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Spend it like you got it: Dealers suffer under facility design programs

By Jonathan Michaels

A wise man once said, “You can’t spend your way to success.” But don’t tell that to the automotive manufacturers who are dead set on spending big — particularly when it’s not their money being spent.

As manufacturers become increasingly brand-oriented, they are dedicating considerable effort toward designing, and in many cases re-designing, dealership facility programs. The initiatives require franchised dealers to conform to a specific “brand” architecture, and dictate every aspect of facility design, from awnings and fascia to floor tiles and furnishings. And, when the next manufacturer comes out with a shinier plan, the one-upmanship games begin, with manufacturers recasting their design concepts to include brighter floors and bigger windows.

The point of all of this is to create a uniform look among a sprawling dealer base and give their product brand identity. In years past, manufacturers only required dealers to use conforming trademarks and proper signage, but those days are long gone. Automakers now have complete design plans, and regulate which architects and vendors must be used and what type of furniture may be bought. To give but a few examples, General Motors has its “Essential Brand Elements,” Toyota has the “Image USA II,” and Mercedes-Benz just calls its program “Autohaus.”

In their rush to beat out the competition, manufacturers are cajoling, inducing, and strong-arming dealers to tear down their existing facilities and build to the hilt — even if it means tearing down a facility that was just erected under the manufacturer’s outgoing program. The industry has seen more than an occasional case where a dealer has been required to restart construction because the design program changed during the renovation process.

Consider the case of Mercedes-Benz dealer Keenan Motor Group of Doylestown, Pa. who is about to build a new facility under the freshly minted Autohaus program. The project will replace a dealership that was built just six years ago at a cost of \$20 million, but is no longer factory compliant.

As independent businesses, the cost of construction is borne almost entirely by the dealers — and the costs are staggering. Under the Autohaus program, 88 percent of U.S. dealers have renovated their facilities at a cost of \$1.4 billion. Asbury Automotive Group, a publically traded dealership conglomerate with 80 retail stores, plans to spend \$100 million in facility improvements between now and 2013.



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An American flag flies outside a Mercedes-Benz dealership in Bloomfield Hills, Mich.

Associated Press

To be fair, manufacturers do contribute to the cost of construction by providing incentives to dealers who participate in the programs. Mercedes pays its Autohaus dealers \$400 per car sold over a three year period. General Motors makes quarterly payments to its Essential Brand Elements dealers in amounts that are dependent on the size of the project.

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But, the cost of real estate and construction is at risk money fronted by the dealers, who can only hope to recover the investment, assuming the brand remains viable. In just the last 10 years or so, Pontiac, Hummer, Saturn, Oldsmobile, Daewoo, Mercury and Plymouth have been laid to rest, leaving a wake of empty dealership facilities and countless dealers who are still paying the construction debt.

Because of this, many dealers are resistant to facility design programs. And, while manufacturers cannot force an existing dealer to participate in their program, many are using every ounce of political and coercive power to get facility upgrades. One method that has been particularly popular is conditioning manufacturer approval for the sale of a franchise on a new facility being built. Yet, such tactics are of questionable validity, as franchise agreements require manufacturer approval to not be unreasonably withheld.

The issue appears to be coming to an ahead, as automotive juggernaut and Fortune 500 company Sonic Automotive is challenging the practice. Sonic has sued Mercedes in North Carolina,

complaining that the automaker is illegally tying approval of a buy-sell to renovations at four other Mercedes stores owned by Sonic. And, the controversy is not limited to Mercedes. Sonic has also charged Toyota with blocking its attempt to sell four of its Toyota stores by tying approval to upgrades under the Image USA II program.

State legislatures have begun to take notice of the issue, with the National Automobile Dealers Association reporting that legislation is under review in 15 states, and that others have already signed bills. Colorado, for instance, enacted HB 1049, which requires a manufacturer to reimburse a dealer for facility upgrades made within five years, if the dealer is terminated for anything other than fraud. A Florida law requires that manufacturers pay 80 percent of their vehicle incentives to dealers who do not participate in manufacturer programs. And, Virginia passed a bill this year deeming dealers who have made improvements to their stores within the last 10 years to be in compliance with an automaker’s current program.

California has also acted. In 2009, Gov. Arnold Schwarzenegger signed into law SB 424, now codified as California Vehicle Code Section 11713.13, which prevents a manufacturer from requiring a facility upgrade unless it is “reasonable” to do so. Yet, what is reasonable is not defined, leaving much debate about whether manufacturers can require upgrades for California dealers. The California legislation is a good first step toward leveling the playing field, but stops well short of what is necessary to fully address the issue. So long as it is the dealers’ capital at risk, they need to be provided with more protection from having to construct, and re-construct, dealership facilities that meet the pleasure of the manufacturer. Any other result leaves too great a power with the party who has everything to gain and very little to lose.