House Legislative Analysis Section
Manufacturer's Bank Building, 12th Floor
Lansing, Michigan 48909
Phone: 517/373-6466

MOTOR FUEL FRANCHISE ACT

House Bill 4244 as passed by the House
Second Analysis (1-8-90)

RECEIVED
05 19

Sponsor: Rep. Curtis Hertel
House Committee: Transportation
Senate Committee: State Affairs, Tourism & Transportation

THE APPARENT PROBLEM:

Since the oil embargo of 1973 the motor fuel distribution industry has undergone radical restructuring. Oil companies ("franchisors") attempted to, and in many cases, did, extend their control over gas service station dealers ("franchisees") in order to more carefully regulate volume of sales and reduce losses. The extension of control by the companies apparently has left many dealers with little say in decision-making processes concerning service stations. One of these decisions involves the transfer of franchise ownership to a third party. Oil companies usually reserve the right within a written contract to grant or refuse transfer of ownership of a franchise to another party, which includes ownership transfer to a relative upon the station owner's death ("survivorship"). While some transfers may be granted, service station owners apparently find the opposite is true in many instances; their position is further frustrated since oil companies do not have to even give reasons for refusing a transfer. Some people feel legislation is needed to give franchisees greater control over decisions regarding transfer of ownership, and, specifically, that an oil company should have to give objective reasons for refusing a transfer.

THE CONTENT OF THE BILL:

The bill would create the Motor Fuel Distribution Act to regulate the termination and transfer of motor fuel franchises and to provide for certain business practices. Specifically, the bill would prohibit a franchisor from withholding its consent to any sale, assignment, or other transfer of the franchise to a qualified third party by a franchisee unless the franchisor could demonstrate for reasons that could be supported by objective facts that the proposed new franchisee would be unable to adequately function as a franchisee or would normally not be granted a franchise if the party was an applicant for a new franchise. Under the bill, a qualified third party would become a franchisee immediately upon the sale, assignment or other transfer of the franchise.

Survivorship, Transfers. Following the death of a motor fuel retailer franch see, the franchisor would enter into a new franchise with the designee of the motor fuel retailer franchisee on the terms and conditions then generally being extended by the franchisor to similar franchisees. This transaction could only take place if the franchisee had notified the franchisor of the designee 90 days prior to renewal of the leased marketing premises (and prior to death) and the designee was the surviving spouse, adult child, adult stepchild, son-in-law, or daughter-in-law of the franchisee who would be a qualified third party. The designee, who met all requirements of the bill, would become the franchisee immediately upon the death of the designator franchisee.

The bill would prohibit a franchisor from preventing the sale, assignment or other transfer of a franchise to a corporation in which the franchisee had and maintained a controlling interest if the franchisee offered in writing to personally guarantee the performance of the obligations under the franchise. In the event of a transfer the franchisor could require the corporation to assume, in writing, all of the franchisee's obligations to the franchisor and require the franchisee to maintain a controlling interest in the corporation and actively operate the marketing premises during the time that the franchise with the corporation continued.

One Recognized Holiday Annually. A franchisor could not prevent a franchisee from closing during one "recognized" holiday per calendar year as determined by the franchisee, nor could a franchisor prohibit a franchisee from closing on Sunday or the Sabbath. The franchisee would have to provide the franchisor with at least 60 days' notice of any closing due to a holiday, and the period of closing would be limited to the 36-hour period of 6 p.m. the day before the holiday to 6 a.m. the day after the holiday. This provision would not apply to "marketing premises" (service stations) used by the franchisee that were within one quarter mile of an interstate highway exit.

Legal Recourse for Violations. Under the bill, a person who sustained injury to his or her business or property by reason of a violation of the bill could bring an action in any court having jurisdiction in the county where the defendant resided or was found, or where service could be obtained, for injunctive relief or to recover damages sustained, and could be awarded attorney fees together with the costs of the action.

FISCAL IMPLICATIONS:

According to the Senate Fiscal Agency, the bill would not have state or local budgetary implications. (11-29-89)

ARGUMENTS:

For:

Currently, a dealer may sell or transfer a station only if an oil company gives consent to the deal and agrees with the dealer's choice of purchaser. Thus, a dealer may have worked hard to build up a station only to find that he or she cannot sell the station to the most appropriate buyer. The bill will allow dealers to sell their franchises to qualified third parties and require oil companies to use objective facts when deciding to withhold their consent of a purchasing agreement. Thus, oil companies would be protected from sales of franchises to clearly unacceptable third parties, while dealers would have some discretion in deciding the purchaser of a franchise.

OVER

For:

Upon the death of a franchised dealer, a franchise may be terminated. Many service station franchises are family-owned and the families of these franchise owners face an uncertain future because of the stipulation concerning a franchisee's death. There is no reason that a competent spouse or child of the deceased should not be able to take over a franchise. A survivor will probably be more capable of running a franchise than a new dealer because in many cases the survivor probably will have already successfully dealt with customers and the oil company involved. The bill would ensure that a qualified survivor would be allowed to take over a franchise, but would still protect an oil company's right to terminate an incompetent survivor.

Response: The survivorship provision would be a violation of fair business practices and sanctions open nepotism. Future dealers would be chosen based upon their relationship with a dealer instead of through open competition among qualified applicants.

For:

Due to decreased traffic on some major holidays, the bill would allow dealers the option to choose one holiday per year on which they would not be be open for business, covering a 36-hour period beginning before and ending after the holiday itself. The bill would also allow franchisees to close on Sunday or the Sabbath. Since many people tend to drive little or not at all on certain holidays, dealers forced to stay open during these times often are wasting their own time and money. Also, allowing them the option to close on certain days would give service station operators the opportunity to spend more time with their families.

Response: The provision in the House-passed version of the bill preventing a franchisor from prohibiting a dealer from closing on Sunday or the Sabbath could be construed as giving dealers the option to close for an entire weekend. While this was intended to permit dealers the option of not working on certain days for religious reasons, some dealers could abuse the intent of the provision by closing for no apparent religious purpose. Even if dealers were to abide by the spirit of the amendment, it seems inappropriate for the state to say when a private company can or cannot keep its holdings open for business.

Against:

The bill would prohibit oil companies from effectively managing their investments. According to testimony in the House Transportation Committee, a service station dealer's investment in a franchise averages about 20 to 30 percent of the total cost of operating and maintaining a service station, including costs for inventory of gasoline and other products, hand tools and capital. Oil companies, conversely, invest a great deal more: estimates of the average worth of a station range from $500,000 to $1.5 million. In addition to paying most of the franchise's start-up costs, oil companies provide other services such as comprehensive paid dealer training, start-up assistance, and advertising. The bill would remove an oil company's control over its investment by allowing dealers to designate a survivor as an automatic lessee upon the dealer's death, and by requiring companies to take extra time to detail why a proposed purchaser of a franchise was unacceptable.

Response: The bill would allow oil companies to reject applicants for franchises who are found to be unqualified based on objective standards. Thus, their control over their investments would be maintained.

Against:

The bill's survivorship provision is an unconstitutional threat to property rights. A "franchisee" (in this case, a service station dealer) *leases* property from a "franchisor" (an oil company) in order to sell gas at a particular location. The oil company owns a large percentage of the property where gas or other items are sold, including all rights to the trademark under which the gas itself is sold, and should not be forced into a contractual position it feels could jeopardize its own investments. For instance, a surviving relative or other designated transferee may not be capable of operating the franchise effectively, or may not even wish to continue using the property to sell gas as established under the original contract. Government intervention into the bargaining process could hinder a company's ability to find the most qualified individuals to operate its holdings, which, in turn, could severely damage its competitive position in the market. Senate Bill 428 was enacted this year (Public Act 88) to regulate a similar relationship that exists between boat manufacturers and dealers. That act simply requires a contract to be written and that the contract cover various concerns within the business relationship (such as the marketing area of a distributor). Contract provisions within this bill go well beyond the scope of that act.

Against:

As the bill deals with complex corporate and legal issues it should be referred to a subcommittee where various issues involved in the bill could be studied more in-depth. Central to the thrust of the bill is how the relationship between an oil company and one of its dealers or distributors is defined. Is an oil company a "franchisor" as that term is defined under the state's Franchise Investment Law? Are those costs a dealer invests in a service station similar to "franchise fees"? Apparently, judicial opinions have not yet satisfactorily answered these or similar questions. In fact, an attorney general's opinion (OAG 89-128) has been requested, and is still pending, which could shed some light on these questions. Further, the bill's survivorship provisions could conflict with, and be pre-empted by, contractual guidelines established in the federal Petroleum Marketing Practices Act. To move the bill forward before the opinion is issued, or without knowing the bill's impact on how other franchisor/franchisee relationships are interpreted, would be premature and unwise.

POSITIONS:

The Service Station Dealers Association of Michigan supports the bill. (1-8-90)

Mobil Oil Corporation opposes the bill. (11-29-89)

Amoco (American Oil Corporation) opposes the bill. (1-5-90)

The Associated Petroleum Industries of Michigan, a division of the American Petroleum Institute, opposes the bill. (1-5-90)