Washington State
House of Representatives
Office of Program Research

BILL ANALYSIS

Business & Financial Services Committee

HB 2524

Brief Description: Concerning manufacturer and new motor vehicle dealer franchise agreements.

Sponsors: Representatives Kirby, Vick, Ryu, Chandler, Blake, Santos, Stanford, Zeiger, Hurst, Fagan, Takko, Habib, Harris, Sullivan, Kretz, MacEwen, Wylie, Moeller, Morrell, Haigh, Freeman, Springer and Stonier.

Brief Summary of Bill

- Provides additional authority for the Department of Licensing to deny a license for a new motor vehicle manufacturer or new motor vehicle dealer.
- Modifies the provisions under which a new motor vehicle manufacturer may terminate a franchise agreement and the obligations of the manufacturer upon termination.
- Modifies provisions regarding the rates that new motor vehicle manufacturers must pay new motor vehicle dealers for non-warranty customer repairs.
- Adds additional prohibited practices by new motor vehicle manufacturers.
- Add provisions regarding access to new motor vehicle dealer data systems and liability for damages for security breaches.

Hearing Date: 1/29/14

Staff: Linda Merelle (786-7092).

Background:

The Department of Licensing (Department) regulates persons who engage in businesses as new motor vehicle dealers (dealers) and motor vehicle manufacturers (manufacturers). The Director of the Department (Director) has the authority to issue and deny licenses. Manufacturers maintain a franchise relationship with their dealers, and the responsibilities of each party are delineated in state law and the franchise agreement of the parties. State statutes generally dictate

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when a manufacturer may own a franchise or terminate a dealer's franchise, the compensation a manufacturer must pay a dealer for warranty work and customer-paid service repair, and the statutes spell out prohibited practices.

Denial of Licenses.

The Director may deny a license for a manufacturer or a dealer when the application is made under deceptive terms that conceal the real person in interest whose license has been denied, suspended, or revoked for cause and where the terms of the application have not been fulfilled or a civil penalty has not been paid.

Termination of Franchise Agreements.

A manufacturer may for good cause terminate, cancel, or decline to renew a franchise agreement with a dealer when the new motor vehicle dealer fails to comply with a provision of the agreement that is both reasonable and materially significant to the franchise relationship. The manufacturer must have notified the dealer within 180 days after the manufacturer learned of the failure and the dealer must have failed to make a correction after a request to do so.

Good cause to terminate an agreement may also exist if the failure of the dealer relates to the dealer's performance in sales, service, or level of customer satisfaction. Good cause is the failure of the dealer to meet reasonable performance standards determined by the manufacturer based upon uniformly applied criteria, where: (1) the manufacturer provided the dealer written notice of the failure based upon performance; (2) the manufacturer provided the dealer with specific, reasonable goals or performance standards to be met within a suggested timetable, which is not less than 180 days; and (3) the dealer did not substantially comply with the manufacturer's performance standards during the suggested time period, and the failure was not due to factors that were beyond the dealer's control.

Upon termination, cancellation, or nonrenewal of a franchise, the manufacturer must pay the dealer for unsold new motor vehicles and associated costs for distribution, delivery, and taxes. The manufacturer must pay for unused, undamaged, and unsold supplies, parts and accessories and inventory, signs bearing the trade name of the manufacturer, equipment, and other related costs.

The manufacturer must pay required sums to the dealer within 90 days after the termination, cancellation or nonrenewal of the franchise if the dealer has clear title to the property or can provide clear title upon payment by the manufacturer and is in a position to convey that title to the manufacturer.

Except in certain cases, in the event of termination, cancellation, or nonrenewal, the manufacturer must also pay the dealer for costs for any relocation, substantial alteration, or remodeling of a dealer's facilities completed within three years of the termination if they were required by the manufacturer for the continuance or renewal of the franchise agreement.

Rates for Warranty and Non-Warranty Work.

Warranty Work.

Each manufacturer must provide each of its dealers with a schedule of compensation to be paid to the dealer for warranty work or service, including parts, labor, and diagnostic work, required by the manufacturer. The manufacturer has the right to audit claims for warranty work and to charge the dealer for any unsubstantiated, incorrect, or false claims for a period of one year following the payment.

Non-warranty Work.

The rates charged by a dealer for non-warranty service or work for parts is the price paid by the dealer for those parts, including shipping and other charges, increased by the dealer's average percentage markup. The dealer must establish its average percentage markup by submitting either (1) the number of repair orders over 90 days or (2) 100 sequential customer-paid service repair orders, whichever is smaller. The change in the dealer's established average percentage markup takes effect thirty days following the submission.

A manufacturer may not require information that the dealer believes is unduly burdensome or time consuming to provide, including part-by-part or transaction-by-transaction calculations.

A manufacturer must compensate a dealer for labor and diagnostic work at the rates charged by the dealer to its retail customers. If a manufacturer can demonstrate that the rates unreasonably exceed those of all other franchised motor vehicle dealers in the same market area, the manufacturer is not required to honor the proposed rate increase, and the dealer is entitled to resubmit a new proposed rate.

Unfair Practices.

Notwithstanding the terms of the franchise agreement, manufacturers, distributors, and other factory representatives are prohibited from certain unfair practices. Some of those prohibited practices include:

- discriminating between dealers by selling or offering to sell parts, accessories, or like vehicles to one dealer at a lower price than the prices offered to another dealer;
- giving preferential treatment to one dealer over another by refusing or failing to deliver inventory in reasonable quantities and within a reasonable time;
- competing with a dealer by owning, operating, or controlling a service facility in the state for repair or maintenance of vehicles under the manufacturer's new car warranty and extended warranty;
- using confidential or proprietary information obtained from a dealer to unfairly compete with the dealer;
- terminating, cancelling, or failing to renew a franchise with a new motor vehicle dealer based upon any of the following, which do not constitute good cause: (i) the fact that the dealer owns, has an investment in, participates in the management of, or holds a franchise agreement for the sale or service of another make or line of new motor vehicles; (ii) the fact that the dealer has established another make or line of new motor vehicles or service in the same dealership facilities as those of the manufacturer or distributor; (iii) that the new motor vehicle dealer has relocated or intends to relocate the manufacturer's make or line of new motor vehicles or service to an existing dealership facility that is within the relevant market area; in any nonemergency circumstances, the dealer must give the

manufacturer or distributor at least 60 days' notice of his or her intent to relocate; or (iv) the failure of a franchisee to change the location of the dealership or to make substantial alterations to use the number of franchises on the dealership premises or facilities; and

- requiring a dealer to make a material alteration, expansion, or addition to the dealership facility, unless it is uniformly required of other similarly situated dealers of the same make or line, and the request is reasonable.

Summary of Bill:

Denial of Licenses.

In addition to the existing statutory authority to deny a license, the Director may deny a license if the issuance of the license would cause a manufacturer, distributor, or other factory representative to be in violation of the statutory provisions governing franchise agreements between manufacturers and dealers.

Termination of Franchise Agreements.

Sufficient Inventory.

If a manufacturer terminates a dealer's agreement based upon the dealer's performance, the manufacturer must establish an additional criterion. The manufacturer must also have provided the dealer with sufficient inventory for the dealer's assigned market area during the time period in which the performance standards were measured. Sufficient inventory is not supplied unless the manufacturer allocated the inventory in the appropriate product mix in the dealer's primary allocation prior to the performance period established by the manufacturer and none of the primary allocations was more than 120 percent of any other primary allocation during the performance period.

Relocation, Alteration, or Remodeling.

The manufacturer must pay the dealer for costs for any relocation, substantial alteration, or remodeling of a dealer's facilities required by the manufacturer for granting a franchise, in addition to any requirements for the continuance or renewal of a franchise agreement. The relocation, alteration, or remodeling must have taken place within three years of the termination, cancellation, or nonrenewal.

Rates for Warranty and Non-Warranty Work.

Warranty work

Upon audit of a dealer's claims for warranty work, the manufacturer may charge the dealer for any unsubstantiated, incorrect, or false claims for a period of six months following the payment, rather than a period of one year.

Non-warranty work.

A change in the dealer's established average percentage markup may only be initiated by the dealer. In calculating the retail rate customarily charged by the dealer for parts and labor, the following work must not be included in the calculation:

- repairs for manufacturer or distributor special events, specials, or promotional discounts for retail customer repairs;
- parts sold at wholesale or at reduced or specially negotiated rates for insurance repairs;
- engine assemblies and transmission assemblies;
- routine maintenance not covered under warranty;
- nuts, bolts, fasteners, and similar items that do not have an individual part number;
- tires, batteries, and light bulbs; and
- vehicle reconditioning.

A dealer must be compensated for labor and diagnostic work at the rates charged to customers and for any documentation work required by the manufacturer to authorize or verify the work, including photographs, paperwork, and electronic data entry.

Unfair Practices.

Relocation: If a dealer relocates its facility, as permitted under statute, the relocation must be in a relevant market area and the manufacturer has an administrative right to protest the location.

The following additional practices are added to the list of prohibited practices:

Location: The manufacturer must not require, coerce, or attempt to coerce a dealer to change the location of the dealership or construct, replace, renovate or make substantial changes, alterations, or remodeling to a dealer's sales or service facilities before the 15th anniversary of the date of issuance of the Certificate of Occupancy or the manufacturer's approval.

Improvements: The manufacturer is prohibited from failing to provide to the dealer the right to purchase signs, building materials, or other franchisor image elements of like kind and quality from an alternative vendor selected by the dealer if the goods manufacturer has designated or selected a vendor to supply goods or services. If the vendor selected by the manufacturer or distributor is the only available vendor, the dealer must be given the opportunity to purchase the signs or other elements at a price substantially similar to the capitalized lease costs of the signs or elements. Nonetheless, a dealer is not allowed to impair or eliminate the intellectual property rights of the manufacturer.

Adverse action: The manufacturer is prohibited from taking any adverse action against a dealer, including charge backs or reducing vehicle allocations, for sales and service performance within a designated area of primary responsibility.

Equipment: The manufacturer is prohibited from requiring or coercing a dealer to order or accept delivery of any service or repair appliances, equipment, parts, or other commodities not required by law and not requested by the dealer.

Access to Dealer's Customer Data.

New terms are defined in the statutory provisions governing franchise agreements between manufacturers and dealers:

A "dealer management computer system" is "a computer hardware and software system that is owned or leased by a new motor vehicle dealer, including the dealer's use of internet applications, software, or hardware, whether located at an existing dealership facility or provided at a remote location, that provides access to customer records and transactions by a motor vehicle dealer located in this state, and that allows the new motor vehicle dealer timely information in order to sell vehicles, parts, or services through the existing dealership."

A "dealer management computer system vendor" is "a seller or reseller of dealer management computer systems, to the extent that the seller or reseller is engaged in such activities."

A "security breach" is "an incident of unauthorized access to and acquisition of records or data containing new motor vehicle dealer or dealer customer information where unauthorized use of the dealer or dealer's customer information has occurred or is reasonably likely to occur or that creates a material risk of harm to the dealer or dealer's customer. Any incident of unauthorized access to and acquisition of records or data containing dealer or dealer customer information, or any incident of disclosure of dealer customer information to one or more third parties that has not been specifically authorized by the dealer or dealer's customer."

Voidable agreement: A dealer may not be required to provide consumer or customer data or information to a second dealer through direct access to the first dealer's management computer system. The dealer may provide consumer or customer data or information to a second dealer upon receipt of a specified request. The dealer providing the information may be charged a reasonable initial set-up fee and reasonable processing fee based on the costs incurred by the requesting party. Any agreement with a manufacturer that requires the dealer to consent to direct access to the dealer's management computer system is voidable by the dealer.

Indemnification: The manufacturer or dealer management's computer system vendor that has electronic access to consumer or customer data or other information in a dealer's computer system, or an entity to whom the dealer has provided consumer or customer data, shall fully indemnify and hold harmless the dealer from all damages and attorneys' fees related to the disclosure of security breaches.

Appropriation: None.

Fiscal Note: Requested on January 28, 2014.

Effective Date: The bill takes effect 90 days after adjournment of the session in which the bill is passed.