

CHARAPP & WEISS, LLP

DRIVING YOUR SUCCESS

YOUR FRANCHISE: AVOID THE TOP TEN REASONS FOR TERMINATION

For many years, auto dealers have fought for state laws to protect their franchises against termination at a manufacturer's whim. That is only fair. A family that puts its life into developing a franchised business shouldn't have their livelihood destroyed because the manufacturer just wants to punish a dealer that does not kowtow to it or because it wishes to take over the dealer's business for itself.

All states give dealers protection against arbitrary terminations. The specific language varies from state to state, but generally lawyers shorthand these protections as a requirement of "good cause" before a manufacturer can terminate or refuse to renew a dealer's franchise. These state laws haven't stopped manufacturers from veiled or even outright termination

threats for whatever this month's hot button may be. Not selling at state average? Not meeting the average on the manufacturer's skewed and unscientific CSI measuring stick? Not selling as many new cars as your facing competitive brand dealer? You haven't relocated next to the new big box store in town? You may get a letter. It will be authored by the manufacturer's legal department, and it will tell you what you are doing wrong. Somewhere in the letter you will be told that the manufacturer "reserves its rights to seek any remedies". That is shorthand for "you better get in line or we are going to terminate you."

Most of these letters are simply law department boiler plate. It is often

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BUYING AUCTION VEHICLES: A GREEN LIGHT IS PROTECTION BUT ONLY IF YOU MOVE QUICKLY

Dealers often seek the protection that buying a vehicle under a green light at an auction can provide. As opposed to a purchase on a yellow or a red light which is an indication of problems, a green light for an auction vehicle generally means that it is free of title problems and serious conditions that can negatively affect its value. Dealers should be aware, however, that green light protections are only effective if a dealer quickly discovers a problem and advises the auction of it.

Auctions operate according to rules to which a dealer agrees when registering. These rules explain the various lights under which a car is sold and the complaint/arbitration process for a dealer who is

dissatisfied with the represented condition of a vehicle. The rules do one thing that is critical for a dealer – they establish a very short period for bringing to the attention of the auction issues with the vehicle's title or condition. That period varies based on the problem found, but it may range from as little as two days after receipt of the vehicle at the dealer's place of business to 21 days after purchase. A request for assistance after the applicable time period has expired may well result in a refusal because it is untimely.

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hard to know whether they are part of a file being built to eventually justify termination or whether they are sent as a warning shot even though the franchisor's staff lawyers know that a termination proceeding against you is a doomed fight.

Nevertheless, there are certain circumstances about which a dealer should be quite concerned. Here are the top 10 problems that can actually lead to a notice of termination of a dealer's franchise. Avoid these situations. A dealer who gets a termination notice will be in for a major fight to keep its franchise.

1. Lack of Capitalization. All manufacturers have capitalization standards. Whether it is net worth, net working capital, or a combination of both. Continuing and serious impairment is a problem, and it is a rather simple matter for a franchisor to march its accountants into court to demonstrate why.

2. Loss of Floorplan. Every manufacturer requires a floorplan line. A manufacturer draws against the floorplan line to pay for new vehicles it ships to dealers. If it doesn't get paid for vehicles, it doesn't ship vehicles. If it doesn't ship vehicles, it doesn't stay in business for very long. Lose your floorplan, and you will lose your franchise.

3. Bankruptcy. While a dealer's bankruptcy will be a breach of its franchise agreement, a dealer's bankruptcy won't automatically lead to termination of its franchise. The automatic stay in bankruptcy will prevent that. However, there is no evidence that any franchised dealer has gone through a reorganization bankruptcy to emerge with its franchise. Generally the franchise is either cancelled or it is sold as part of a bankruptcy proceeding.

4. Apathy. There are many requirements on a dealer in a franchise agreement. There are many reasons why a manufacturer can be unhappy and generate a warning letter. A committed dealer responds and takes action to address any problem that may actually exist. A dealer who does not respond looks to a franchisor like it doesn't care. Eventually, a manufacturer comes to believe that a dealer that doesn't care won't fight for its franchise, so why not send a termination notice?

5. Lack of effort. The most common reason for a manufacturer threat to a dealer is because of a claim that the dealership is not selling enough new cars. After all, the manufacturer makes money when it sells new cars to a dealer who will only keep buying cars as long as it is selling them. Most of these warnings never materialize into terminations because dealers either take the time to solve problems that are hindering sales or they explain why the manufacturer's standardized methods of calculating sales efficiency are an inappropriate measure of the dealership's true performance. From time to time, a dealer will simply make no effort to either address the cause of manufacturer dissatisfaction or to take issue with the manufacturer's calculations. The poor sales will simply continue with no explanation until the manufacturer sends a termination notice.

6. Conviction of a Crime. Manufacturers want dealers who are upstanding citizens. Dealers convicted of a felony or of certain misdemeanors (depending upon the definition in the franchise agreement) will find themselves subject to termination. Occasionally, a dealership itself will be indicted for a crime such as money laundering. That is a death sentence.

7. Loss of License. Every dealer agreement provides that a dealership must have the appropriate state licenses. Behavior that is serious enough to lead to suspension or termination of your license to operate as a dealer will put you in breach of the franchise agreement. If you are not open, you cannot sell and service vehicles. Loss of your state dealer license is a death sentence for your franchise.

8. Fraud. Many dealers have been victimized by employees. Sometimes, that victimization extends to claims for compensation from the manufacturer under warranty and incentive programs. Where the fraud is sufficiently systemic and long standing that the dealer should have known of it, and it appears to the manufacturer that the dealer did not take the steps necessary to prevent it, the result may be a termination notice.

AN ALTERNATIVE VIEW ON UNION INFORMATIONAL PICKETING

There has been a great deal of recent industry publicity concerning the UAW's announcement that it will be picketing selected car dealerships to bring attention to efforts to unionize workers at domestic operations of import name plate manufacturers. Dealers are justifiably concerned about picketing of their dealerships. It generates negative publicity, it causes distraction in the workplace, and it potentially upsets customers.

Unfortunately, there isn't a lot that an individual dealer targeted by a union for informational picketing can do. A union has the right to make its views known through picketing, provided it does not cross the line (literally with respect to improperly coming onto your property and figuratively with respect to behavior such as blocking the entrances to your business). So it does no good to get upset. Picketing is outside your control. The real question is how best to deal with it. Here is an alternative view you may want to consider.

1. Don't overreact. The purpose of informational picketing is to get attention. An overreaction leading to a confrontation will simply feed that purpose. Take it in stride.

2. Take advantage of the publicity. News crews at your store to film the events? Don't issue a "no comment". Make yourself available to the press. You've worked hard to be a notable business where picketers think they will get noticed. You don't have to comment on the purpose of the picketing. It's not your fight. But you can comment on how gratified you are that the union felt it would get noticed at a business you've worked so hard to make a landmark in the community, and people should visit to see why your business is so noteworthy.

3. Treat the picketers well. They are potential customers. If it is a cold day offer them coffee. If it is a warm day offer them soft drinks. Your business treats everyone well.

4. Offer service specials. The picketers are there anyway. They got there somehow, probably by car. Maybe they need an oil change or a tune up. Offer them a "picketer's service special".

5. Sell the picketers a car. Presumably, they're union workers. These days finding a customer with a job is

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9. Change of Control without Consent. A franchise agreement names the equity owners and the dealer. Any change requires consent of the franchisor. A manufacturer may overlook minor adjustments in ownership percentages among approved equity owners. But a sale of equity to someone who has not been approved by the manufacturer will be a problem. And a sale that results in a change of control of the dealership without franchisor approval will be a major problem.

10. Breach of a Supplemental Agreement. Dealers often sign contracts with manufacturers that are separate from or that are supplements to a franchise agreement in which they promise to build a new facility, to relocate, to meet certain sales requirements, or for other purposes. Dealers sometimes fail to recognize how these supplemental agreements can affect them. They establish performance standards to which the dealer agrees. "I agree that my facility is substandard and must be improved" or "I agree that I am not selling enough cars and I must improve." The failure to meet a standard to which the dealer agrees can be viewed as good cause for termination. That is why a dealer should never sign an agreement requiring performance unless it knows it can meet the terms and it consults with a knowledgeable attorney.

much of the battle. Folks with jobs are walking outside your showroom.

In short, while no dealer wants to be the target of a picket line, these are short term events designed to generate as much publicity as possible. Since there's nothing you can do to stop it, at least take advantage of the opportunities it provides.

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TIPS ON PREPARING FOR 2012

As 2011 comes to an end, dealership personnel are working hard to close out the year. General office personnel are probably working with checklists from the dealerships' outside accountants. Here are a few things that dealers should consider to close out the year and to begin 2012.

 Do a quick LIFO calculation now. Natural disasters in Japan and Thailand have had an impact on the availability of vehicles from some manufacturers. Hot sales of some models have depleted dealer supplies even where manufacturing has not been affected by natural disasters. The volatile economic situation has kept all dealers concerned about excess inventories so that hot sales and unavailability of vehicles have left their new car inventories severely depleted. Depleted inventories might have an impact on a dealer's LIFO reserve leading to "income" from a LIFO reversal. Do a quick calculation now. If you foresee LIFO issues, consult your accountant immediately to discuss methods to blunt the impact of this problem.

 Notification of 8300 Form Filings. The deadline for notifying customers whose transactions in 2011 led the dealership to file IRS Forms 8300 regarding the receipt of cash in excess of \$10,000 is January 31, 2012. These notifications should be on the dealership's checklist to ensure that all customers with reported transactions have been or are notified of the filing. And, while the dealership is considering notification of customers, it should also determine if it has filed all the required IRS 8300 returns for the year. If the general office has not been running a regular 8300 report through the company's computer system, this is probably a good time to do so. Even though an IRS 8300 filing may be late, a late filing is much better than no filing whatsoever.

 New NLRA Poster. Effective January 31, 2012, employers covered by the National Labor Relations Act (most dealers are covered) must post a notice of employee rights under the law. The notice is controversial because its detractors contend that there are no statutory basis for the required notification that employees have the right to join a union and to engage in concerted activity with respect to wages and working conditions. Pay close attention to industry

publications on this since the poster requirement has generated substantial criticism and several lawsuits, so a further implementation delay is possible. As of the time that this is written, however, the poster must be printed on one 11 x 17 page, or two 8 1/2 x 11 pages taped together and prominently posted. The poster is available at www.nlrb.gov.

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A dealer cannot assume that a vehicle it buys under a green light justified that designation. Look for problems immediately. If you do not discover problems, and you are confident that you can sell the vehicle to your customers as a sound used car, then do so. But if you find there is a problem, take action. What should you do?

- Run a vehicle history report. If you haven't done so already, run a vehicle history report when the vehicle hits your lot. As we have written repeatedly, vehicle history reports are not always accurate. There can be problems in a vehicle that are not reported. But if there are problems reported on the vehicle history report, that is something you must look into.
- Look at the title history. Is there any notation or prior title-holder evident on the title to cause a concern? Also, in some states with online title processes dealers have access to the title history within the state. That may be of limited help if the vehicle comes from out of state, but one never knows if the vehicle has an in-state title history.
- Inspect the vehicle. Look at it. Are there tell-tale signs of serious damage or evidence of flooding? Put the car up on a lift. Is there evidence of serious structural damage or significant work on the undercarriage?
- If you find a problem, notify the auction immediately. Explain the problem. Provide any corroborating information. Request relief.