Alaska Automobile Dealers Association

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February 6, 2017

The Honorable Kevin Meyer
Alaska State Senate
State Capitol Building
Juneau Alaska 99801-1182

Dear Senator Meyer:

I am the President of the Alaska Automobile Dealers Association (the "Association"), an association including seventeen (17) Alaska new automobile dealerships, and additional related companies doing business in Alaska. I am writing in support of Senate Bill 47, which is introduced in the 30th Alaska Legislature. SB 47 (the "Bill") contains long overdue and much-needed revisions to existing Alaska law governing franchise agreements between automobile dealers and automobile manufactures.

In 1978, the United States Supreme Court recognized the need for motor vehicle dealer franchise laws:

> Dealers are, with few exceptions, completely dependent on the manufacturer for their supply of cars. When the dealer has invested to the extent required to secure a franchise, he becomes, in a real sense, the economic captive of his manufacturer. The substantial investment of his own personal funds by the dealer in the business, the inability to convert easily the facilities to other uses, the dependence upon a single manufacturer for supply of automobiles, and the difficulty of obtaining a franchise from another manufacturer all contribute toward making the dealer an easy prey for domination by the factory. On the other hand, from the standpoint of the automobile manufacturer, any single dealer is expendable. The faults of the factory-dealer system are directly attributable to the superior market position of the manufacturer.[1]

[1] *New Motor Vehicle Bd. v. Orrin W. Fox Co.*, 439 U.S. 96 (1978).

The National Automobile Dealers Association also explained the compelling need for state franchise laws in its recent comments to the FTC:

> In addition to benefitting consumers, the franchise laws that the state legislatures have enacted level what is otherwise a very imbalanced economic playing field between auto dealers and manufacturers. Despite a number of assertions at the Workshop to the contrary, the simple fact is that auto manufacturers retain to this day a massive economic power advantage over their franchised dealers, resulting from market structure, manufacturer behavior, and intrusion in the market by the federal antitrust statutes. And manufacturers often use this excess power to overreach and act opportunistically in their relationships with their dealers, to the detriment of dealers and ultimately consumers. The state franchise laws that have been enacted operate to counteract these anomalies and to afford the dealers a reasonable opportunity to negotiate their economic relationships.
>
> The structural economic imbalance between auto manufacturers and dealers is extensive. One key manifestation of the uneven relationship between manufacturers and dealers can be seen in the various franchise contracts. These agreements are not negotiated; they are contracts of adhesion that are presented to the dealer on a "take it or leave it" basis. And any movement to change those terms emanates from the manufacturer in the form of either unilateral amendments to existing agreements or replacement agreements, both of which almost always contain terms that are more onerous from the dealer perspective then what existed before. Frequently supplementing these agreements are controversial programs designed to control dealer behavior, often developed with little or no meaningful dealer input.[2]
>
> There is also a significant existing asymmetry of information between dealers and manufacturers. This exists not only during the exploratory and purchase phase but also during the operational life of the dealership. The manufacturer knows the full details of a dealer's operations, including its customer information, its finances, the disposition of its assets, and its succession plans. Conversely, a dealer has no such insight into its manufacturer beyond public documents and SEC filings. Meanwhile, the manufacturer heavily vets any dealer principal and has minimum requirements for assets and investment and continuing access to the dealer's books and records.

[2] Footnote omitted.

Alaska adopted its motor vehicle dealer franchise law in 2002. This law, while helpful, is seriously deficient when compared with the automobile dealer franchise laws adopted by the other 49 States. In fact, since the Alaska law was adopted, hundreds of state motor vehicle dealer franchise laws and refinements have been passed throughout the country. Many of these laws were enacted to address changes in the business climate and because manufacturers have continued to exercise their inherent ability to dominate their smaller and weaker dealers.

Now, the Alaska Automobile Dealers Association is proposing much-needed updates to Alaska's franchise law. Some of these modifications are intended to clarify provisions that are already in state law. Others address concerns which are addressed by the franchise laws of other states, but which until now have not been addressed in Alaska. Finally, some of the proposed amendments are tailored to address unique situations found in the State of Alaska.

In preparing the proposed legislation, the Alaska Automobile Dealers Association consulted with the legal staff of the National Automobile Dealers Association, and determined that the State of Washington's franchise law could serve as a good model for Alaska. Consequently, many of the proposed amendments are identical to or closely track Washington franchise law. What is also important to remember is that despite any claims the auto manufacturers may make, Alaska's proposed franchise law amendments do not represent any sort of a radical departure from the franchise laws currently existing in most other states. To assist the Legislature in making this comparison, the Alaska Automobile Dealers Association has prepared a comparison of the proposed amendments to the franchise laws of other states, which is attached to this response.

The Auto Alliance, a trade organization consisting of twelve (12) large automobile manufacturers[3] based in both the United States and abroad (the "Alliance") opposed passage of almost identical legislation introduced in the 29 Legislature (HB 318 and SB

[3] Including, for example, BMW Group, DaimlerChrysler Corp., Ford Motor Co., General Motors Corp., Mazda North American Operations, Mitsubishi Motors North America, Inc., Porsche Cars North America, Inc., Toyota Motor North America, Inc., and Volkswagen of America, Inc.

197). This is not surprising, since by its own admission the Alliance has opposed more than 250 automobile franchise bills over the last decade. To support its opposition, the Alliance prepared "comments" on those bills, which the Association understands has been provided to members of the Legislature.

I am writing on behalf of the Association to respond to the Alliance comments, and to offer you Alaska automobile dealers' perspective on why existing Alaska franchise law is in dire need of updating and revision. For ease of reference, I will set out excerpts from the Alliance's comments on the bills proposed in 2016, followed by the Association's response.

SECTION 1: APPLICABILITY

> Section 1. This section would make this bill retroactive to previously existing contracts, it would make the entire existing franchise code retroactive as well. That is extraordinary. When two parties enter into a contract, they do so based on the law as it is when they sign the contract. (SB 47 Sec 20)

If enacted, the Bill would apply to existing franchise agreements, to franchise agreements that are renewed, and franchise agreements that are entered into after passage of the law. With respect to retroactive application, the Alliance claims this is "extraordinary,"[4] and that passage of the Bill would in effect rewrite existing franchise agreements. This statement is both a gross oversimplification of the issue, and implies the Legislature may never pass a law that impacts existing contracts. This is simply not true. In fact, as explained below, the manufacturers have repeatedly made the same arguments in various forums, and have had these arguments rejected by the courts.

Article 1, Section 15 of the Alaska Constitution provides: "No law impairing the obligation of contracts . . . shall be passed." The Alaska Supreme Court (as well as courts throughout the United States) has adopted a two-prong test to determine whether a

[4] At least fifteen (15) other states have *explicit* retroactivity clauses that apply the franchise law to existing contracts, including Alabama, California, Colorado, Florida, Hawaii, Michigan, Minnesota, North Carolina, North Dakota, Ohio, Oklahoma, South Dakota, Vermont, Washington, and West Virginia. See attached maps, at page 2.

retroactive change in the law is permissible. The court must first determine whether the change in the law "has operated as a substantial impairment of a contractual relationship." If there is a substantial impairment, the court then examines whether the impairment "is reasonable and necessary to serve an important public purpose."[5]

The first prong of the test is the most important: With respect to dealer franchise laws, the court must determine whether the new law substantially impairs an existing contractual relationship between the automobile manufacturers and automobile dealers. In answering this question, courts have routinely held that where, as in Alaska, manufacturers are already regulated under existing franchise law, modifying franchise law to provide additional dealer protections does not constitute substantial impairment. For example, in *Chrysler Corporation v. Kolosso Auto Sales, Inc.*,[6] the court held that amendments to the Wisconsin dealer franchise law could be applied retroactively to existing franchise agreements because when the manufacturer entered into the franchise agreement it should have anticipated that the state's franchise law would be amended from time to time. In other words, where manufacturers are already subject to existing franchise laws, amending those laws does not substantially impair the parties' contractual rights because it was reasonably foreseeable to both parties that existing law may be changed by future amendments.

The Alliance recently challenged a Connecticut amendment to its dealer franchise law, which, like this Bill, revised the method used to determine rates for reimbursing dealers for warranty work. As here, the Alliance claimed that retroactive application of the new law would impair contract rights. Ultimately, the Second Circuit Court of Appeals held that the manufacturers' contract rights were not substantially impaired by the new law because "the relationship between automobile manufacturers and Connecticut dealers has long been the subject of close state regulation, including of warranty reimbursement rates. Although the [amendment changed existing law] it was

[5] *Simpson v. Murkowski*, 129 P.3d 437, 444 (Alaska 2006).

[6] 148 F.3d 892, 894–95 (7th Cir. 1998).

eminently foreseeable that the legislature could seek to close a loophole in its regulatory scheme."[7] The court went on to hold that a foreseeable change in the regulatory scheme does not impair existing contract rights.

To illustrate this rule and how it may be applied, it is helpful to compare existing Alaska law with one of the proposed amendments. Under A.S. § 45.25.140, when a manufacturer terminates a dealer's franchise, the manufacturer is required to purchase certain unsold motor vehicles, parts, signs, equipment, tools, etc. Section 7 of the Bill would amend the law to, among other things, require that manufacturers also pay for loaner vehicles, computers, printers, and software. Since automobile manufacturers already have repurchase obligations under existing law, applying Section 7 retroactively to provide additional dealer protections does not constitute an impairment of contracts.

SECTIONS 3–4: TERMINATIONS

These sections interact with each other and are most easily addressed together. They seek to make it harder for a manufacturer to terminate a poorly performing dealer.

The proposed amendment does not constitute a radical departure from existing law. Under A.S. § 45.25.110, a manufacturer may terminate a franchise with a motor vehicle dealer upon a showing of "good cause." However, as it is currently written, the statute does not contain any standards for determining what constitutes "good cause." The existing statute also does not contain any express requirement that manufacturers act in "good faith" when terminating a franchise. The proposed Section 2 requires that terminations be in good faith, and Section 4 contains a detailed description of what constitutes "good cause" for terminating a franchise.

[7] *Alliance of Auto. Mfrs., Inc. v. Currey*, cv. no. 13-4890 (2d Cir. April 7, 2015) (citations omitted). The Supreme Court has denied review of the case. 136 S. Ct. 1374 (2016). The First Circuit similarly held that a recoupment bar was a necessary means to effectuate the state's warranty reimbursement scheme, was a reasonably foreseeable addition to the statute, and was permissible under the Contracts Clause. *Alliance of Auto. Mfrs. v. Gwadosky*, 430 F.3d 30, 42 (1st Cir. 2005).

The proposed amendment adds clarity to existing law, and allows both automobile dealers and manufacturers to understand the standards that will be applied in determining whether good cause exists to terminate a franchise. Alaska automobile dealers, like dealers throughout the nation, make substantial investments in building their dealerships. "Dealerships require sizeable investments; millions of dollars are needed to fund working capital, inventory financing, and investment in facilities and other property. In addition, most capital lenders, especially when dealing with smaller dealerships, require some form of personal guarantees for their investments."[8] It is only fair that dealers be able to know in advance on what grounds their franchise agreement may be terminated given the sizeable investment that must be made to secure a franchise agreement. A dealer should not be required to guess or speculate as to what constitutes "good cause." Instead, it should be able to look to the law, as Sections 2 and 4 propose, and clearly identify its obligations and rights.

Sections 2 and 4 are nearly identical to Washington law, which also clearly defines "good cause" so that there is little room for ambiguity. Washington is not alone in that regard, as several other states have adopted similar statutes that define what constitutes "good cause" for a termination.[9]

One of the most surprising aspects of Section 4 is that it requires the manufacturer to notify the dealer within 180 days of when the manufacturer first becomes aware of the dealer's failure to comply with a provision of the contract. It would appear to not be in either the dealer or the manufacturer's interest to need to force the issue of a termination.

Under existing law, a manufacturer is required to provide notice of termination at least 90 days before the effective date of a termination, except for a termination as a result of the dealer's insolvency, fraud, etc. The proposed 180-day notice provision protects both the manufacturer and the dealer. It allows the manufacturer 180 days to

[8] Nat'l Auto Dealers Ass'n, Letter to the Fed. Trade Comm'n, at 12 (March 4, 2016), *available at* http://www.tada.org/web/Images/NADA2016ResponseToFTCWithAttachmentA.pdf.

[9] For example, HAW. REV. STAT. § 437-58, MICH. COMP. LAWS § 445.1567 and .1568, and OR. REV. STAT. § 650.140 all define "good cause."

investigate a dealer's alleged noncompliance before it is required to give notice of termination. It also allows a dealer additional time to correct any perceived deficiencies before the manufacturer issues a notice of termination. This right to cure provision only applies if the ground for termination is noncompliance with a material term of the franchise agreement.

In addition to requiring 180-day notice, the proposed amendment requires manufacturers to provide the notice within 180 days of first discovering the alleged noncompliance. This operates to create a limitation on the notice period, so that manufacturer's cannot seek to arbitrarily terminate contracts based on stale or irrelevant complaints. It is, in essence, akin to a statute of limitations. If adopted, Alaska would join numerous other states that have very similar 180-day notice provisions.[10]

Section 4 also allows a dealer to challenge a performance termination by relying on market analysis based upon not only that dealer's vehicle allocation, but also the allocation of that dealer's competitors. That data is confidential yet the bill would force the manufacturer to disclose it.

Section 4 provides that if a manufacturer seeks to terminate a franchise because the dealer has not met sales performance standards, the dealer is permitted to present evidence that the manufacturer has not supplied the dealer with an adequate supply of vehicles to meet sales performance goals. Obtaining adequate inventory is a particular problem for Alaska dealers, since manufacturers tend to supply their best selling vehicles to larger, out of state dealers, or to dealers located closer to the distribution point. For example, after Chevrolet introduced the Spark, the vehicle was provided to outside

[10] DEL. CODE ANN. § 4906 (substantially the same); Fla. Stat. § 320.641 (180-day period to correct when noncompliance with contract alleged before notice of termination provided); GA. CODE ANN. § 10-1-651 (substantially the same); HAW. REV. STAT. § 437-58 (substantially the same); IDAHO CODE § 49-1614 (substantially the same); KY. REV. STAT. ANN. § 190.045 (requiring notice of termination within 180 days of first discovery of noncompliance); ME. STAT. titl. 10, § 1174 (requiring notice of termination within 180 days of discovery); MINN. STAT. § 80E.06 (requiring that the dealer "has been notified in writing of the failure within 180 days after the manufacturer first acquired knowledge of the failure"); VT. STAT. ANN. TIL 9, § 4089 (requiring notice be given within 180 days of actual or constructive knowledge of noncompliance).

dealers a full year before the first Spark was delivered to an Alaska dealer. By the time the Spark was delivered, it was "old news." If manufacturers do not supply Alaska dealers with an adequate supply of desirable vehicles on a timely basis, manufacturers should not be able to terminate Alaska franchises by pointing to lower sales by Alaska dealers than outside dealers.[11]

Furthermore, dealer allocation information is already provided to dealers, and is not treated as confidential.[12] The proposed amendment would not create any new allocation disclosure requirements.

SECTIONS 6–9: TERMINATION ASSISTANCE

These Sections spell out a manufacturers obligations to pay a dealer various forms of severance fees upon termination. Many of these obligations are simply forms of "risk shifting." When a franchisee in any industry goes into business, he or she is accepting a certain amount of risk that the business will either succeed or fail.

Alaska law currently provides that upon termination of an automobile dealer franchise, the manufacturer must purchase unsold motor vehicles, parts, signs, equipment, etc. In fact, so called "termination assistance" is required in virtually every state,[13] primarily because manufacturers *require* that dealers purchase certain amounts of inventory, equipment, signs, special tools, and other items. When a manufacturer chooses to terminate a franchise, it is only fair and appropriate that the manufacturer repurchase those items it required the dealer to purchase as a condition to holding the franchise.

The proposed amendments merely expand on the manufacturer's already existing repurchase requirements. For example, the proposed amendment would require that

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[11] In *Beck Chevrolet Co. v. General Motors, LLC*, No.48 (N.Y. May 3, 2016), New York's highest court recognized that "performance benchmarks that reflect a market different from the dealer's sales area cannot be reasonable or fair." The court went on to find a manufacturer's performance standards unreasonable and unfair because market challenges like brand popularity and import bias vary from area to area. The court was answering two questions certified by the Second Circuit Court of Appeals.

[12] In fact, some states require disclosure in writing of the basis for allocation, including how vehicles, parts and accessories are allocated, scheduled, and delivered. *See* WIS. STAT. § 218.0123.

[13] For example, *see* MICH. COMP. LAWS § 445.1571; WASH. REV. CODE § 46.96.080.

manufacturers repurchase "loaner" vehicles that manufacturers require that dealers purchase and make available to their customers. The amendments would also require that the manufacturers purchase software, printers, computers, and other items which dealers were required to purchase. The proposed amendment also contains criteria for establishing the purchase price of the items. The proposed amendment does not provide a golden parachute; rather, it provides a reimbursement mechanism if a manufacturer terminates for a reason other than good cause.

The bills also require payment for early lease terminations and payment for remodeling or relocation costs from the previous three years.

Under existing law, manufacturers are required to pay rent for eighteen (18) months following termination of the franchise, so the proposed amendment is not a radical departure from existing law. However, current law does not require manufacturers to reimburse dealers for the cost of relocating their dealership or for the cost of making improvements to the dealership facility, even when the manufacturer mandated the relocation or improvements within the three years preceding the manufacturer's termination of the franchise. Laws requiring termination assistance recognize that once facilities are purchased, built, or remodeled for use as a dealer facility, the market for resale is extremely limited, especially in Alaska. Requiring reasonable termination assistance addresses this injustice.[14]

Even more astounding is that HB 318/SB 197 would require the manufacturer to pay these generous benefits to a dealer even if it was the dealer that decided to terminate the franchise agreement and quit the business. … But there is certainly no reason that a *dealer* who voluntarily quits the business should receive the same severance benefits as a dealer who was terminated by the manufacturer. Dealers should not be rewarded for quitting. (Section 6 in SB 47)

[14] *See* MICH. COMP. LAWS § 445.1572; WASH. REV. CODE § 46.96.090 (allowing three years for remodeling or alterations and the shorter of the unexpired term of the lease or one year).

Rarely if ever do Alaska automobile dealers "voluntarily" terminate their franchise agreement with manufacturers. More commonly, dealers are forced to terminate the franchise because of problems created by the manufacturer, like failing to provide Alaska dealers with sufficient, desirable inventory needed by dealers to operate profitably. This operates as a *de facto* termination by the manufacturer. It is also important to note the proposed amendment specifically provides that dealers who are terminated for good cause (as set forth in proposed Section 4) or who voluntarily sell their dealership are not entitled to termination assistance. Moreover, under Section 11 of the Bill, all dealers are required to mitigate any damages they incur as a result of the termination.

SECTION 10: SALE OR TRANSFER OF THE DEALERSHIP

> . . . . it is very important for manufacturers to be able to exercise a "right of first refusal" when a dealer wants to sell his or her franchise to someone else. That means the manufacturer has the option to match the buyer's price and then assign the dealership to someone that the manufacturer thinks would be a better dealer. That way a manufacturer can avoid an under qualified candidate from taking the franchise.

Current law provides a manufacturer may not unreasonably refuse to approve the transfer of a franchise to a new franchisee. The proposed amendment provides additional clarity by setting out the conditions a dealer must satisfy before it can transfer the dealership to a new franchisee. Most importantly, the amendments make it clear the proposed franchisee *must* be qualified to hold the franchise, including being able to meet the "normal, reasonable and uniformly applied standards, *established by the manufacturer*"[15]

The Alliance complains the amendment would eliminate manufacturer's rights of first refusal. This is incorrect. Manufacturers may still exercise this right, if the prospective buyer is not qualified to operate a dealership. The Bill also provides a mechanism for manufacturers to acquire the information necessary to determine if a buyer is qualified and requires proposed franchisees to provide this information upon

[15] Emphasis added.

request. And while a right of first refusal may seem innocuous on its face, in practice manufacturers use this right to control the sale of dealerships without good cause and to limit Alaskan's ability to acquire dealerships in favor of offering dealerships to outsiders. An Alaska automobile dealer should be able to sell its business to whomever it chooses, provided the buyer is in all ways qualified to own and operate the dealership.

SECTION 12: SUCCESSION

Dealers oftentimes seek to leave their franchise to their heirs as part of a succession plan. Manufacturers typically work with dealers to accommodate these plans. However, both manufacturers and local consumers have an interest in making sure that whoever does take control of a dealership has the experience, qualifications, and moral character to run a dealership.

The proposed amendment specifically provides that a dealer may only transfer a franchise to a designated successor who is in all ways qualified to own and operate an automobile dealership. In fact, the proposed section specifically provides that a proposed transferee must be "qualified and experienced in the business of being a new motor vehicle dealer" and must meet the "normal, reasonable, and uniformly applied standards of a manufacturer . . ."

Section 12 would prohibit a right of first refusal in an instance where a dealer is simply selling the business to a person who is related in the second degree, or is the husband or wife of a relative of the second degree. This is simply too expansive.

If allowed to exercise a right of first refusal, a manufacturer may prevent an Alaska dealer from transferring the franchise to a family member. The Association believes a dealer should be able to "hand down" the business to a member of the dealer's family,[16] so long as the family member is in all ways qualified to own and run the

[16] Other states recognize the right of succession to a family member, including, for example: ARIZ. REV. STAT. ANN. § 28-4461; COLO. REV. STAT. § 12-6-120.7; CONN. GEN. STAT. § 42-133y; DEL. CODE. ANN. tit. 6, § 4906; GA. CODE ANN. § 10-1-663.1 (specifically providing no right of refusal if the succession is to a designated family member); IDAHO CODE § 49-1615; IND. CODE § 9-32-152; VA. CODE ANN. § 46.2-1569.1; VT. STAT. ANN. tit. 9, § 4093; WASH. REV. CODE § 46.96.220.

business. The proposed amendment specifically provides the family member must be qualified and experienced in the business of being a motor vehicle dealer and must comply with the standards established by the manufacturer or must employ an individual who is qualified and experienced in the business of being a new motor vehicle dealer.

SECTION 13: ADDING OR RELOCATING DEALERSHIPS

> Situations may arise when a manufacturer may seek to add new dealerships to meet consumer demand, or the manufacturer may seek to relocate an existing dealership. . . . Section 13 of HB 318/SB 197 would add extremely high hurdles for a manufacturer that seeks to add or relocate a dealership. The result will be less competition and underserved consumers. (Section 13 in SB 47)

Currently, before a manufacturer may open a new dealership, or relocate an existing dealership in a dealer's relevant market area, the manufacturer must establish "good cause" for doing so. Current law imposes this requirement to prevent manufacturers from "flooding" the existing dealer's market, threatening the viability of the dealer's business, and jeopardizing the dealer's substantial investment.

The proposed amendment expands this protection and provides clarity by including a description of the relevant factors a manufacturer and ultimately a reviewing court should consider when determining whether good cause exists to add a new dealer or relocate an existing dealer. Other states have similar provisions requiring consideration of certain factors in determining good cause for adding a dealer or relocating an existing dealer.[17]

While Alliance claims that establishing multiple dealerships in the same area is good for consumers ("intra-brand competition"), the opposite is true. Manufacturers like to flood the market with new dealerships since manufacturers believe this helps them sell more cars overall. However, too many dealers for a given market area makes it harder for

[17] For example, *see* CONN. GEN. STAT. 42-133dd; GA. CODE ANN. § 10-1-664; HAW. REV. STAT. § 437-55; R.I. GEN. LAWS § 31-5.1-4.2; WASH. REV. CODE § 46.96.160.

all dealers to survive, which drives dealers out of business, leads to less competition, and creates "mega-dealers" who dominate the market.

The proposed amendment does not prevent manufacturers from opening a new dealership in a given market area. Furthermore, the proposed amendment *specifically* requires that the manufacturer and ultimately the reviewing court consider the effect a new or relocated dealership will have on consumers in the market area. Section 13(c) requires that the court consider, among other things, the following:

> (3) the effect on the consuming public in the relevant market area;
>
> (5) the reasonably expected or anticipated motor vehicle market for the relevant market area, including the age of the population, income, education, size class preference, product popularity, retail lease transactions, other demographic factors, and other factors affecting sales to consumers in the relevant market area;
>
> (6) whether establishing an additional new motor vehicle dealer would injure or benefit the public welfare;
>
> (7) whether the new motor vehicle dealer of the same line make in the relevant market area is providing adequate competition and convenient customer care for the new motor vehicles of the same line make in the relevant market area . . .;
>
> (8) whether the establishment of an additional new motor vehicle dealer would increase competition and be in the public interest.

The quoted provisions dramatically refute the manufacturers' claims that the proposed amendment will result in less competition and "underserved consumers."

The Alliance claims it seeks to foster "intra-brand" competition in the interests of consumers. In reality, manufacturers are not so interested in "intra-brand" competition as they are in having as many of their dealers in a market area as possible since manufacturers believe this results in increased overall sales of their vehicles. The amendments proposed by the Association assist dealers from having to try and survive in a "flooded" market, while at the same time the amendments protect consumers from

limited competition. It is for this reason that the Association anticipates that the State of Alaska Consumer Protection Section will have no objection to the proposed amendment.

SECTION 14: COURT ACTIONS

Section 14 also creates "automatic stays" when a protest is filed in a case involving closing, opening or relocating a dealership. Rule 65 of the Alaska Rules of Civil Procedure already covers preliminary injunctions and courts have a wealth of experience in applying it.

Section 14 applies when a manufacturer has given a dealer notice that its franchise agreement is being terminated. This Section provides that if the dealer files an action to protest the termination, the status quo must be maintained until the court has issued a decision on the matter.[18] This type of provision is not unique at all, as there are many provisions in Alaska law which require the maintenance of the status quo until a court or administrative agency has ruled on the matter. The proposed amendment does not favor either the manufacturer or the dealer, nor does it create any competitive advantage, since it simply requires the status quo be maintained until the issue is decided by the court. This results in less expense to both the manufacturer and the dealer and places less burden on the judicial system.

SECTION 15: WARRANTY REIMBURSEMENT

Manufacturers and dealers already have agreements in place that provide compensation for both parts and labor. This bill would allow dealers to ignore those agreements and require the manufacturer to pay the dealer the same retail rates that it charges to the public.

[18] Other states have enacted similar laws, *see*, for example N.J. STAT. ANN. § 56:10-30.

This Section is modeled after Washington law. It is not at all unique, in that many, many states now require that manufacturers reimburse dealerships for warranty work at retail rates.[19]

Also, while it is true that the manufacturers have warranty agreements with their dealers, the Alliance fails to note that these agreements are not arrived at through negotiation with the dealers. Rather they are contracts of adhesion, forced upon the dealers by the manufacturers. As a result, dealers currently have no say in the amount they will be reimbursed for performing warranty work the manufacturers require that dealers provide. The proposed amendments attempt to level the playing field by allowing dealers to charge for parts and service at the same rates charged by dealers to all of their customers. Additionally, manufacturers' refusal to pay standard retail rates ultimately results in Alaskan customers subsidizing the cost of dealer service work. Meanwhile, manufacturers spend that money in other states, where manufacturers *are* required to pay retail rates.

And while it is also true that manufacturers do provide dealers with substantial service work, it is not true, in Alaska at least, that manufacturers supply dealers with the majority of their service work. In Alaska, the ratio is approximately 50% warranty work and 50% non-warranty work. The Alliance also fails to recognize that while 50% of the service work is warranty, those customers who require warranty work often feel inconvenienced and unsatisfied from the outset because they are having to bring their vehicle in because of a manufacturer recall or equipment failure, rather than for routine service work or a failure caused by the customer.

The Alliance also fails to recognize how extremely expensive it is for Alaska dealers to perform warranty work. The manufacturers require that dealers provide extensive training to service personnel, who for the most part must be sent to the Lower

[19] Including, for example: Alabama, Arkansas, California, Florida, Georgia, Hawaii, Idaho, Illinois, Kentucky, Louisiana, Maryland, Michigan, Missouri, Montana, Nebraska, Nevada, New Mexico, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Texas, Utah, Vermont, Virginia, Washington, Wisconsin, and West Virginia.

48 for training, at the expense of dealers. Manufacturers also require that dealers purchase expensive special tools, keep and maintain mountains of paperwork, consult with manufacturers' representatives before performing repairs (without being compensated for this time) and impose additional requirements which make it extremely expensive to provide customers with warranty service. And yet manufacturers typically pay Alaska dealers approximately 70% of their standard retail rates for warranty work. The proposed amendments allow Alaska dealers to be paid fairly for the work they are required to perform—fixing manufacturing defects.

Furthermore, the Alaska parts and service business is highly competitive. In fact, independent, third-party servicers can purchase wholesale parts from warehouse distributors like MOPAR or AC Delco for a price less than charged by the manufacturer. Consequently, dealers do not have unfettered discretion to arbitrarily raise retail rates, as this would only cause service customers to take their business to independent service facilities. There is no risk that dealers will raise their retail rates if the proposed amendment is enacted. This is supported by the fact that at least 31 other states require that manufacturers pay retail rates for warranty work.

The bill seeks to establish a higher cost for the manufacturer in doing business in Alaska. It then goes on to say that despite an Alaska-specific law that raises costs, the manufacturer must distribute that cost across the country rather than having the option to have a surcharge for cars sold into Alaska. State should not pass laws that benefit in-state interests and then pass the costs for them onto other states.

Section 45.25.200(i) simply prevents a manufacturer from trying to recoup from the dealer the cost of paying for warranty repairs at retail rates by "making a separate charge, surcharge or other imposition" against the dealer. Obviously, as a general matter, manufacturers' cost of paying dealers for warranty work is included in the price of their vehicles, so this cost is spread throughout the nation. Subsection (i) would not change this expense allocation.

Another problem can be found in (u), which would allow noncertified technicians to perform a repair, yet the dealer can still bill the manufacturer as if they were certified technicians if they are under the supervision of a certified technician. (SB 47 45.25.220(a))

In many Alaska markets, there is a shortage of certified technicians. This can lead to a delay in performing repairs, which adversely impacts consumers. The revision represents a common sense solution to this problem, since it allows a noncertified technician to perform the repair, provided the noncertified technician is supervised by a certified technician or a service manager. This approach is not a radical departure from the norm, and in fact, some manufacturers already allow noncertified technicians to perform repairs, if necessary and if supervised by a certified technician. This provision benefits consumers rather than dealers, since having to use both a noncertified technician and a certified technician on the same repair is more costly to the dealer, and the dealer does not get reimbursed for this additional expense by the manufacturers. Additionally, allowing this practice often results in higher customer satisfaction since there is no delay in servicing the vehicle. Otherwise, customers must wait until a certified technician is available.

Section 15 incentivizes abuse and sloppiness in other ways. For example, (s) would require manufacturers to pay dealer warranty claims even if the dealer did not follow proper procedures for repairing the vehicle or filling out the claim. (SB XX 45.25.200(h))

Section 15 does not create a license for Alaska dealers to charge for repairs that are improperly performed. Rather, the subsection specifically provides that a motor vehicle dealer is entitled to payment for warranty work only if the dealer can demonstrate that the repair was needed and that the repair was properly performed. Since the repair must be properly performed before the dealer gets paid, it is not at all overreaching to require that the manufacturer pay for the cost of the repair. Additionally, there is no incentive for the dealer to perform anything less than excellent work due to reputation risk and the emphasis manufacturers place on customer service and retention. What the

proposed amendment *does* do is prevent manufacturers from raising "technicalities" (such as where a technician inadvertently forgets to initial a repair order) as an excuse for not paying a dealer for a properly performed warranty repair.

> Finally, Section 15 addresses how consumers that are more than 100 miles from the closest dealership can receive warranty work on their vehicle. (v) would allow a dealer to arrange for an independent technician to perform the warranty work, and then the manufacturer must pay the dealer. Section 16 of this bill would actually prohibit the manufacturer from doing this function, which would give the dealer total discretion in choosing the third party repairer. (SB 45 45.25.220(b))

This provision is intended to address a problem which is somewhat unique to Alaska. There are many, many locations in Alaska, both on and off the road system, where a manufacturer-authorized service facility is not available. So if an Audi breaks down in Tok, the consumer must have the vehicle towed to Anchorage or Fairbanks for warranty service, even if there is a technician in Tok who is qualified to perform the repair. In fact, some manufacturers only provide for one-way towing, which means that the customer is responsible for the cost of getting their vehicle back to their home. Other manufacturers, for example GM, require that if a dealer provides a replacement vehicle during service, the dealer rent a GM vehicle to the customer, or the dealer will not be reimbursed for the cost of providing the rental. Again, in Alaska, this is particularly troublesome in that in some locations there may not be a sufficient quantity of vehicles to meet demand, especially during the tourist season.

The proposed amendment would allow a franchised dealer to make arrangements to have the repairs performed locally, eliminating the need for a long tow, and preventing a long delay in getting the vehicle repaired. Additionally, the proposed amendment saves manufacturers money on towing costs, shipping costs, and rental car reimbursements. If the local technician can properly perform the repairs, there is no reason why the customer

should be inconvenienced, nor is there any reason why the manufacturer should not pay for the cost of performing the warranty repair.[20]

Section 15 also adds a new section to the code, 45.25.200. This section would allow a dealer to consider itself constructively terminated based upon a reduction in the selection of vehicle lines. Whether a manufacturer has discontinued a line make should not be a question of fact for courts to consider. There are clearer ways for states to address compensation in the event of a line make discontinuation. (SB 47, 45.25.230)

In order to open a franchised automobile dealership, dealers are required by manufacturers to build or provide facilities meeting manufacturer standards, purchase special tools, special equipment, and much more. This lifetime worth of investment can vanish in a moment should a manufacturer decide to eliminate a product line (such as GM did with Oldsmobile, Pontiac, and Hummer; Chrysler with Plymouth; Lincoln with Mercury; and Toyota with Scion).[21] Since manufacturers expressly dictate what their dealers must purchase in order to operate a franchised dealership, it is only fair that a manufacturer who chooses to eliminate a product line should be required to provide termination assistance to the effected dealer.

SECTION 16: UNFAIR PRACTICES

(1-3) These subsections seek [to] prohibit a manufacturer from selling to dealers at different prices. The problem is that this prohibits various incentive programs such as those for sales performance or inventory. These three subsections harm good dealers.

Subsections 1 and 2 have to do with the initial sale of the motor vehicle, parts, accessories, equipment or other items. The price charged by the manufacturer must be the

[20] It should be noted that when the dealer chooses the remote repair facility, it is still the dealer who carries the risk on repairs. Thus, the dealer has a vested interested in choosing a competent repair facility.

[21] At least one dealer in Alaska lost all 5 of the discontinued GM lines after investing heavily in the business to support those lines.

same for each franchised dealer. This is fair and is routinely required by most state franchise laws.[22]

Subsection 3 prevents manufacturers from unreasonably excluding Alaska dealers from participating in incentive programs available to other dealers, by imposing economically burdensome participation requirements. As an example, Lincoln requires that Alaska dealers sell a certain number of returned, leased Lincolns in order to participate in a very valuable dealer incentive program. This requirement is imposed even though there are virtually no leased Lincolns in Alaska. So, in order to participate in the incentive program, Alaska dealers have to buy a returned leased Lincoln in the Lower 48, ship it to Alaska, and then sell it. Obviously, it is not always financially feasible to do this, and as a result Alaska dealers are excluded, due solely to geography, from participating in incentive programs which are available to other dealers nationwide.

(4) These subsection seeks to allow dealers to know more about a manufacturer's method for allocating vehicles. The state should be concerned that this language could be used to force disclosure of trade secrets simply because the dealer would like to know more about the manufacturer's allocation strategy.

Subsection 4 prohibits a manufacturer from engaging in an arbitrary allocation process. For example, manufacturers sometimes require that a dealer buy a certain number of one model of vehicle in order to obtain an allocation of more desirable vehicles. This can require, for example, that an Alaska dealer buy a certain number of rear wheel drive convertibles, in order to obtain a reasonable allocation of four-wheel drive SUVs. And, as previously noted, allocation information is already provided to dealers.

(5) This subsection would prohibit manufacturers from limiting document preparation fees in these programs. It would allow dealers to charge higher fees to members of the military, employees, and recent graduates.

[22] For example, *see* attached maps, at page 28.

The Alliance is fully aware that Subsection 5 would not affect military or recent college graduate programs. The subsection is intended to address other types of manufacturer sales programs, such as the "friends and family" program offered by Ford. This program requires that dealers sell particular vehicles at a set price that is established by the manufacturer. However, the price established by the manufacturer does not generally take into consideration the additional cost of doing business in Alaska. Yet Ford will not allow its dealers to charge any additional fee to assist dealers in recouping the additional cost of doing business in Alaska.[23] The proposed amendment addresses this problem.

(6): This subsection requires manufacturers to deliver parts of vehicles to the dealer if other dealers are receiving the same item. This subsection is more inflexible then it should be. It does not account for situations beyond the manufacturer's control.

This subsection simply prevents a manufacturer from refusing to deliver a reasonable quantity of vehicles, parts, and accessories to the dealer unless the dealer meets the manufacturer's unreasonable demand that it purchase advertising displays or remodels or renovates existing facilities.

(7): This subsection would require manufacturers to offer all models to the dealer. This subsection is also too broad. (SB 47 - (9))

This subsection does not apply to limited edition models. It requires that manufacturers offer all of its motor vehicle dealers an equal opportunity to purchase all models generally offered by the manufacturer.

(10): This subsection would prohibit manufacturers from allowing anyone other than a dealer to do warranty repairs. (SB 47 - (12))

[23] Some manufacturers, such as Ford, do allow a minimum documentation fee, but this fee is approximately half of the fees typically charged in Alaska, and does not cover all costs.

This provision does not prohibit manufacturers from establishing a service facility to perform repairs for fleet customers, such as rental car companies. Rather, the provision simply requires the consent of the dealer in the particular relevant market area. This provision is necessary because manufacturers may otherwise establish manufacturer-owned repair facilities, which directly compete with local dealers. This is unfair to the local dealers, since manufacturers require that the local dealers send their service technicians Outside for training at dealer expense, require that the dealers purchase special tools, and impose other financial burdens on the dealer. Manufacturers should not be permitted to insist that dealers incur these substantial costs and then compete with dealers in their market area.

> (14): This subsection seeks to protect dealers from manufacturers requirements to upgrade their facilities unless the same requirement is imposed on all dealers. . . .It should also allow the manufacturer to incentivize dealers to use a manufacturer's preferred vendors. (SB 47 - (15))

Manufacturers should not be allowed to require dealers to perform hundreds of thousands of dollars' worth of renovations and alterations to a dealership unless the requirement is both reasonable and imposed on similarly situated dealers. Nearly every state has some type of restriction on a manufacturer's ability to require renovations or alterations. The proposed amendments do the same. Similarly, a manufacturer should not be allowed to require a dealer to use particular vendors to perform the renovations or alterations. This is particularly true in Alaska where no manufacturers have a factory or corporate locations. Manufacturers have absolutely no familiarity with local vendors, and dealers should be allowed to use local qualified vendors who offer the lowest price. This allows dealers to make renovations or alterations without a substantial, unnecessary financial hardship.

(18): This subsection restricts the manufacturer's ability to seek conditions on site control agreements and required improvements to facilities. This section is needlessly restrictive and takes away a valuable tool that the manufacturers have to ensure that their brands are adequately represented and that customers have pleasant stores to shop in. (SB 47 - (19))

This provision is in harmony with other clauses of the statute that prohibit manufacturers from withholding their consent to sale, transfer, relocation, or renewal without meeting certain statutory requirements. Like many other states, this provision prohibits manufacturers from effectively mandating that a dealer enter into site agreements or that a dealer their remodel its facilities. Instead, site control agreements must be negotiated, and cannot be required as a condition of the manufacturer consenting to the transfer, relocation or renewal of a franchise.

(19): This would prohibit manufacturers from conditioning a dealer's new or renewed franchise agreement on a commitment by that dealer to not protest an additional or relocating dealership. This is another example of this bill seeking to make dealer networks unreasonably rigid. (SB 47 - (20))

Given the unequal bargaining power between local dealers and national/international manufacturers, many manufacturers condition renewal of franchise agreements on the dealer's waiving their right to protest relocation or addition of new dealers and/or remodeling the existing dealership. This places the dealers in the situation of losing their lifetime investment or concede to the manufacturer's demands. The Bill seeks to resolve this inequity and is in accordance with the laws of many other states, as evidenced by the attached maps.[24]

(20): This subsection seeks to limit the manufacturer's ability to change the capital structure of dealerships. Manufacturers must rely on their dealerships being stable and able to borrow effectively. Manufacturers should have input into the capital structure and financing in their dealer network. (SB 45 - (21))

[24] See maps, at page _____.

If the dealer is at all times meeting reasonable capital requirements, there is no reason why manufacturers should be allowed to arbitrarily and without reason, require a dealer to change its capital structure. The proposed amendment still allows a manufacturer to require change when the dealer is not meeting reasonable capital requirements and does not hinder manufacturer's ability to have reasonable input and oversight of the capital structure of dealerships. Many states have substantially similar provisions.

(23) [sic:21]: This subsection very unusual and, if read literally, it would create serious constitutional takings clause issues. . . . It is entirely unreasonable for this bill to say that manufacturers may never raise the price of the products. (SB 47 - (22))

This provision does not prohibit manufacturers from ever raising the price of products. Instead, this Bill, similar to the majority of other states, prohibits a manufacturer from raising a vehicle's price *after* a dealer places an order for the vehicle based on a sale to a retail or fleet customer. Another limitation is that the order must be made *before* the manufacturer provides the dealer with a written price increase notification. This provision, instead of prohibiting price increases across the board, only prohibits a price increase in one very narrow situation—after the dealer has placed the order based on a sale to a customer and before the dealer received notification of the increase.

(23): This subsection seeks to define when manufacturers must indemnify dealers. This is unnecessary because franchise contracts already have well-defined indemnification clauses. SB 47 (24))

This provision does not lead to an unreasonable expansion of indemnification, as the Alliance suggests. Instead, it clearly codifies for all dealers the two situations in which the manufacturer must indemnify a dealer—(1) from a court judgment for damages or a settlement *if the manufacturer approves the settlement* and (2) where applicable law

or the franchise agreement so requires. Many states have codified indemnification provisions and this codification recognizes the unequal bargaining power of the parties. Because franchise agreements are adhesion contracts ("take it or leave it") dealers may be forced to waive indemnification or have no ability to negotiate for indemnification. This Bill seeks to protect dealers from waiving all their indemnification rights.

SECTION 21: SCHEDULE OF COMPENSATION

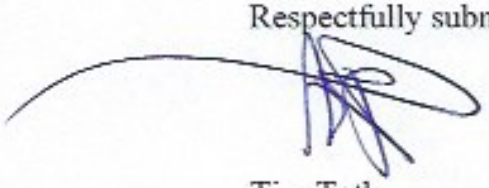
This section sets a price floor in perpetuity for the dealer's compensation. It says that the schedule of compensation may not be less than it was on the day before the effective date of this bill.

This provision seeks to prohibit manufacturers from rushing to reduce existing compensation schedules before the Bill gets enacted.

CONCLUSION

I would appreciate the opportunity to discuss these matters with you, and I look forward to constructive engagement and a helpful dialogue on these issues. Please feel free to contact me at alaskatim@mac.com.

Respectfully submitted,



Tim Toth

President, Alaska Auto Dealers Association