

# Dealers resurrect demand for franchisee protection law

Harley-Davidson's abrupt exit from India last month and another three OEMs' departure in recent years has brought the issue of introducing strong legislation to protect franchisee owners to the fore. It was a subject first raised two decades ago, reveals **Shahkar Abidi**.

On December 13, 1996, when most of North India was under the grip of severe winter chill, a landmark judgement at Delhi High Court had India Auto Inc all. The litigation, which came to be known as Classic Motors vs Maruti Suzuki, was probably the first time that the issue of bringing in legislation to protect franchisees was raised in the country.

The petitioner, a Delhi-based car dealer, challenged Maruti Suzuki's action of terminating its dealership contract by merely giving 90 days' notice, without offering any valid reason. There were also some allegations made by the petitioner against RC Bhargava, then a prominent member of Maruti Suzuki India's marketing team. The interest around the case was further amplified due to the presence of some of India's finest legal minds including former finance minister Arun Jaitley and TK Ganju (both representing Maruti Suzuki) and Madan Bhatia (representing Classic Motors) who debated on multifaceted aspects of the relationship between franchisor and franchisee.

The court judgement, which finally went in favour of the vehicle manufacturer, relied heavily on some of the watershed legal precedents from around the automobile world including United States versus Arnold, Schwinn & Co. and Vijay Traders versus Bajaj Auto

amongst others. Also, the allegations made against Bhargava were found to be without any substance.

Recollecting the case more than two decades later, Bhargava, who is now chairman of Maruti Suzuki says, "For Maruti, relationship with dealers has always been excellent, though from time to time there have always been some dealers who for various reasons had to leave the organisation. This may happen in any organisation". "Classic Motors, perhaps was the only case when somebody made allegations," Bhargava, a former bureaucrat, told *Autocar Professional* in a telephonic conversation.

## Flurry of OEM exits in recent years

Though the vehicle showroom parc has grown massively in recent years, even as new OEMs have entered the automobile market, the subject of franchisee protection laws has largely remained under the carpet. The exit of four OEMs – General Motors, MAN Trucks, UM Lohia and Harley-Davidson – in the past three years has brought the issue back into the limelight.

There is a growing feeling amongst showroom owners that a franchisee protection law may help in providing a level-playing field between vehicle manufacturers and dealers. The developments



## THEY QUIT INDIA

**General Motors**  
End-2017  
**MAN Trucks**  
August 2018  
**UM Lohia**  
October 2019  
**Harley-Davidson**  
September 2020

even prompted the Federation of Automobile Dealers Association (FADA), which represents over 15,000 dealers to approach the Centre in end-2019 to introduce a 'Franchisee Protection Act'. In fact, for FADA's newly elected president Vinkesh Gulati, the issue has been right on top of his agenda since he took over in September this year.

"Currently, the arrangement between a dealer and an OEM or supplier is covered under a normal contract agreement, and it's usually lopsided. We will be working with other

retail associations also for the franchisee law, as it will benefit all the retailers," Gulati told *Autocar Professional*, echoing the beliefs of dealer community on the issue. "Had there been franchisee protection laws, brands like these would not have abruptly closed their operations, leaving their channel partners and customers in a fix," emphasised Gulati.

FADA is said to be working on developing a legal framework for the legislation, apart from lobbying with the government for a franchisee protection act.



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**Vinkesh Gulati, president, FADA:** "Had there been franchisee protection laws, brands like these (Harley-Davidson, UM Lohia, MAN and GM) would not have abruptly closed their operations, leaving their channel partners and customers in a fix."



**Karan Singh Chandhiok, Partner, Head (Disputes and Competition), Chandhiok and Mahajan:** "Any similar legislation in India would increase the compliance burden for both franchisor and franchisee and limit a party's freedom to contract."



**Inder Mohan Singh, Partner (General Corporate), Shardul Amarchand Mangaldas & Co:** "In case of termination which is in violation of the agreement, the franchisee may pursue arbitration / civil proceedings against the franchisor, for damages and losses."

the vehicle manufacturer turns insolvent, claims for compensation can be made under the framework of the IBC though filing fresh suits or arbitrations will be barred due to the moratorium.

Karan Singh Chandhiok, Partner, Head - Disputes & Competition at Chandhiok and Mahajan, claims that the current legal system provides sufficient safeguards for franchisee owners. "At the end, the dealer agreement is the Bible that governs the relationship between parties," says Chandhiok. Dealers, however, differ in their views claiming that situation on ground remains different as OEMs invariably dictate terms by formulating standard agreements and calling shots on most of the occasions.

Likewise, for end consumers, though existing laws provide safeguards under the Consumer Protection Act, 2019, in actual practice, redress of such grievances remains only a legal recourse. Vehicle purchases come with an assumption that the OEM will continue to provide aftermarket services for several years even after expiry of the warranty period. In case of operation closure, the OEM generally makes arrangements to provide services for vehicles under warranty. However, for out-of-warranty products, OEMs generally do not have a long-term plan, thereby leaving consumers in a lurch.

**Multiple laws hamper franchisor-franchisee pact**

In absence of any franchisee-related legislation, a myriad of laws regulate the relationship between a dealer and OEM in India. Some of them are the Indian Contract Act, Specific Relief Act, Competition Act, Insolvency and Bankruptcy Code (IBC) and Intellectual property Act.

As per legal experts, a typical dealer agreement allows both the parties to terminate the relationship by giving an advance notice. In business parlance, this is referred to as 'no fault' termination. However, the dealer can negotiate a clause seeking compensation in case of a termination without cause. The damages sought can be for actual, indirect and even consequential losses. Some of the main legal disputes that arise in India

**DEALERSHIPS VS MANUFACTURERS**

**Vijay Traders vs Bajaj Auto:**

In 1995, an Ahmednagar dealer took Bajaj Auto to court, alleging that the Pune-based OEM had appointed it as its permanent sole selling agent in mid-1960s. Bajaj Auto later terminated the agreement. The plaintiffs alleged that this termination was wrongful, illegal and without proper notice, causing loss to the plaintiffs. The defendants contested

that their relationship was that of principal to principal. The plaintiffs used to pay for the said automobiles and sell them independently.

**US vs. Arnold, Schwinn & Co:** In 1967, an anti-trust action was brought by the US against Arnold, Schwinn & Co and its distributor Schwinn Cycle Distributors Association. Arnold only allowed distributors to sell its products to approved dealers. Declaring this to

be unlawful, a district court allowed for sales directly from Arnold to dealers. In an appeal, the Supreme Court in a 5-2 decision held that it is unreasonable for manufacturer to restrict where its products are sold after it has transferred title and responsibility for loss. Hence, in circumstances where Arnold retains the title and dealer act as an agent, those restrictions are not a constraint on trade.

between the franchisor and franchisee relates to wrongful termination and misuse of IPR, though these are very specific issues, the experts add. Interestingly, it is this aspect which was the main bone of contention in the Classic Motors vs Maruti Suzuki case. Here, the petitioner had alleged

that he was made to sign on a standardised form of contract by the defendant, and his contract terminated without cause.

Secondly, there may be specific clauses in the agreement such as buyback of unsold stock, which can be used to bring a claim. Further, if

**American bikemaker UM Motorcycles and its Indian partner Lohia Auto shut shop in India in October 2019. The last product launch was the Renegade Commando Classic, priced at Rs 189,000, in September 2017.**



**Strong franchisee regulation in some matured markets**

According to legal experts, even as India Auto Inc debates over a Franchisee Protection Act, the legislation per se is not very common worldwide. Like India, the UK does not have any specific law for it. However, some countries including the US, China,

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Australia and South Africa have special laws dealing with franchisee agreements.

In the US, franchisee rules prescribe disclosures to be made by a franchisor before entering into a franchisee agreement, to ensure that a franchisee has adequate information available before entering into a pact. In addition, many States within the US have enacted laws regulating franchisee relationships. Some have enacted statutes impacting a franchisor's right to terminate or a franchise agreement to have a "good cause". The term "good cause" may include failure to meet the terms of franchise agreement including sales quota or quality parameters, amongst others. China has similar provision. In South Africa, the Consumer Protection Act governs the offer of franchisees but it does not lay down any specific requirements for terminations.

However, Australia has regulation stronger than most of these countries. The Australia Competition and Consumer Commission

has a Franchising Code of Conduct which requires disclosure (similar to US), registration, a good faith obligation, a dispute resolution mechanism, a cooling-off period and procedures for ending a franchise agreement. This includes specifying the notice period for termination. ACCC also introduced a specific amendment for the motor vehicle sector, which provides for a one-year notice period for a franchisee agreement with a term of one year or more.

#### The devil is in the detail

Indian auto industry stakeholders claim that despite the safeguards from the existing laws, the loopholes remain. So, what is the way forward?

Stakeholders claim that in order to protect the interests of dealers and end consumers, there is a need to bring new legislation or suitable amendments be made in the existing laws. A key requirement is for OEMs to provide aftermarket support and services to customers for at

**A Harley-Davidson India showroom in Bangalore. Its 35 dealers, who invested around Rs 3-4 crore each in setting up the showroom, service bays, buying stock and appointing personnel, now face an uncertain future following the company's exit on September 24, 2020.**

least 10 years after closure of operations. It will also help if the OEM continues to have an office to address customer or dealer complaints.

"A law that sets out the framework for both key stakeholders and balances their rights would be welcome," says Chandhiok, emphasising that the changes be brought with some caution. "At the same time, the law makers must be cognizant about the additional regulatory burden, compliance costs for both dealer and manufacturer and the impact of reducing the parties' freedom to contract," he adds.

Offering a similar perspective, Inder Mohan Singh, Partner (general corporate) at Shardul Amarchand Mangaldas & Co, claims that foreign players who enter the Indian market largely depend on auto dealers for market intelligence and knowledge, to provide a supply chain support and provision of aftermarket service. Both the parties can have equal negotiating

power. "However, any legislative governance in this regard may curb this freedom and may even discourage foreign players to enter in the Indian market".

However, Gulati of FADA begs to differ, saying that franchisee protection laws are meant for compliance in case OEMs decide to shut down the business and not for starting one. "The regulation is for bringing some kind of responsibility for OEMs towards dealers and customers in case of closing down," continues Gulati.

The regulations, if introduced, will certainly have an impact on the OEM-dealer relationship. Maruti Suzuki India's RC Bhargava says: "I have no idea because I have not studied this matter at all."

So, the dice has been cast. Even as OEMs and dealers struggle to sell vehicles and mitigate the impact of the Covid-induced lack of demand, the issue of empowering franchisees with a legal act of law will continue to remain a vexing – and delicate – one. ■