session) know how hard it is to get this legislation passed. The manufacturers fought Ruth Lemon, the executive director of the state association, all the way to the bitter end, trying to prevent dealers in West Virginia from having an opportunity to have a hearing/trial on whether a proposed termination is wrongful. This issue came to the attention of the state association because a dealer who was threatened with termination could not afford to take the case to trial because, if he lost, he would have nothing to sell. He has other dealerships and has never had a problem with any other manufacturer. It was his belief, and the belief of our firm, that if this case could have gone to trial – the dealer would have won. But, the risk of loss was too great to get the answer. This unnamed dealer got active in the association, and working with Ruth and the other dealers, got these important amendments passed.

Even when the statute makes the factory continue the franchise relationship pending the outcome of a trial or an appeal, they still try to play games. For example, many years ago we argued a case against GM in Florida where the state law authorized an "automatic stay" during the litigation. In other words, the dealer agreement would remain in place throughout the litigation while the dealer challenged the proposed termination. To make a long story short – the dealer lost at the trial level and appealed the case. While on appeal, the owner of the dealership tried to sell the dealership and the manufacturer took the position that the only thing the dealer had to sell was a "terminated dealership!" That is to say, the factory took the position that only the remaining term of the franchise agreement was transferable. We took them on and won. GM, however, is a slow learner! Lo and behold I recently heard of GM doing the same thing in another state just last week. Guess we will just have to teach it again!

One more war story for the books. A dealer received a notice of termination and a petition was filed on his/her behalf in state court asserting the termination was wrongful. Since that state did not have the protections addressed in this article, an emergency hearing requesting a "stay" was scheduled. Because there was a short time frame before termination became effective, the hearing was scheduled as ex parte (only one side appears), with the purpose of getting a temporary order. Another hearing would follow where both parties would make their arguments regarding a "stay" pending the final hearing. Despite the fact that the hearing was supposed to be ex parte, the manufacturer's attorney came to the hearing and represented it had no objection to the "stay." Relying on that representation, the state court entered an order "staying" the termination and did not schedule another hearing because the manufacturer represented it had no objection. Shortly thereafter, the manufacturer moved the case to federal court. With the case now in federal court, the factory pretended not to remember it had agreed to continue the franchise relationship pending the outcome of the trial and on the 90th day turned off the dealer's computer and closed his parts accounts. It tried to eliminate the dealer's ownership and ultimately his assets by claiming that if the dealer was terminated and if the termination was wrongful, the dealer could sue for damages. We flew up and camped out in the federal judge's chambers and, when allowed to meet her, argued that it would be a travesty if the factory could put the dealer out of business without a day in court. The manufacturer argued that although it had appeared at the state court hearing, it made no representation regarding whether or not it objected to the "stay." Truth is obviously not important to some factories. No court reporter had been at the state court hearing because it was to be attended by only one side and the notice was too short for the court reporter to get there. In a nutshell, the federal judge refused to enforce the state court's order, saying that notice was too short and there was no evidence that the manufacturer represented it did not object to the "stay." The dealer was forced into a settlement while completely under the gun. Shortly after that we rewrote that state's law to insure that nothing like that could ever happen again.

"Most state laws do not include the element of 'coercion'— yet many (if not most) remain ineffective. WHY?"

The legislative mantra is to GET INVOLVED with your state dealer association, identify changes that need to be made to your statute – you never know when YOU will need it. If the termination section of your state statute does not have the two protections identified in this article – then the dealers probably do not have protection from wrongful termination.

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

Article summary

- Every state should have termination protection
- Termination protection must include:
  1. An automatic stay of termination throughout litigation, including appeal;
  2. Being able to sell a dealership throughout litigation, including appeal
- Get involved with your state dealer association
- Identify changes that need to be made to your state statute

The Legacy of the Oldsmobile, continued from page 3

right to renewal of your franchise agreement at each expiration as long as you do not do something that gives the factory the right to terminate you (i.e. commit a fraud or other violation of the franchise agreement). Those laws state that you can only be terminated for "good cause." Most states' automobile franchise laws specifically list the items which qualify as good cause. In every state, the items that qualify as good cause center upon some action by the dealer. A good cause termination is not defined in terms of something the factory does such as "termination as a result of a market withdrawal by the manufacturer." We believe the various state legislators did not include such language because they did not intend to allow a factory to up and terminate your franchise without being held accountable. Otherwise, the factories would only be required to pay you the pittance of termination "benefits" called for under the dealer agreement and most state laws (buying back of certain special tools and new vehicles on your lot). That result defies the years of investment of money, sweat and time that dealers make to create the goodwill which leads to a valuable dealership.

It is critical for the remaining GM dealers, Sprinter Van dealers and other multi-line dealers to learn from the legacy of the Oldsmobile discontinuance. In the weeks following the announcement of the termination of Oldsmobile, Myers & Fuller counseled some 300 Oldsmobile dealers on their legal rights vis a vis the going concern value of their franchise that had just been yanked out from under them. At the time of the announcement there were approximately 2,700 Oldsmobile dealers around the country. Despite our national push to educate dealers on their rights through industry periodicals such as *Dealer* magazine, only 11 percent of the dealers sought expert legal advice. Out of those 300 dealers, only 10 percent of those dealers ultimately sought to enforce their franchise law rights. Of course, there were several of those 300 dealers who were able to negotiate a settlement over and above the transition benefits offered by GM without involving a franchise lawyer. Nevertheless, the number of dealers who were willing to go to war with the General was a small minority. Those dealers that went to battle have received settlements that include benefits which far outstrip what was being offered under GM's "Transition Financial Assistance Program." Unfortunately, **the legacy of the Oldsmobile discontinuance is that, in the grand scheme of things, GM got away with murder.** Even considering the dealers who stood up for their rights, GM has paid pennies on the dollar in comparison to the fair market value of each of the Oldsmobile franchises as they existed on December 11, 2000.

"It is critical for the remaining GM dealers, Sprinter Van dealers and other multi-line dealers to learn from the legacy of the Oldsmobile discontinuance."

In defense of those Oldsmobile dealers that ultimately accepted the transition monies without going to war with GM, this was the first time a major linemake had been terminated. **Terminate a linemake once – shame on GM – terminate a linemake twice – shame on the dealers.** Pontiac and Buick dealers, Sprinter Van dealers, as well as any other dealer representing a multi-line manufacturer can no longer hide their heads in the sand when it comes to the possibility of their franchise being discontinued. Shame on you if you don't take steps to protect yourself the best you can. There are several steps that should be taken. First and foremost, it is imperative for Sprinter Van dealers today, and dealers representing a linemake discontinued in the future, to reject the "transition package" offered by the factory and fight for the value of your franchise. Every dealer has state franchise laws that can be taken advantage of in an effort to receive the going-concern value of your franchise. Second, every dealer should be lobbying (and financially backing) their state dealer association to pass legislation which expressly provides that a dealer shall receive the "fair market value" of their franchise in the case of a termination without good cause. Third, every dealer should enter into every transaction related to your franchises with your eyes wide open. If you are being asked to spend money on your facility or to enter into a side agreement which ties up your property for some length of time, as an example, have an experienced automobile franchise lawyer guide you through the process of documenting protections which give you a strong foundation for demanding reimbursement of monies spent or which allow you to unwind an onerous side agreement when the day comes that you are told your franchise is no longer viable from the factory's standpoint.

These are desperate times for automobile and truck manufacturers. Dealers have become a mere pawn in the game of maintaining manufacturer profitability. Learn from the legacy of Oldsmobile – when it's nut cuttin' time there is no loyalty toward the dealers. **BEGIN PROTECTING YOUR FRANCHISE TODAY!**

By Richard N.Sox, Jr.

Article summary

- Sprinter Van dealers as well as Buick, Pontiac and other dealers for multi-line manufacturers should learn from the legacy of Oldsmobile
- Manufacturers have a right to discontinue a linemake but must pay damages
- Dealers must fight to receive the going-concern value of their franchise
- Dealers must support their dealer associations in an effort to amend the termination provisions to include a manufacturer's duty to pay fair market value upon discontinuance
- Dealers must enter into every transaction with the factory with the thought that the franchise may be terminated in the short-term

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