House Legislative Analysis Section

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FARM EQUIPMENT AGREEMENTS

House Bill 4506 (Substitute H-2)
First Analysis (3-10-94)

Sponsor: Rep. Lloyd F. Weeks
Committee: Business & Finance

THE APPARENT PROBLEM:

When farm machinery breaks down during planting or harvest season, it is essential that it be repaired as quickly as possible. Farm machinery dealers must therefore carry large inventories of parts and machines in preparation for all such events. In fact, some contracts between farm equipment dealers and suppliers contain stipulations that certain inventories, worth, in some cases, over $1 million, be maintained by dealers to meet emergency demands. As a result of this requirement, a clause requiring that a supplier repurchase a dealer's inventory when a contract is terminated has always been an important part of any contract between a farm machinery dealer and his or her supplier.

Another reason that a "buy-back" clause is important for farm equipment dealers is that most operate under franchise agreements with suppliers that allow them to sell equipment manufactured by a specific company -- Case International Farm Equipment, or John Deere, to name a few. However, unlike contracts that cover, say, employment practices, franchise agreements are somewhat flexible. For example, a supplier of XYZ equipment may notify a dealer that a new line of tractors is being introduced, and the old line of equipment, including the necessary parts and accessories, is being discontinued. If the dealer wants to continue selling XYZ tractors, then he or she must buy this new line of equipment. Since it would be extremely difficult for a small business to finance the purchase of new stock unless it got rid of its old inventory, the dealer would probably go out of business in this situation, were it not for the buy-back clause in the contract.

The Farm and Utility Equipment Act was created in 1984 to protect dealers from losses in such situations. However, other circumstances also serve to create problems in contracts between farm equipment dealers and suppliers. Changes in the global economy resulted in mergers and consolidations in multi-national corporations. In the flux and change of the business world, it became not uncommon for a large company to close down its operations in this country and relocate in another, or to close down in this country and turn its operations over to a subsidiary in another country. When this happens, questions arise regarding contracts that the company has entered into. Who inherit the company's obligation to its dealers? Is it the newly formed corporation, or is it the company's remaining subsidiaries? The proponents of the original legislation say that certain provisions of the act need to be updated to provide clarification on this and other issues. They ask that a broader definition of the term "supplier" be provided; and that the definition of dealer supplies that may or may not be returned upon termination of a contract be clarified.

THE CONTENT OF THE BILL:

The Farm and Utility Equipment Act regulates agreements made between persons who sell farm and utility equipment (that is, dealers) and those who supply them with their equipment inventory. Generally, the act requires an equipment supplier to repurchase a dealer's surplus inventories if an "agreement" (i.e., a written or implied contract) between the supplier and dealer is terminated. The bill would amend the act to add new provisions governing the obligations of both a dealer and supplier when inventory goods must be repurchased due to the termination of an agreement. Under the bill, an agreement would include an oral contract made between these parties. The bill also would expand the definition of "supplier" to include any controlled group of corporations, including "parent-subsidiary" or "brother-sister" controlled groups or other "combined groups." The provisions of the bill would apply to contracts entered into after January 2, 1990.

Repurchase requirements. Currently, when an agreement between a supplier and dealer is terminated, the supplier must pay to the dealer 100 percent of the net cost of all new, unused, undamaged and complete tractors, equipment and attachments, and 90 percent of the current net price of all new, unused and undamaged repair parts. The bill would revise this provision to specify that a supplier would have to pay 100 percent of the net cost of only all undamaged and complete tractors, equipment and attachments "which are resalable, less a reasonable allowance" when the equipment was used for demonstration or rental purposes. Provision also would be made for situations where inventory that was to be repurchased had been rented or used for demonstration purposes.

In addition, the supplier would have to purchase or repurchase--at the dealer's book value net of depreciation on the date of termination--all dealer supplies, with the following exceptions: no "electronic device" more than five years old would have to be purchased; the supplier would have to assume the dealer's lease obligations with respect to any dealer supplies that were leased; and the supplier would have to pay the dealer at least 75 percent of the supplier's net price last published for any new dealer supplies purchased from the supplier.

<u>Return of inventory</u>. The bill would permit a dealer, with or without the prior consent or authorization of a supplier, to ship all inventory suitable for repurchase to the supplier not less than 60 days after the supplier had notified the dealer, or the dealer had notified the supplier by certified mail, that the agreement between them had been terminated. The supplier could inspect a dealer's inventory and designate portions of it as not returnable under the bill's provisions. This designation would not be effective, however, if it were received by the dealer more than 30 days after a contract was terminated.

Not more than 90 days after an agreement was terminated, the dealer could ship inventory to any location from which goods of like kind had been shipped to the dealer in the 12 months preceding the shipment, or, if such goods hadn't been shipped in this time period, to any place of business maintained by the supplier. The dealer would have to pay the freight charge and the supplier would have to accept the shipment. If a properly-shipped shipment was undeliverable or not accepted by the supplier, the dealer could order the inventory returned, order it stored for the supplier's account, or order it liquidated or abandoned by the carrier.

A supplier would assume all risk of loss for properly-shipped but undeliverable or unaccepted goods, including, but not limited to, losses from exposure, liquidation, abandonment or theft. A supplier's acceptance of a shipment would not constitute an admission that the inventory inspected by him or her before it was shipped and declared not returnable would have to be repurchased, but that all properly-shipped inventory that was not deliverable or not accepted was considered to have been properly submitted for repurchase, and the supplier would be liable to pay the repurchase amount for that inventory.

Instead of returning inventory to a supplier in this way, a dealer could notify the supplier by certified mail that the dealer had inventory which he or she intended to return. The notice would have to be in writing, and the accuracy of the inventory list and suitability of items for repurchase would have to be sworn to by the dealer before a notary public. The notice would have to contain certain identifying information of the person in possession of the goods as well as of anyone authorized to act on behalf of the dealer as an "escrow agent." A supplier would have 30 days from the date the notice was mailed to inspect the inventory and verify the accuracy of the dealer's list. Within 10 days after inspection, the supplier would have to do one of the following: pay the escrow agent; give evidence that a credit to the dealer's account had been made if the dealer had outstanding sums due the supplier; or send to the escrow agent a credit list and shipping labels for the return of inventory to the supplier that were acceptable as returns.

If a supplier sent a credit list to the dealer's escrow agent, payment or a credit against the dealer's indebtedness for the acceptable returns would have to accompany the credit list. Upon receipt of 1) the payment, 2) evidence of a credit to the dealer's account, or 3) the credit list with payment, the title to the inventory acceptable as returns would pass to the supplier who made the payment or allowed the credit, and the supplier could keep the inventory. The escrow agent would have to ship or cause to be shipped the inventory acceptable as returns to the supplier unless the supplier elected to personally perform the inventorying, packing and loading. When the inventory was received by the supplier, the escrow agent would have to be notified of this by certified mail and he or she would have to disburse 90 percent of the payment he or she had received--less its actual expenses and a reasonable fee for the agent's services--to the dealer. The agent would have to keep remaining funds in the dealer's escrow account until he or she was notified that an agreement had been reached regarding the nonreturnables, after which remaining funds would be disbursed and remaining inventory disposed of as provided in the settlement.

Bringing of an action. A dealer could bring an action against a supplier in a court of competent jurisdiction for actual damages sustained by him or her that resulted from a supplier violating the bill's provisions, together with the actual costs of the action and reasonable attorney fees. A dealer located in the state could not waive his or her right to bring any action under the act in the state's courts, and a dealer would not--simply by contracting with a supplier in another state--be considered to be doing business in another state.

Termination of an agreement. A supplier could not terminate, cancel, fail to renew or substantially change the competitive circumstances of an agreement "without good cause" and would have to provide a dealer at least 90 days' prior written notice before taking any of these actions. The notice would have to state why action was taken and would have to specify that a dealer would have 90 days to rectify any claimed deficiency. If a corrective plan was submitted or the deficiency rectified within 90 days, the notice would be voided. Provisions requiring a notice to be given would not apply if the reason for termination, cancellation or nonrenewal was insolvency, the occurrence of an assignment for the benefit of creditors, or bankruptcy.

If an agreement was changed because sums due under it hadn't been paid, the dealer would be entitled to written notice of default in payment and would have 10 days from the date when the notice was made to correct the default. A dealer could bring an action in any court of competent jurisdiction for damages and injunctive relief if a supplier failed to give prior notice and could recover the actual costs of the action, including reasonable attorney fees.

Arbitration. If an agreement was terminated, any party to it could require that all issues relating to the parties' rights under the act be submitted to binding arbitration under the supervision of the American Arbitration Association or a similar binding arbitration process to which the parties could agree. An arbitrator's decision would be final unless procured by fraud.

MCL 445.1452 et al.

FISCAL IMPLICATIONS:

According to the House Fiscal Agency, the bill would have no impact on state funds. (3-9-94)

ARGUMENTS:

For:

Farm equipment dealers have advocated for changes in the Farm and Utility Equipment Act that would supply additional details on the obligations of both parties when contracts between farm equipment dealers and suppliers are terminated. During the past decade, a general downturn in the economy has had serious consequences for the farm equipment industry. Massey Ferguson, one of the oldest farm equipment companies, has ceased operations in the United States. An 80 percent reduction in farm equipment sales also convinced Ford Motor Company to leave the field four years ago. Beginning in the 1980's, economic changes also resulted in mergers, consolidations, and the movement of large multinational corporations to other countries -- practices that not only affect the corporation's employees, but also the contracts and franchise agreements that bind a company to its equipment dealers and franchisees. When these events take place, farm equipment dealers say that they are at the mercy of suppliers. Dealers maintain that suppliers, being large corporations, have the resources to hire large legal firms that can argue successfully for interpretations of contracts that are favorable to their clients. The bill would help avoid future litigation by provisions that clarify the relationship between dealers and suppliers; that extend the act's definition of "supplier" to include companies that are members of corporate chains; that specify the types of farm equipment that a supplier must repurchase; and that outline the procedures to be followed when inventory must be returned for repurchase by a supplier.

Against:

Negotiations between manufacturers and dealers should be conducted in the private sector through bargaining in the free market system. The bill would provide a legislative mandate that spells out the exact nature of the relationship. Competition would decrease as a result of the bill.

Response:

The bill would not restrict the bargaining process in any way. Manufacturers and dealers would still work out the details of their agreements. The bill would simply require both manufacturers and dealers to provide more detail about the expectation and obligations of their relationship.

Against:

The provisions of the bill would apply to contracts entered into after January 2, 1990. This provision is patently unfair to those who have lived under the conditions of a contract for four years.

Response:

The bill requires that the provisions of the act apply to contracts entered into after January 1, 1990, to assure that these provisions are extended to contracts currently in effect. To do otherwise would leave open the possibility that current contracts could be terminated to avoid the provisions of the bill.

POSITIONS:

The Michigan Equipment Dealers Association testified before the committee in support of the bill. (3-8-94)

The Michigan Merchants Council supports the bill. (3-8-94)

Deere and Company does not oppose the bill. (3-7-94)

Caterpillar, Inc. does not oppose the bill. (3-7-94)

The Michigan Trial Lawyers Association has no position on the bill. (3-8-94)

The Michigan Manufacturers Association has no position on the bill. (3-8-94)

The Michigan Farm Bureau has no position on the bill. (3-9-94)

The Michigan State Chamber of Commerce has no position on the bill. (3-9-94)