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A NEW DAY RISES, BUT WITH MORE OF THE SAME

By Peter K. Bauer

The economy is on an upswing. Slow, but on an upswing. While the lending and housing markets are slow to rebound, vehicle manufacturers are seeing vehicles moving off dealer lots at a quickening pace. At the major auto shows, such as Los Angeles and Detroit (as well as at the Philadelphia, Pittsburgh and Harrisburg shows), new product was everywhere. Some new product was driven by the need to remain competitive, other new product was driven by government safety and fuel mileage requirements. There were electric, turbo and diesel vehicles for increased mileage, while electronic content is expanding to appeal to a demanding customer base looking to be entertained and informed.

And the competition is fierce! Quality across the product segments from sub-compacts to crossovers to luxury vehicles is at a virtual dead heat, leaving customers with no reason to leave a brand, as the disappointments in the vehicle ownership experience are few and far apart. That leaves vehicle manufacturers scrambling to differentiate their product lines from others in the marketplace. With product being nearly equal, the manufacturers have refocused their sights (again!) on their dealer body to further elevate the buying and service experience to win over new customers, and to keep those in the family happy.

Improved Buying Experience via Increased Throughput

Evidence of this push for a grander and glorified buying experience has had a real impact on all dealers. The push to decrease the number of dealers (and increase sales for the remaining dealers) has come from not only the Chrysler bankruptcy eliminations and GM wind-downs, but also from other manufacturers looking to

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reduce the number of dealers in a given market. Even Volkswagen, Volvo and Suzuki trimmed their dealer levels in the past years.

And it is no secret Lincoln has had the big push on in the metro markets, including Pennsylvania. Ford has even tied itself into the shrinkage process with Lincoln by trying to get dealers to consolidate Ford and Lincoln dealerships based on the proximity to each other. Ford has not only done this by seeking dealers to buy each other out, but Ford has also issued notices of poor sales performance, setting the stage for possible termination of a dealer's franchise (with not-so-subtle hints that a relocated or renovated facility might help boost sales). Lighting a fire by threatening termination as a tool to increase sales is tolerable, but it appears the ultimate goal is for the dealer to succumb to the unstated but related pressure to sell out to the neighboring Ford dealer to "help" consolidate the marketplace. But Ford is not alone in sending deficiency notices to dealers. Toyota, Honda, Nissan, Volkswagen and Subaru, to name a few, have also been issuing poor sales performance and other deficiency notices to dealers in an effort to secure a desired result, whether that be increased sales, renovated facilities or reducing the size of the dealer body.

The collective manufacturers' view is that reduced dealer count results in increased throughput for remaining dealerships. This will, the theory goes, give dealers more profit to improve the customer buying experience through enhanced facilities, treatment and services. While this may be commendable, customers may not behave as manufacturers planned. With competitive dealers located near a closed dealership, some customers will not drive to the next closest, remaining same line make dealer. Instead, the customers are buying from another line make franchised dealer located in their neighborhood, or on their commute. While manufacturers believe it is the vehicle brand customers are loyal to, it is the dealership's local relationship that fosters brand loyalty. Recently, a dealer, who lost a franchise as a result of the manufacturer bankruptcies and acquired a new franchise, boiled it down further: the staff on the sales and service floor are the real ties that bring a customer back. The dealer noted, a customer buys a vehicle based on how well the salesperson can match a vehicle to the customer's needs, not based on brand loyalty. This is as opposed to the surviving brand being available across town, or even to the dealer's prior manufacturer's sister franchise being located across the street.

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Using the Carrot, Not the Stick

Instead of using the franchise agreement provisions to threaten termination, other manufacturers are using the tactic of tying monetary payment under incentive programs to drive a dealer to the results the manufacturer has set out in the franchise agreement. For example, if a dealer does not meet a manufacturer's exclusivity or image requirements, the dealer is denied incentives or payments. This has forced some dealers to quickly segregate or upgrade facilities, or to remove a non-compliant franchise in order to qualify for incentive money. In many instances, compliance was driven by competition within the franchise line.

Specifically, if a neighboring dealer qualifies for the incentive money, then the other dealer needs to qualify in order to sustain area pricing levels. How these types of programs are structured can result in a program being in violation of the Pennsylvania Board of Vehicles Act ("Act"), such as where the incentive is paid out resulting in a different price being charged for the vehicle provided to dealers (or as a result of vehicle sales made by dealers).

As of now, manufacturers have not elected (on a wholesale basis) to take dealers to task for not meeting sales performance goals and/or not complying with the facility requirements of a franchise agreement; nor have they sought (in a broad fashion) to terminate any dealer for failing to remove a non-compliant franchise from a dealership facility. However, a manufacturer's decision not to exercise more extreme remedies to date does not preclude the use of its rights in the future.

New Day with More of the Same

Many manufacturers, including Ford, GM and Chrysler, are displaying a renewed sense of "swagger" as sales increase, and as some manufacturers achieve additional market share increases. With this renewed sense of vigor, we see vehicle manufacturers looking to franchise agreements (or prior side agreements) to force dealers to follow through on obligations or commitments. These include de-dualing, making promised facility upgrades, relocating or building at a new location, and meeting sales performance requirements.

However, the Act offers a dealer substantial protections from a manufacturer's onerous requirements. The Act is designed to level the playing field between manufacturer and dealers. Pennsylvania's Dealer Board serves to enforce the Act's provisions in a fair and equitable manner for all involved. For the dealer there are protections from:

1. **Threatened Termination for Poor Sales Performance (or for Not Fitting into Market Plans)** – a manufacturer needs "just cause" to terminate, §8(a) of the Act;

2. **Requirements to Construct Exclusive, or to Relocate or Renovate Facilities** – facility upgrades required only where economic and business considerations justify the investment, §12(a)(6)(i) and (8) of the Act;

3. **Not Allowing the Dualing of Franchises or Requiring Undualing of Franchises or Exclusive Franchises** -- expedited process to allow dealer to dual franchises, §12(a)(6), or undualing/exclusive franchises only where economic and business considerations justify the investment, §12(a)(6)(ii) - (iii) and (a)(8) - (8.1) of the Act;

4. **Revised Area of Responsibility** – right to protest modification of a franchise that materially alters agreement, §12(b)(10) of the Act; and

5. **Incentives that Alter Dealer Versus Dealer Vehicle Price** – pricing must be the same for each dealer, §12(b)(18) of the Act.

So as the economic horizon brightens on a new day, the manufacturers are refocusing to enforce their one-sided franchise agreements. Which is just more of the same! But in contrast to these demands are the Act's protections. While a dealer may not want to file a protest against its manufacturer with the Board, being aware of these protections and citing them to a manufacturer could stop a manufacturer's efforts, with the end result being a more reasonable result in comparison to their demand. ■

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McNees Automotive Dealership Law Group

MOORE:	*GENERAL, BUY/SELL, DEALER LICENSING BOARD, FRANCHISE LITIGATION, DEALER MANUFACTURER ISSUES*
BAGLEY:	*LABOR & EMPLOYMENT*
BAUER:	*PENNDOT, BUREAU OF CONSUMER PROTECTION, STATE POLICE, DEALER LICENSING, DEALER MANUFACTURER ISSUES*
DARKES:	*PENNDOT, BUREAU OF CONSUMER PROTECTION, STATE POLICE, DEALER LICENSING BOARD, FRANCHISE LITIGATION*
DEANGELO:	*FRANCHISE LITIGATION*
DEJOIE:	*BUY/SELL*
FRIEDMAN:	*ENVIRONMENTAL*
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MARSAR:	*BUY/SELL, DEALER MANUFACTURER ISSUES, VOLUNTARY TERMINATIONS*
VAN BASTELAAR:	*BUY/SELL*

In addition to the McNees Automotive Dealer Law Practice Group's knowledge and skill in working with dealer and manufacturer issues for over 25 years, McNees also has long-term experience in assisting with dealer issues regarding dealer business activities, such as buy/sells, taxation and business structure, as well as other dealer issues, including labor and employment, environmental concerns, consumer complaints, government regulatory assistance, dispute litigation, succession planning and estate planning.

Please contact the McNees Automotive Dealer Law Practice Group to learn how we can help in these other facets of a dealer's operation.

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