DEFENDER
THE NADC NEWSLETTER

The Myths of the Non-Recourse Agreement

Les Stracher

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Without fail, every dealer has been presented with a dealer finance agreement from its friendly local lender that purports to be a non-recourse agreement or, in other words, a lending facility which affords the lender no recourse against the dealer in the event of a consumer default. Through the years, though, full recourse language has slowly crept into these "non-recourse" agreements thereby affording lenders much more leverage vis-à-vis our dealer clients. You may wonder how sophisticated business people fall into the trap of accepting on face value the representations of their lenders that they will forbear from seeking recourse against the dealer. The answer lies somewhere in the irony that our clients, who are masters of fine print, get sold a bill of goods when the lender comes a callin' with an attractive program and promises that they would never damage their valued business relationship with the dealer by seeking recourse.

At some point, you will be presented with such an agreement and you will be pitted against aggressive finance and insurance people armed with tools which purport to analyze lease and finance facilities to maximize dealer gross. Faced with the prospect of unfavorable terms, you may feel like telling your dealer client to "just say no" to the whole prospect of doing business under the agreement as presented. This is a difficult and daunting prospect when your client wants to do a deal. However, there is a win-win solution to this quandary and part of the trick, as I will outline below, is knowing which fights to pick and to analyze your client's presence and strength in the marketplace to

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Sidebar

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U.S. Dept of Labor Recovers $1 Million in Overtime Pay from One Employer

Stevan Labonte

The United States Department of Labor recently announced that an Alabama-based bank agreed to pay more than one million dollars in back overtime wages. Violations of the Fair Labor Standards Act (FLSA) can open employers (including dealerships) to thousands of dollars in fines and hundreds of thousands of dollars in back wages. Dealer counsel should remind their clients that careful monitoring of wage and hour issues will not only help them avoid fines and violations but will also help to improve employee morale.

The FLSA requires that covered workers be paid at least the applicable minimum wage and one-and-one-half times their regular rate of pay for all hours worked over 40 in a single work week. Hours worked does not include non-work time such as holidays and sick and vacation days.

Not all dealership employees are entitled to overtime benefits, however. The FLSA exempts certain dealership employees from the overtime requirements. Exempt employees include:

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President's Message

Jonathan P. Harvey

If you did not attend the Annual Conference in Chicago, you missed an exceptional two days. Gene Kelley did his usual superb job as Conference Chair and, in addition, gave the benefit of his years of experience as a lawyer. We were fascinated to hear Steven Baker, Director of the Federal Trade Commission's Midwest Regional Office, and equally interested to hear from Terri Harris, Motor Vehicle Technical Advisor to the Internal Revenue Service for the entire country. If you don't know about the Technical Advisory Program, you should. Oren Tasini, Les Stracher and Gordon Devens gave us some interesting perspectives regarding current trends in buy-sell agreements and were happy to answer the many questions asked of them. Eric Chase demonstrated why he is in such demand as a speaker and gave us a good overview of current litigation issues. Len Bellavia provided an interesting discussion of mass litigation, and Joe Roesner, from the Fontana Group, one of our associate members, gave us the viewpoint of an expert witness.

Jeff Ingram, Larry Byrne, Jim Blume and Lew Goldfarb covered arbitration and, in particular, what is good and what is bad about the process. In the afternoon of the first day, John Donovan gave us a good overview of what's happening in the field of Labor Law with dealers, and then Jerry Coker got up and scared everyone in the room. If you want to know why, you'll have to go to the website and read about the Conference. Later on Monday, Steve Maskiewicz and Anne Gambardella talked about the TREAD Act and various issues involving vehicle standards and conditions. That stuff is important to know.

On Tuesday, after Terri Harris' talk, Rob Cohen, Paul Metrey from the NADA, and Mike Charapp talked about F&I matters, discussions which I always enjoy and rarely understand. After the break, Patty Covington, Jim Chareq and Randy Henrick gave us a good overview, and also a detailed description of information safeguards, privacy, security breaches and all the Acts about which we are supposed to know.

My hat goes off to all of the speakers, and I give them grateful thanks for the time and energy and enthusiasm with which they selflessly spoke to a group of over one hundred sixty attendees. I also want to thank the associate members who took the time to come to the Conference and staff their information tables. I encourage all of you to become familiar with our associate members and to communicate with them and use their services. They know what they are doing.

Incidentally, we were delighted to have a number of lawyers from the NADA, and particularly pleased to welcome Andy Koblenz, an Albany boy, as am I, as the new General Counsel of NADA.

On the business side, the number of authorized Directors has been increased from fourteen to twenty-five, and we are asking for volunteers. If you have interest, send me an e-mail, or send one to Jack Tracey, along with your CV.

On a final note, as of the first day of the Conference, we reached a membership of four hundred and one. This Association has clearly surpassed all our hopes and is now a requirement for any lawyer representing dealers. We have come of age in less than two years. Congratulations to all of you.

Jonathan P. Harvey of Harvey and Mumford LLP is President of the NADC and can be reached by e-mail at: jpharvey@harveyandmumford.com

Special Workshop: California Car Buyer's Bill of Rights

10 am to 3 pm, June 23, 2006

Hilton San Diego Gaslamp Quarter

If you are an attorney representing auto dealers in California, this workshop is for you. Learn how this important bill that takes effect July 1 will affect your dealer clients.

Panelists include Peter Welch, president of CMCDA, Bert Rasmussen, partner with Manning, Leaver, Bruder & Berberich, and Rob Cohen, president of Auto Advisory Services. MCLE will be available.

The workshop will include a discussion regarding the formation of a California state chapter of the NADC.

The registration fee is $295 and includes a night's stay — Thursday or Friday — or $395 for both nights. If you wish to attend the workshop only, registration is $195.

Register now at www.dealercounsel.com/CA.html

There are No Elephants in Mouseholes (and the Privacy Rule Does Not Apply to Lawyers)

Rob Cohen

Rob Cohen

Like many dealer compliance attorneys, I have spent a lot of time studying the Gramm-Leach-Bliley Act and its brood, the FTC's Privacy and Safeguards rules. It's not exactly riveting stuff to read, but hey, we're attorneys, we get paid to read the things that could be approved by the FDA as a cure for insomnia.

Little did I know, however, that while I was busy trying to explain federal privacy rules to my clients, there was a storm brewing over the FTC's ability to enforce their own rules against a particular class of "financial institutions." This storm culminated into a lawsuit (as many metaphorical storms do) but did not involve car dealerships or other more traditional financial institutions. No, this suit was brought against the FTC by the American Bar Association. You see, the class of financial institutions the FTC was trying to impose its regulations upon was, pause for effect, lawyers!

In December of last year, the U.S. Court of Appeals for the District of Columbia Circuit held that the FTC had overstepped its authority when it issued an opinion stating that the Gramm-Leach-Bliley Act applied to attorneys (thereby giving the FTC the ability to regulate the practice of law). I will spare you the mind-numbing details of the Court's decision, but suffice it to say that us attorneys will not have to worry about the FTC knocking on our doors and asking for our customer information security policy.

The FTC had until March of this year to appeal to the U.S. Supreme Court, but choose not to do so—and understandably so. The FTC's tortured path of reasoning was harder to follow than a graffiti-covered subway map in New York city. The Circuit Court noted:

> When we examine a scheme of the length, detail, and intricacy of the one before us, we find it difficult to believe that Congress, by any remaining ambiguity, intended to undertake the regulation of the profession of law–a profession never before regulated by "federal functional regulators" – and never mentioned in the statute. To find this interpretation deference-worthy, we would have to conclude that Congress not only had hidden a rather large elephant in a rather obscure mousehole, but had buried the ambiguity in which the pachyderm lurks beneath an incredibly deep mound of specificity, none of which bears the footprints of the beast or any indication that Congress even suspected its presence.

I think we should all send the Circuit Court judges a little thank you card. If not for this very sensible decision, we could have found ourselves having to issue privacy notices and implement a comprehensive information security policy. That sounds like a lot of non-billable work.

Rob Cohen is President of Auto Advisory Services, Tustin, CA, First Vice President of the NADC and Editor of Defender, The NADC Newsletter

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gain leverage over the lender. In this article, I lay out what I refer to as "Lender Myths of Non-Recourse" as well as some tools to help you debunk them.

A. Lender Myth 1: This is our standardized form and everyone signs it without question"

Should you elect to challenge the status quo with respect to these agreements, the first argument that you will hear is that these agreements are signed all the time and no one ever questions them. I can tell you with no hesitation that, with the exception of the captive lenders, this is rarely true. Perhaps a more accurate statement of fact would be something to the general effect of "we never change these agreements unless someone with bargaining power actually looks at the verbiage of the document and challenges it." The fact is that were you to review the agreements entered into between lenders and mega dealers (or publicly traded dealer groups) that you will find changes are made with some degree of regularity, and more strikingly, that the types of changes made are of a similar nature. Indeed, I have found that with the exertion of some force, lenders are more willing to make changes to their agreements than you may realize; particularly as it relates to the warranty and representation portion of their agreements (which I believe make the dealers insurers of the liabilities being assumed under the contract).

B. Lender Myth 2: "Privacy provisions? Not to worry, we don't disclose customer information"

To a lesser extent as time has progressed, but still to an alarming degree, lenders may not include language protecting their dealer partners from exposure under the Gramm-Leach-Bliley ("GLB") Act (15 USC § 6801, et seq.) and its offspring, the FTC Safeguards Rule (16 CFR part 314). Again, with the exception of the captives, who will tend to send you addenda to address these issues, most lenders will not incorporate language protecting the dealer and/or assisting the dealer in meeting its statutory requirements under GLB. Of course, as in any contract negotiation, you can either seek to modify the document from the other side or simply provide the lender with a blanket addendum to deal with the issue. Depending on the willingness of the lender to provide you with a version of their agreement in a format which will permit you to provide editorial or "blackline" comments, you may want to throw the ball in their court by simply providing them with what I refer to as a "privacy addendum," stating, in pertinent part, as follows:

> *Indemnification*: Notwithstanding anything contained in the Dealer Agreement to the contrary, Dealer shall have no obligation whatsoever to indemnify, hold harmless and/or defend the Lending Institution from any actions, suits, losses, damages, claims and/or costs, of any kind whatsoever, unless same arising solely from the conduct of the Dealer. Lending Institution shall indemnify, hold harmless and/or defend Dealer against any and all actions, suits, losses, damages, claims and/or costs of any kind whatsoever, arising out of the use of any forms provided by Lending Institution and/or Lending Institutions obligations under the Gramm-Leach-Bliley Privacy Act ("GLB").
>
> *Safeguarding Customer Information:* Lending Institution represents and warrants to Dealer that Lending Institution presently maintains, and will continue to maintain and periodically test the efficacy of, appropriate information security programs and measures designed to ensure the security and confidentiality of "Customer Information" (as defined in 16 CFR Section 314.2(b)). Such information security programs and measures shall include appropriate procedures designed to (a) protect the security and confidentiality of such information, (b) protect against anticipated threats or hazards to the security or integrity of such information, and (c) protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any customer of Dealer. Dealer, its representatives and applicable governmental regulators may, from time to time, also audit the security programs and measures implemented by Lending Institution pursuant to this Section, and Lending Institution shall not impose any fees or charges on Dealer, its representatives or applicable governmental regulators in connection with any such audit.

Among the changes which you may elect to request, this will clearly be among the easier changes to sell to the other side. After all, attempting to make an argument that a request for the lender to be GLB - compliant is not reasonable, just doesn't pass the red face test. I have always used this as a starting point for negotiation and have had some considerable success in using this argument to break down barriers with the other side that their agreements are not subject to modification.

C. Lender Myth 3: "We are not really trying to make you the insurer of the transaction"

Typically, when you review the warranties and representations that the lender is attempting to impose, you will make the argument, and properly so, that the lender is attempting to make your client the insurer of the consumer's performance under the terms of the contract and his, her, or their truthfulness in making and application for credit. The standard response you will hear is that the dealer is in a better position to assess the risk presented by the transaction and that, therefore, the warranties requested are only reasonable under the circumstances. A review of that which is typically requested reveals this is plainly not the case. Standard among the warranties requested (and those which generally are not problematic) are those which (i) relate to the state of title of the vehicle being sold, (ii) pertain to cor-

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Message From Executive Director

Jack Tracey, CAE

When a conference ends and the dust settles I always like to review what has happened, the good, and the not so good. I am very impressed with the quality of our Association's first two conferences. The sessions are developed with much care and thought and presented with great professionalism. Everyone wants to contribute to the collective knowledge of our membership. There is an uncommon amount of valuable information being shared among our members. Candid, provocative and timely communications are hallmarks of NADC conferences. If this assessment of our organization is correct, all of our members are better professionals because of NADC. What a fine legacy to have developed in just two short years.

Those in attendance at the conference acknowledged the conference quality through the comments they made on the evaluation forms:

- Great speakers and outlines
- Outstanding
- Not only informative, but also entertaining
- Outstanding. Took a lot of nuts and bolts notes to take home
- Excellent. What a great overview of buy/sell concerns
- Good presentation for a very relevant subject
- Very timely and useful
- Good speakers, substantive and they followed materials
- This was an excellent program. Can't wait until the next one

What could have been done better? Some sessions should have been allotted more time to cover their material. The length of the first day's program could have been shortened. We will take all the comments provided in the evaluations and use the information to build next year's event.

As I've said in the past, NADC will continue to improve through communication among its members. As our membership grows we enjoy the opportunity to learn from a broader base of attorneys representing dealerships. Help us grow. Encourage membership among your peers

US Department of Labor.. from page 1

- Executives, administrative, and professional employees (Note: On August 23, 2004 the United States Department of Labor enacted new regulations under the FLSA that redefine exemptions for overtime pay for certain white-collar employees.)
- Salespersons, parts-persons, service advisors and technicians (Note: It is customary in the auto industry for technicians to receive overtime pay)
- Finance employees (Note: two recent decisions from federal appellate courts in California and Colorado have challenged this conclusion by ruling that finance managers may be entitled to overtime compensation.)

Employers are also required to maintain certain records concerning covered employees. There is no particular form of recordkeeping, but the information must be clearly and accurately recorded in order to facilitate an investigation by the DOL.

Stevan LaBonte, Esq. is an Associate with the firm of Bellavia Gentile & Associates, LLP in Mineola, New York. He is part of the fim's Automobile Dealership Law Practice Goup. Mr. LaBonte has considerable experience in the field of dealership law having spent the nearly 11 years with the Greater New York Automobile Dealers Association (GNYADA). He earned his J.D. fom the Touro College Jacob D. Fuchsbeg Law Center in Huntington, Long Island. Prior to his tenue with the GNYADA, he served as a Consumer Frauds Representative with the New Yok State Departmen of Law, Office of the Attorney General

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porate structure of the dealer and compliance with laws as they relate to licensure, (iii) state that the lender is getting true and accurate copies of the buyer's order and other selling documents generated by the dealer.

What is problematic are representations and warranties which make the dealer the guarantor of the transaction. While the lender will tell you that these provisions are contained in the agreement because your client is in a better position to evaluate the deal, don't believe them. Lenders uniformly try to insulate themselves from the risk of the deal and go so far, in some instances, as to ask for representations and warranties that they know do not comport with their own standard practices. An example of a few of the representations and warranties which one sees are: representations and warranties as to the legal age and capacity of the buyers, the signatures of the buyers are genuine, the buyers have no record or reputation for violation of laws relating to intoxicating beverages and narcotics, and all down payments are to be made in cash. Clearly, without seeking to modify the agreement, your dealer-client is going to become the guarantor of the transaction as the lender originally intended.

The Cure

It should be noted that these representations would not be too significant but for the charge-back language that typically follows the statement that the agreement is non-recourse, and consequently, makes the dealer liable to buy back the contract in the event that any representation and/or warranty proves to be untrue or incorrect. This is what makes these agreements something other than non-recourse. You can attempt to negotiate with the lender to soften the warranties and representations by inserting "best efforts" or "commercially best efforts" language. The other approach is to seek to strike the chargeback language in the agreement. This almost never works. However, I have found some lenders receptive to the idea that chargebacks should only occur where there has been a knowing and material breach and the lender has been materially harmed thereby.

As a matter of logistics and practical application, I would suggest that you ask your dealer-client to negotiate these agreements with your direct participation, as counsel for the dealer, together with *both* the lending officer and their counsel. Bank officers can make a deal but can't make legal decisions. The opposite is true of their attorneys. By getting everyone together and agreeing on modifications "on the fly" you may find that you will be able to dramatically shorten the time it takes to complete the negotiation process.

Apart and aside from the utility of keeping your current lenders honest, it is not unheard of for the lenders that you deal with today to leave the market. It may become difficult if not impossible to defend against audits on a deal-by-deal basis with the passage of time. Vigilance will keep your current lenders honest and, over the long term, will keep your client from facing charge backs from lenders who decide to audit stale transactions; looking for charge-backs that your client unwittingly agreed to pay.

Les Stracher is a Shareholder with the twenty-five member law firm of Rothstein Rosenfeld Adler, PA, in Fort Lauderdale, Florida. He is the Chairman of the firm's Automotive Law Practice Group. In that capacity he advises dealers on mergers and acquisitions for dealers throughout the country, and concentrates on the advising dealers on their day-to-day operations. Mr. Stracher has been involved in numerous buy-sells as well as complex corporate structuring and third party negotiations associated with these transactions as well as other legal issues related to the representation of dealers including, franchise disputes, fixed operations, consumer defense, contractual review and compliance issues.

Special Workshop: California Car Buyer's Bill of Rights

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