

Choosing the Right Successor Requires Careful Planning

By Jonathan Samel, Esquire

If you should die or become incapacitated, who will take your place as the leader of your automobile dealership? Having an approved successor trained and ready to take over is one of the most important planning objectives you can accomplish.

While the specific provisions of each manufacturer's franchise agreement relating to succession differ, dealers are usually permitted during their lifetime to nominate a successor. Most agreements provide a process for placing a successor on the successor addendum.

The manufacturer will want to know who will be in charge. Lenders will want to know who will be responsible for the continued profitable operation of the dealership to help repay loans. Your managers and employees need to know who to turn to for leadership and guidance.

If you fail to name a successor during your lifetime, things can become much more complicated after your death or incapacity. Under these circumstances, your franchise agreement probably leaves the process for approving the successor up to the discretion of the manufacturer, and provides a limited time frame after death or incapacity for the designation of a new dealer. Your absence will be difficult enough for your family and your business without the challenge of having to quickly choose a competent successor and obtain the manufacturer's consent. The manufacturer may demand new facility

upgrades, the naming of a new general manager, CSI improvement targets, new networking capital requirements, and commitments to meet other demands that could ultimately cost large sums of money.

Many states have franchise laws addressing succession. These laws have often been developed because of past manufacturer abuses. For example, the Pennsylvania Board of Dealers Act provides that any dealer may appoint a successor in advance who is either a family member or who is an unrelated qualified manager who has been employed at the dealership for at least two years. The manufacturer cannot withhold its consent to such a successor without good cause.

You should work through the succession planning process with the help of your legal and financial advisors. This process should include a complete legal analysis of your state's franchise law, if there is one, as well as a careful review of the succession provisions contained in your manufacturer's franchise agreement.

Dealing with the franchise issues is just one element of succession planning which can be a complex process. We also often advise clients to participate in pre-succession training sessions to adequately prepare the family members involved with the dealership and its transition. The objectives of the training include: (1) increasing the level of self-awareness of all the parties involved in the process, with particular attention paid to identifying the strengths, weaknesses and

commitment level to the business of each participant; (2) providing an opportunity for each participant to define their personal purpose and objectives; (3) encouraging and challenging the active listening skills of each participant; (4) fostering an environment in which succession issues are addressed honestly, objectively and courageously; (5) creating an effective mechanism for conflict resolution; and (6) emphasizing objectivity in evaluating the proposed successor's leadership and management skills.

Please contact our office if you wish to discuss the succession provisions in your franchise agreement, state franchise laws relating to succession, pre-succession training or any other aspects of succession planning. ■

Does the New
3.8%
NET INVESTMENT
INCOME TAX
Apply to You?

By Andrew P. Grau, Esquire

Beginning in 2013, certain investment income is subject to an additional 3.8% federal income tax. You may be affected by this tax if you have annual gross income of over \$250,000 and you are married filing jointly, or over \$200,000 if you are a single taxpayer.

The 3.8% tax applies to net investment income (NII), which includes interest, dividends, rent, royalties, capital gains, and business income derived from "passive activities."

If you are an automobile dealer who regularly participates in the operations of

continued on other side

PENNSYLVANIA COURT RULES THAT CHRYSLER DEALER IS EXEMPT FROM PROTEST

By Andrew P. Grau, Esquire

If a manufacturer intends to establish a new dealership or to relocate an existing dealership within a market area where the same brand is already represented, Section 818.27 of the Pennsylvania Board of Dealers Act requires the manufacturer to provide advance notice of its intention to the State Board of Vehicle Manufacturers, Dealers and Salespersons and to each dealer of the same brand in that market area. Any such dealer then has the right to file a protest with the Board of the manufacturer's proposed action.

Section 818.27(b) of the Act provides that the right to protest does not apply if the proposed dealership is to be established within two miles of the location where a former dealership with the same brand had ceased operating within the previous two years.

In a recent ruling interpreting Section 818.27, the Pennsylvania Commonwealth Court ruled that a Chrysler dealership was exempt from protest because Chrysler



notified the Board of its intention to establish a new dealership within two years of the closing of a prior dealership located within two miles of the new dealership's location.

In this case, Barbera's Autoland filed a protest to the proposed opening of a new dealership in Jenkintown, Pennsylvania. The Bar-

bera dealership, located in Philadelphia about five miles from the proposed location of the new dealership, had been sold. The buyer of the Barbera dealership was not aware of Chrysler's intention of opening a new dealership in Jenkintown.

The Board of Vehicle Manufacturers, Dealers and Salespersons initially upheld the protest because the new dealership, Abington Auto World, had not filed its initial dealer license application or opened for business within two years of the closing of Faulkner, a prior Chrysler dealership which had been located within two miles of Abington Auto World.

However, on appeal, the Commonwealth Court disagreed with the Board and ruled that the opening of Abington Auto World was exempt from protest because Chrysler had notified the Board of its intent to establish a new dealership within two years of termination of the Faulkner dealership. According to the Court, the Board of Dealers Act does not assume that a manufacturer has already signed a franchise agreement prior to its notification of the Board or that the new dealership has been built and is opened for business, but rather the Act only speaks to the manufacturer's intent to enter into a franchise agreement at the time of the notice. ■

The New 3.8% Tax...

continued from page 1

your dealership, and the dealership operating company is a pass-through entity for tax purposes (S corporation, limited liability company or partnership), the shareholder or partnership distributions you receive from the operating company will not be NII because they come from an active trade or business. On the other hand, if your participation is limited or you are retired, ownership distributions may be NII if you fail to meet a material participation test based on criteria set by the IRS. If your dealership is a C corporation, the income received by the corporation is not subject to the 3.8% tax, but any shareholder dividends you receive will be classified as NII.

The 3.8% tax may also apply if you, directly or indirectly through an entity, own the real estate where your dealership is located and receive rent from the dealership operating company. Unless the IRS determines that you are a "real estate professional," the rent you receive could be treated as coming from a passive activity and classified as NII. Increasing your participation in the active management of the real estate, and making the lease a "gross" lease rather than "triple net" could help to avoid NII. However, this requires careful planning because changing your real estate ownership from a passive activity to an active business may trigger other taxes that could outweigh the advantage of lowering NII.

For 2013 and beyond, it is crucial for automobile dealers to review their projected income from all sources, analyze the possible effect of the new 3.8% tax, and engage in comprehensive strategic tax planning. Please contact our office if you have any questions or want to discuss your planning. ■

HRMM&L

HAMBURG, RUBIN, MULLIN,
MAXWELL & LUPIN, PC
ATTORNEYS AT LAW

Lansdale • Limerick
Harrisburg • Allentown, PA

Phone 215.661.0400 • www.HRMML.com

It's About the Result