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## Issues Unique to Transfer of Multi-Point Franchises

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Single point asset sales and purchases are becoming less and less common. Most deals these days involve multiple points as a result of years of mergers and acquisitions that have swallowed up single points, as well as the new reality that a single point is just not as economically feasible as having multiple franchises at one location when space permits. Several issues that are unique to multi-point franchise sales are not often discussed, but can significantly impact a deal. Just a few of these issues include: whether to use one or more purchase agreements, if one agreement is used; whether to itemize the goodwill for each franchise; what issues arise for sellers when a manufacturer exercises its right of first refusal but declines to purchase assets related to other franchises that are part of the deal; and how to prevent it from happening in the first place.

### Right of First Refusal

One of the more pressing issues for most buyers is whether the manufacturer will exercise their right of first refusal. Buyers don't want to end up going through all the work of negotiating a buy/sell and conducting due diligence (not to mention

lining up financing and people for the store), just to find out that the manufacturer has exercised its right of first refusal. In California, the manufacturer must reimburse the buyer for the legal fees and expenses incurred in connection with the buy/sell if they exercise their right of first refusal, which is not much of a consolation prize. It is much easier for a manufacturer to exercise its right of first refusal if there is a separate purchase agreement for each franchise. In large, multi-franchise transactions, it is typical to use one purchase agreement and to state one amount for goodwill. Some manufacturers are attempting to require dealers to use separate purchase agreements to make it easier for the manufacturer to exercise their right of first refusal.

In California, the law specifically states that if a manufacturer exercises its right of first refusal they must provide the same consideration that was being offered per the terms of the purchase agreement, by the original buyer, i.e. perform all the terms of the contract. Even with separate purchase agreements the manufacturer would be required to purchase all the franchises that were part of the deal if the agreements included 1) an obligation to purchase the other dealership assets and close simultaneously, and 2) a right to walk if that does not happen.

Still, in Virginia, which has a statute similar to California's, the Federal District Court recently ruled that Volvo Truck had the right to purchase just one of the franchises of a multi-franchise truck dealer even though the stock of the entire business, which included multiple franchises, was the subject of a stock purchase agreement. The court did not address how the sale would transpire. Since the stock was being sold, not the assets, a transfer of some of the stock to Volvo would not have transferred just the Volvo franchise. Rather, the Court ruled that the Volvo Truck franchise assets were to be valued to enable Volvo to exercise its right of first refusal and buy the assets of only that franchise. Frankly, I think it was a bad decision and it should be, and is being, appealed.

Other courts have been reluctant to require a valuation in order to enforce a right of first refusal and will just issue an injunction to the sale if no separate price is stated for the assets associated with their franchise in a purchase agreement including other franchises. Eventually, due to differences in the way the different courts interpret these provisions, this issue may make its way up to the Supreme Court. However, that may not be for quite a while.

### **Purchase Agreement Provisions**

What can dealers do now to address rights of first refusal so they don't end up holding up a deal? Manufacturers may be less likely to exercise their right of first refusal if a value is not separately stated in the purchase agreement for their franchise. Why? Because exercising the right can result in litigation that leads them nowhere. Some franchisors are beginning to require that the purchase price for their franchise be specifically stated in purchase agreements even if separate agreements are not required. In response, dealers could, and should, insist that if that provision is going to be included in their Dealer Agreement, another provision

also be added.

At least some of the courts that have heard these cases state that any dealer could insist a provision be included in the franchise agreement providing that if the right of first refusal is exercised by the manufacturer they must also purchase any other assets that are part of the transaction. Although this is already stated in California law, and was also stated in Virginia law, the Virginia court found that the law was not enforceable unless the same language is stated in the franchise agreement. They found that otherwise, the right of first refusal would be meaningless. However, the logic is not sound. The statute already requires the manufacturer to perform all the terms of the contract. The Court failed to reconcile the Virginia law with its opinion. Sounder logic would have been to find that if the manufacturer wanted to preclude the dealer from including any other assets with the sale of its franchise, it could have said so in the franchise agreement, thereby requiring that the dealer clearly waive the contrary law, rather than essentially ruling (without saying it) that inaction caused a waiver. Some franchise agreements do in fact include such language. The Court also failed to recognize the unequal bargaining power between the manufacturer and the dealer.

### **Avoiding Dealer Agreement Modifications**

Resisting the urge to allow the manufacturer to modify the Dealer Agreement to require a separate purchase agreement or purchase price for their franchise can go a long way to assisting with a smooth transition. Manufacturers are less likely to exercise their right of first refusal if doing so is likely to result in a lawsuit. If the Dealer Agreement does not require the dealer to state a separate purchase price for each franchise the dealer has no obligation to do so if the manufacturer asks for it. In California, the manufacturer cannot turn down the buyer on that basis and must approve the dealer within 60 days of receiving all documents or the dealer is deemed approved. I have not yet seen a manufacturer refuse to purchase the assets of all the franchises included in a purchase agreement when the dealership is located in California, but I have heard it has happened. I also have not seen more than one manufacturer exercise a right of first refusal on any one deal, but with manufacturers more frequently exercising their rights of first refusal, the chances of it happening have increased.

Arguments have been made that a manufacturer has no right of first refusal with respect to any franchise other than the one it issued. Certainly this is the argument that could be made by a manufacturer if two manufacturers exercised their right of first refusal on the same deal. If the right of first refusal specifically states that the manufacturer has the right of first refusal with respect to all franchises being sold as a package provided it is the first to exercise the right of first refusal, but no rights if another manufacturer exercises the right first, this would address all the potential problems and enable the seller and buyer to get the benefit of their bargain (provided the seller's other dealer agreements also include the same language). But this provision would have to be negotiated with all manufacturers so that it is included in all Dealer Agreements of a potential

seller, otherwise it could leave the seller in breach of another right of first refusal. At a minimum, dealers should insist that the Dealer Sales and Service Agreement require the manufacturer to comply with California law in exercising any right of first refusal.

Make sure you read your new Dealer Sales and Service Agreement before you just sign it. If you don't want to read it, have your attorney read it and tell them what to look for. Under California law, your Dealer Agreement cannot be terminated for refusing to sign a new one. Demanding terms that are reasonable is the only way for a dealer to be protected from changing statutes and case law. As it stands, although California statutes should protect a dealer from having to sell to a manufacturer who refuses to deliver the full consideration for the sale upon exercise of a right of first refusal (and in my experience, they always have), manufacturers are getting more aggressive and this is an issue that is heating up. Protect yourself while you still can or you may find yourself in the midst of a nasty lawsuit when you try to sell your dealerships.

### **DEALER ALERT**

If you want to make sure California does not go the way of Virginia, contact [Brian Maas](#) at California New Car Dealers Association (CNCDA) and suggest that they propose some legislation that prohibits a waiver of the California law requiring the manufacturer to deliver all the consideration promised by a buyer if they exercise their right of first refusal. I have already made this suggestion to Brian and gave him the contact information for the person in Virginia who is leading the charge for new legislation there, but the more people he hears from, the more likely CNCDA is to introduce new legislation.

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