THE HIDDEN RISKS OF UNWRITTEN DEALER AGREEMENTS

AUTHORS: James R. Waite, Esq and Alexandra Ong, Esq

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Dealership agreements are notorious for their daunting legalese and lack of uniformity. As if that weren't enough, courts in many states and, indeed, throughout the world (including those in the EU, England, China, Australia, South Korea and, to a lesser extent, Japan) have acknowledged the existence of oral or implied dealer agreements. Nevertheless, industry participants often start with the assumption that, to be legally enforceable, a dealer agreement must be in writing. That's a reasonable thing to think in most industries. The traditional emphasis on written contracts in commercial transactions, coupled with long-standing legal principles like the Uniform Commercial Code's Statute of Frauds, require most contracts for the sale of goods valued at $500 or more, or which cannot be fully performed within one year, to be memorialized in writing. But in the equipment industry, this assumption can be dangerously incorrect.

Why? Because state dealer laws often override more general contract principles to create legally binding agreements where such agreements otherwise wouldn't exist. These laws typically take the form of equipment dealer statutes (or in a few cases, franchise statutes) that prescribe a wide range of rights, remedies, obligations and responsibilities of dealers and suppliers and apply them to vastly different types of equipment, including farming, industrial, construction, mining, lawn and garden, maritime, horticultural, forestry and others. Confoundingly, the vast majority of such laws also expressly accommodate the existence of "oral" dealer agreements. As discussed below, this can yield unanticipated consequences (some positive, some profoundly negative) for both suppliers and dealers. For example, Alabama's Equipment Dealer Statute1 defines a "Dealer Agreement" to mean "[a]n agreement or contract, expressed or implied, oral or written, by and between a supplier and a dealer…" It goes on to require the supplier to: (a) notify all existing dealers in any market area where a new dealer is to be appointed, and then (b) prove that doing so "is not unreasonable." Query: How would Alabama's requirement that a supplier notify incumbents prior to appointing a new dealer apply in a case where the agreement with the new dealer was "implied" after the fact? And what of the requirement that the supplier prove it was not unreasonable (particularly where the supplier didn't even realize an agreement had been formed)?

A Long Story:

Is it a dealer agreement? Owing to an array of diverse statutes, fact patterns, judicial interpretations and arbitration awards, even industry veterans can find themselves wondering if they might have accidentally entered into an enforceable dealer agreement, and if they have, what its terms consist of. Depending on the jurisdiction(s) involved, the answer(s), even for the same dealer (consider a relationship involving a supplier and a multi-state dealer), can range from "no contractual relationship of any kind exists" to "yes, a dealership has been created, it applies to the entire range of equipment made available by the supplier, and, incidentally, it effectively grants the dealer exclusivity within the dealer's market area."

A patchwork of state laws: As noted above, further complicating matters is the fact that most states' equipment dealer statutes expressly acknowledge the existence of "oral" dealer agreements. Those that do, however, usually fail to specify what terms these oral agreements will be presumed to include beyond (typically) requiring "good" or "just" cause for termination and/or the supplier's repurchase of certain equipment, parts and/or other items from the dealer upon termination. (Note: Not all of them even do that; Georgia's multiline equipment dealer statute, for example, requires good cause for termination, but contains no repurchase requirement.) As a consequence, equipment dealers and suppliers may be surprised to learn that they have created legally binding relationships through their words, conduct and/or correspondence, perhaps without even realizing it. Th is might, for example, be deemed to have occurred as a result of something as seemingly benign as emailing information requests and responses, though we see it far more oft en result from repeated requests for products; engaging in multiple purchase and sale transactions; off ering reimbursements, rebates or discounts; providing training or advertising materials; and/or taking other actions that suggest the existence of a more directed and intentional dealersupplier relationship.

If a dealer agreement exists, what does it address? Obviously, in the absence of a written contract, it can be nearly impossible to prove what the parties intended to agree upon, or what either side might be legally obligated or entitled to do. And by the time a court is asked to make that determination, the parties' memories and interpretations are likely to be very diff erent. Dealers may assert rights to statutory protections, such as mandatory order fulfillment obligations; advertising assistance; equipment and parts provisioning; diagnostic equipment, tooling and software (including updates and bug fixes) rights; warranty reimbursements; buyback obligations; and most commonly of all, strict termination and notice requirements. Suppliers, on the other hand, can usually be expected to argue, at least initially, that no legal relationship of any kind, including any dealership, was ever intended or formed. Or, as the supplier's arguments typically go, if a relationship was formed, it was extremely limited (for example, a "one-off " dealer agreement limited to the specific item(s) provided pursuant to a given order or a "partsand-service-only" relationship in which the dealer has the right to purchase only parts, supplies and consumables in connection with the provision of warranty service and repairs). Adding to the uncertainty is the fact that arbitration awards are typically confidential and, as a result, provide little or no precedential guidance.

Also importantly, states have largely eliminated the appeals process with respect to arbitration awards. The arbitration process appears to have become more time-consuming and expensive, and arbitration awards less predictable, making arbitration less appealing than it once was for domestic issues. (Note: Arbitration continues to be an attractive option with respect to international relationships because many countries continue to honor contractual arbitration provisions, which allow for resolutions of disputes in the U.S. if required by the parties' written agreement, rather than forcing U.S.- based participants to take their chances in foreign courts.)

How have dealers and suppliers reacted? In response, industry participants and their lawyers have accumulated an assortment of arguments designed to address the lengthy list of statutes, rulings, facts and circumstances that may apply to these disputes. For example, depending on which side of the argument you find yourself on, you might hear:

- "Oral dealer agreements are inherently vague and must therefore be severely limited (or vastly expanded) in order to accommodate the legislature's intent in allowing them to exist."
- "A supplier's provision of additional products after termination of a written dealer agreement must be deemed to (or can never) create a new, oral dealer agreement."

- **“A buyer of a dealership should never (or should always) be permitted to enforce an oral dealer agreement entered into by the dealership’s former owner(s).” (Query: What if the former owner(s) didn’t realize they had done so – for example, through emails discovered by the buyer after the sale?)**
- **“As a matter of fundamental fairness, if an oral dealer agreement is deemed to exist, exclusivity must (or should never) be implied in a case where a supplier has never in the past appointed overlapping dealers in the same territory.”**
- **“If exclusivity is to be implied in favor of the dealer, fairness dictates that it must (or should never) also be implied reciprocally in favor of the supplier to prohibit the dealer from selling competing products within the same territory.”**
- **“A supplier can never (or must be permitted to) require a dealer to refrain from selling products that compete with the supplier’s products.”**

What Do the Courts say? As noted above, courts and arbitration panels around the country have come down on all sides of these issues, often in confusingly different ways. For example:

- **MISSOURI (2022): In S&H Farm Supply, Inc. v. Bad Boy, Inc.," the 8th Circuit Court of Appeals found that S&H had a valid oral dealership agreement with Bad Boy, which Bad Boy breached by appointing other dealers within S&H's territory and then terminating S&H for selling competing equipment. A jury awarded S&H over $5.8 million, which amount was affirmed on appeal.**
- **PENNSYLVANIA (2016): In Precision Industrial Equipment v. IPC Eagle, the court found that Pennsylvania's statute of frauds barred the existence of an oral dealer agreement.**
- **NORTH CAROLINA (2004): In Dealers Supply Co., Inc. v. Cheil Industries, Inc. and Samsung Chemical (USA) Inc.,? the court found that an oral dealer agreement did not exist, but it permitted the dealer's unfair and deceptive trade practices act claim to proceed based on Cheil/Samsung's admission that they had done business for three years "on a handshake.”**
- **TEXAS (2019): In Mercedes-Benz USA, LLC v. Carduco, Inc. the Texas Supreme Court reversed a $130.3 million verdict in favor of the dealer, Carduco, finding that its oral contract claims were defeated by an earlier written dealership agreement with Mercedes.**

HOW TO PROTECT YOUR BUSINESS GOING FORWARD

- **Create a list of mission-critical issues prior to commencing discussions. Make certain that, at a minimum, the list includes all essential operational issues, including equipment needs and demands, customer requirements, exclusivity or non-exclusivity (on both sides), locations, facilities, stocking requirements, management, staffing, financial capacity and metrics, competitive environment, repair and maintenance capacity, warranty and reimbursement requirements, delivery timing and acceptance requirements, financing and payment terms, security interests, recordkeeping and retention, and the myriad other factors that**

must be considered in order to successfully navigate an equipment dealer-supplier relationship.

- Do not simply sign your counterparty's "form agreement." First and foremost, there is no such thing as a "form" dealer agreement. Beyond that, nowadays, first drafts are often wildly unfair, overreaching, inaccurate and/or unenforceable. Be prepared to negotiate.
- Carefully review the laws of each jurisdiction in which you plan to do business. These laws can differ dramatically, making it imperative that you understand the likely results of entering into a dealer or franchise agreement in each jurisdiction ahead of time.
- Negotiate and document the issues thoroughly in an enforceable written agreement.
- Never commence pertormance before receiving a fully executed counterpart of that agreement from your prospective counterpart (whether a dealer or a supplier).
- Never rely on oral agreements or "handshake" understandings. Although they may ultimately be found to exist, determining that they do and what their terms consist of can be immensely expensive and time-consuming (and remember, people move on; the person whose hand you shook initially may not be there by the time you need to enforce your handshake agreement).
- Don’t, however, simply give up if you lack a written contract, as most states’ dealer laws now at least allow for the possibility that an implied or oral dealer agreement will be deemed to exist (often strengthened if a proposed dealer agreement was proffered by one side but never signed, as “part performance” can provide substantial legal support for the existence of a valid agreement)

CONCLUSION

As courts and state legislatures increasingly recognize that ongoing conduct and informal arrangements can give rise to enforceable dealer relationships, the risks of relying solely on handshake deals - or assuming that no contract exists - are real and growing. Today's byzantine array of statutes, cases and facts can render it virtually impossible to determine without the assistance of a lawyer and/or a judge whether a legally binding dealer agreement has been formed. What may seem like casual business dealings could, under the right (or wrong) circumstances, trigger statutory protections and binding legal obligations. Given this uncertainty, industry participants should not leave anything to chance. Instead, they should proactively address and, to the extent possible, seize control of all mission-critical issues (and do so in writing) before their ability to do so is placed in the hands of people who may not adequately understand the issues involved in this deceptively complex industry. Feel free to contact us if we can help, at www.jwlinternational.com or 866-582-2586.