

OEM Sales And Service Agreements

Are They Functional or Fractured?

In our highly-acclaimed textbook, ***Achieving Excellence in Dealer/Distributor Performance***, author Walter McDonald presents his recent research on “How Dealers Evaluate Their Manufacturers” in Chapter 29.

In the following article by Jim Wilson, we continue the discussion on how to improve dealer/distributor relations with their OEMs. Jim now takes this important issue to the next level. He offers recommendations on how dealers can avoid problems with OEM Sales and Service Agreements:

How Dealers Can Avoid Problems with OEM Sales and Service Agreements

By Jim Wilson

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After almost a 50-year career working in the equipment industry, both for OEMs and as a consultant to dealers/distributors, I'd like to share just a few simple observations. In a worst case scenario these thoughts and recommendations may help you and your OEM get to “yes” rather than battling out legalities in court.

BACKGROUND

When I took my first job as an OEM division manager many years ago, my boss said:

“We don't run our business on Sales and Service Agreements. Look at them for your dealers then put the documents in the drawer. Hopefully, you can leave them there.”

What he meant was if both parties want the relationship to work, they don't need to govern their daily business by a *Sales and Service Agreement (Agreement)*. However, both the OEM and the dealer, as they conduct their business, need to be respectful and mindful of the intentions, mutual expectations and landscape defined by a business Agreement.

CAUSES OF CONFLICT

When two parties begin to constantly scrimmage over the language of an Agreement in their day-to-day operations, communications and trust have begun to break down and customers may get caught between these clashes. Although not limited to these reasons, here are eight common causes:

- 1. Both parties misunderstood the Agreement.**
- 2. The wording of the Agreement was ambiguous.**
- 3. Key principals to the Agreement have changed (retirements, promotions, death or, resignations).**
- 4. Uncertainty as to which Agreement is in effect.**
- 5. Lack of familiarity with the Agreement.**
- 6. A sense that conditions have changed over time and the Agreement could be unreasonable.**
- 7. One or both parties never intended to honor the Agreement.**
- 8. State or federal law prohibit certain aspects of an Agreement.**

THREE CASES

How easily can things go wrong? In one situation the OEM had gone through a cycle of Agreements due to brand acquisitions and mergers. This OEM lost sight of what particular Agreements dealers were still operating under.

In another case, when a distributor principal retired, his successor neither grasped the Agreement nor sufficiently familiarized himself with it.

And, in a third situation, the dealer principal was a neighbor of the CEO of his OEM in a resort community. The principal leveraged this with his OEM contacts and inferred that he had protection from some aspects of the Agreement. When the CEO retired, this house of cards collapsed and the dealer was replaced for non-performance. The morale of this story is if you are a dealer, do not assume that special relationships exempt you from complying with the letter of an Agreement.

All of these situations resulted in expensive and time consuming litigation that could have been avoided.

RECOMMENDATION—*Ensure Clarity*

Here are some constructive thoughts that some may find helpful.

View the Sales and Service Agreement like you would with some of the new safety features and instruments on modern vehicles. One must become familiar with them. They exist to keep you from running off the road or into someone.

Of course, you can't drive a vehicle by just focusing your eye on the instruments. Nor can you run a business by becoming overwrought over every nuance in a sales and service agreement. However, it is essential in this age of excessive litigation, that an experienced lawyer on contractual Agreements makes sure that the relevant language is as clear and concise as possible and that you understand the obligations.

RECOMMENDATION—*Periodic Agreement Review*

Whether you work for an OEM or a distributor, I recommend your company makes sure key parties subject to the Agreement get a periodic review and training session on the spirit of the document governing their business conduct. If they have questions, then do your best to answer them or get an official interpretation. A once a year review should be sufficient.

RECOMMENDATION—*Annual Compliance Verification*

Likewise, signers to an Agreement or their designated representatives should formally meet at least once a year with one another to verify compliance with an Agreement and/or satisfaction with the relationship. For the twenty percent of your Agreements that feed eighty percent of your business, there is too much at stake not to formalize these processes. Anticipate potential problems and head them off before they exist.

RECOMMENDATION—*Update New Executives on Agreements*

If new people of authority are brought on board such as a dealer principal, general manager, department head, or regional manager, it is highly advisable that not too much time elapses without giving them some exposure to the critical Agreements that drive your business. If you fail to do this, one of your people might violate the Agreement. In a worse case, this blunder could end the business relationship or result in the offended party's refusal to work with the individual who violated the agreement.

RECOMMENDATION—*OEMs: Keep Agreements Current*

If you are an OEM, limit the life of your Agreements so that they have meaning and don't become entitlements. This forces you to keep them current and to standardize the language.

RECOMMENDATION—*Recognize Anniversaries*

For the important parties you do business with, whether dealer/distributor or OEM, thank them for doing business with you. On anniversaries ending in five even consider a special dinner or lunch. This is not a celebration of longevity of

the Agreement because that may designate entitlement, but rather a nice human touch that says you value the business the other party has given you.

There are just a few reasons why you may have provisions for immediate termination of the Agreement. For example:

- Committing fraud.
- Misrepresentation on a matter material to the agreement.
- Breach of the agreement because of a refusal to do what was agreed upon.
- A change of the principal on the agreement without the approval of the other party.

Everything else should usually be subject to a ***cure period***. The “cure period” is part of a formal written warning letter and it sets a deadline to correct a violation of the Agreement and it usually requires a formal written action plan and specific timetable for achievement.

Having to enter into a new Agreement after a defined period of time has value to both parties. It is sort of like repeating your wedding vows. Industry and market dynamics may have changed enough to merit an overhaul of a standard Agreement. An update may also allow for inserting a side letter that recognizes the unique circumstances of an individual relationship.

If you are entering into a first time business relationship, both the OEM and distributor/dealer must recognize that newness means that performance goals must be reasonable and not what would be set for an established relationship. If you are a distributor, get in writing what support the OEM will provide during a startup period over several months.

WHAT TO DO IF A DISPUTE OCCURS

What do you do when a dispute emerges over the language of the Agreement? How you react may determine whether the business relationship survives.

First, it is important to know if an OEM tolerates an omission by a dealer regarding a particular provision, then it may set a precedent that undermines all Agreements regarding that particular provision. So most OEMs will push back hard to enforce compliance. They usually have more financial resources than a dealer to defend their Agreements.

If an OEM or a distributor sends a warning or ***demand letter***, the relationship has begun to spiral toward disaster. A “demand letter” states the provision of an

Agreement that has been trespassed and spells out the action or next steps the OEM expects. It can range from surrendering the Agreement to requesting a meeting to discuss resolution. Getting to this state can be avoided by speaking to one another openly and honestly about a perceived offense. This first step may clear up legitimate misunderstandings or even lead to an amendment to the existing Agreement.

Neutral Third Party Review

If an Agreement cannot be resolved through civil discussion and negotiation, then before taking the matter to the courts, you should consider retaining a neutral third party to review your situation and to see if he can guide you to a resolution, short of a lawsuit proving detrimental to both parties.

Arbitration

A next step may be arbitration. This may prove less destructive, expensive, and disruptive to business than subpoenas for files, records, emails, letters, and giving and responding to depositions.

Downside of Litigation

When a relationship has degenerated to litigation, you must assume your customers and employees will get wind of it. Some may leave your business or question your integrity. And, be prepared to pay a high price for ego or ignorance. If you go to court, a final settlement may take years due to appeal processes. This can be a drain on your financial as well as personal and family health.

FINAL THOUGHTS

It is important to stay familiar with the critical language in your Agreement. Be sure you know what you signed when you entered into an Agreement. If you take exception to standard language in an Agreement, try to negotiate for a valid exception before signing it. Then do your best to honor your Agreement, recognizing that there is always room for some legitimate interpretation or at the very least an apology for an offense and corrective action.

If the offended party is open to discussing corrective action or cure period as mentioned earlier, do make sure that your counterpart to the Agreement concurs with the steps, measurements, and timeframes. Then make sure your team understands the stakes and importance of executing the new action plan you proposed to remedy the violation. If your company falls short of the plan, your business may not get another chance to comply with the Agreement.

If for some reason you cannot continue to operate under an existing Agreement, then meet with the other party and work to either amend the Agreement or end the relationship in a manner that is least disruptive to both businesses.

Finally, remember, both distributors and OEMS can acquire a negative reputation in their industry for how they conduct themselves in these matters, possibly

making it more difficult to find a future business representative/supplier. You may assume all disputes are confidential, but somehow over time, word has a way of getting around to either the dealer network and/or the industry.

Jim Wilson is willing to suggest resources for helping to resolve Sales and Service Agreement disputes. (jmwilson0426@gmail.com)

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