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Tesla Unplugged:

Automobile Franchise Laws and the Threat to the Electric Vehicle Market

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ABSTRACT

Electric vehicles have captured the imagination of drivers seeking a high-tech answer to rising gas prices and environmental damage. As the electric-vehicle sector develops, however, manufacturers are confronting state laws that restrict sales from manufacturers to consumers and pose a significant barrier to market expansion. This Article provides the first broad discussion of how franchise laws differ, disaggregating the primary types of state laws and using Tesla's and Ford's experiences to analyze options for challenging direct-sale restrictions. It also includes the first analysis of Tesla's court victories in New York and Massachusetts. The discussion suggests electric-vehicle producers should focus on legislative lobbying in states with sweeping prohibitions on direct sales, while exploring judicial challenges in states with partial restrictions that only prevent manufacturers from competing against their own franchisees. Ultimately, this Article provides a framework for thinking about ways to challenge a looming impediment to development in the electric-vehicle sector.

TABLE OF CONTENTS

I. INTRODUCTION

Tesla Motors, Inc. ("Tesla") is widely considered an innovative manufacturer of electric cars. One of its less-publicized facets—but one with just as much potential to revolutionize the automobile industry—is its business model that exclusively relies on direct manufacturer-to-consumer sales. State franchise laws illegalize such sales in much of the United States, and dealers have sued to keep Tesla from selling in their jurisdictions. Tesla, however, contends that low-maintenance electric cars cannot profitably be sold through independent dealers, whose businesses largely depend on servicing.[1] Tesla has started to challenge restrictive franchise laws in courts and legislatures around the country. Whether Tesla will overturn the current automotive legal landscape is an open question, but one with the potential to benefit consumers while threatening the interests of independent automobile dealers.

In June 2013, North Carolina passed an amended franchise law that is representative of the legal obstacles Tesla faces in much of the country.[2] In states with laws like North

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[1] Terrence Henry, *Tesla Has Eyes for Texas, But Will the State Oblige?*, STATE IMPACT (Apr. 24, 2013, 10:30 AM), http://stateimpact.npr.org/texas/2013/04/24/tesla-has-eyes-for-texas-but-will-the-state-make-oblige; *see also* Galen Moore, *Can Car Dealers Survive Tesla and the Electric Vehicle?*, BOS. BUS. J. (July 23, 2013, 9:30 AM), http://www.bizjournals.com/boston/blog/startups/2013/07/tesla-world-takeover.html?page=all (noting that service and parts accounted for 41.4 percent of profits in 2012 at Penske Automotive Group, the second largest global operator of car dealerships, service and parts).

[2] Bruce Siceloff, *NC Legislators Drop Bid to Curb Tesla Sales*, NEWS & OBSERVER (June 25, 2013), http://www.newsobserver.com/2013/06/25/2989207/nc-legislators-drop-bid-to-curb.html.

Carolina's, which prohibit virtually all direct sales by manufacturers, legal challenges to overturn those laws have resoundingly failed.[3] What North Carolina's new law does not contain, however, says more than what it does. Tesla's successful lobbying to exclude the law's more odious proposed provisions, such as a term that would have outlawed online sales in the state, illustrates Tesla's potential to succeed when it focuses on persuading legislatures to abandon such initiatives.[4] Tesla faces a similar battle in Texas, where its franchise laws resemble North Carolina's.

In other jurisdictions, notably Massachusetts and New York, the legal landscape is very different. Their franchise laws take a fundamentally distinct form from those of other states, prohibiting manufacturers from operating company stores in addition to granting franchises.[5] Such laws are silent on producers like Tesla that exclusively sell directly to consumers. When unaffiliated dealers sued Tesla in Massachusetts and New York to enjoin its sales activities, state courts dismissed their claims for lack of standing.[6] Those courts held that the state franchise laws, designed to remedy disparities in bargaining power between manufacturers and their affiliated

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[3] *See, e.g.*, Ford Motor Co. v. Tex. Dep't of Transp., 264 F.3d 493 (5th Cir. 2001) (upholding a Texas ban).

[4] *See* David Noland, *Anti-Tesla Bill Backed By North Carolina Car Dealers Is Dead*, GREEN CAR REP. (June 27, 2013), http://www.greencarreports.com/news/1085059_anti-tesla-bill-backed-by-north-carolina-car-dealers-is-dead.

[5] *See* MASS. GEN. LAWS. ch. 93B, § 4(c)(10) (2012); N.Y. VEH. & TRAF. LAW § 415(7)(f) (McKinney 2012).

[6] *See* Mass. State Auto. Dealers Ass'n, Inc. v. Tesla Motors MA, Inc., No. NOCV201201691, 2012 WL 7985777, at *4-7 (Mass. Super. Ct. Nov. 9, 2012); *In re* Greater N.Y. Auto. Dealers Ass'n v. Dep't of Motor Vehicles, 969 N.Y.S.2d 721, 726–27 (Sup. Ct. 2013).

dealers, were never intended to be a tool for retailers to attack their legitimate competitors.[7]

This Article is the first scholarly analysis of how franchise laws encumber Tesla's business model, discussing how these laws differ by state and the resulting implications for challenging statutory restrictions on direct sales. It argues that Tesla should tailor its opposition strategy to match the breadth of the law at issue, focusing its resources on legislative lobbying in states like North Carolina and Texas, while concentrating on the judiciary in states like Massachusetts and New York. Part I begins by sketching the legal landscape, examining the two main types of state laws and summarizing relevant constraints in federal law. Part II orients this discussion by placing it within the scholarly context regarding policy implications of direct-sale restrictions. Part III explores prior court challenges to these laws, explaining why Ford failed in the Fifth Circuit, why Tesla succeeded in New York and Massachusetts, and the different ways Tesla might distinguish unfavorable precedent in future challenges. This Article concludes by identifying consequences for Tesla's options to challenge restrictive franchise laws going forward.

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[7] *See Mass. State Auto. Dealers*, 2012 WL 7985777, at *4-7; *Greater N.Y. Auto. Dealers*, 969 N.Y.S.2d at 727.

II. AUTOMOBILE FRANCHISE LAWS IN THE UNITED STATES

A. North Carolina and Texas: Prohibitions on All Direct Sales

Some state franchise laws, such as those of North Carolina and Texas, include sweeping prohibitions on automobile sales from producers to consumers.[8] These are the laws that Tesla's co-founder and CEO Elon Musk calls a "perversion of democracy."[9] They prohibit manufacturers like Tesla from selling cars in a physical store within the state but permit online or phone sales to customers.[10] While there are no traditional stores in such states, one can find Tesla "galleries" in Texas, Arizona, and Virginia.[11] At a Texas gallery, potential consumers are permitted to view Tesla models but cannot test-drive, purchase, or even be told the price of a Tesla.[12] North Carolina appears to be among the most restrictive states, keeping North Carolinians from catching even a glimpse of the Model S in a Tesla showroom.[13]

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[8] Mike Ramsey & Valerie Bauerlein, *Tesla Clashes with Car Dealers*, WALL ST. J., June 18, 2013, at B1; *see also* Derek E. Empie, Note, *The Dormant Internet: Are State Regulations of Motor Vehicle Sales by Manufacturers on the Information Superhighway Obstructing Interstate and Internet Commerce?*, 18 GA. ST. U. L. REV. 827, 849-51 n.153 (2002) (extensively detailing the statutory text of state franchise laws).
[9] Ramsey & Bauerlein, *supra* note 8, at B2.
[10] *Id.* at B1.
[11] *Id.*
[12] Henry, *supra* note 1.
[13] Ramsey & Bauerlein, *supra* note 8, at B1.

North Carolina restricts direct sales under the guise of protecting independent dealers from unfair competition.[14] As the statute provides, "[i]t is unlawful for any motor vehicle manufacturer . . . to directly or indirectly . . . own any ownership interest in, operate, or control any motor vehicle dealership in this State."[15] To be sure, there are limited exceptions that permit certain manufacturers to sell outside the independent dealer framework, including temporary operations, certain public-interest categories, and situations in which an independent dealer cannot be found to operate a franchise in the relevant market.[16]

When North Carolina passed an amended franchise law in June 2013, the only updates to its unfair-competition provisions related to warranty repairs, leaving the direct-sale restrictions the same.[17] The initial proposal, which unanimously passed the Republican-controlled state Senate,[18] would have prohibited online sales by amending the definition of dealers and altering licensing requirements.[19] Depending on

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[14] N.C. GEN. STAT. ANN. § 20-305.2 (West 2013) (carrying the heading, "Unfair methods of competition").
[15] *Id.* § 20-305.2(a).
[16] *Id.* § 20-305.2(a)(1)-(4).
[17] S.B. 717, 2013 N.C. Sess. Laws 11 (amending N.C. GEN STAT. ANN. § 20-305.2(e)-(f) (West 2013)).
[18] Ramsey & Bauerlein, *supra* note 8, at B1.
[19] S.B. 327, 2013 N.C. Sess. Laws 1 (proposing to amend N.C. GEN. STAT. ANN. § 20-286(11)(a) (West 2013) (altering the definition of "dealer" to include a person who engages in sales activities using "a computer or other communications facilities, hardware, or equipment at any location within this State . . . for the purpose of transmitting applications, contracts, or orders for motor vehicles purchased or leased by retail purchasers or lessees located in this State.")); *id.* (proposing to amend N.C. GEN. STAT. ANN. § 20-287(a) (West 2013) ("Any of these license holders who operates as a motor vehicle dealer, including a person who . . . uses [a] computer or other

how they would have been interpreted, the proposed provisions could have prevented Tesla from selling its product online, emailing potential customers, or responding to online questions from consumers in North Carolina.[20] The exclusion of those terms in the passed legislation signaled a defeat for proponents of tighter restrictions.

Texas franchise law similarly restricts direct sales.[21] Under the statute, "a manufacturer or distributor may not directly or indirectly: (1) own an interest in a franchised or nonfranchised dealer or dealership; (2) operate or control a franchised or nonfranchised dealer or dealership; or (3) act in the capacity of a franchised or nonfranchised dealer."[22] Limited exceptions are allowed for temporary operations, grandfathered sellers of used trucks or motor homes, and certain other narrow categories.[23] In general, however, the blanket prohibition on manufacturer sales prohibits Tesla and other producers from implementing a direct-to-consumer business model in Texas as in North Carolina.

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communications facilities, hardware, or equipment at any location within this State . . . for the purpose of transmitting applications, contracts, or orders for motor vehicles purchased or leased by retail purchasers or lessees located in this State, may sell motor vehicles at retail only at an established salesroom.")).

[20] John Voelcker, *North Carolina Wants to Make it Illegal for Tesla to E-Mail Customers*, GREEN CAR REPORTS (May 16, 2013), http://www.greencarreports.com/news/1084212_north-carolina-wants-to-make-it-illegal-for-tesla-to-e-mail-customers.

[21] *See* TEX. OCC. CODE ANN. § 2301.476 (West 2011).

[22] *Id.* § 2301.476(c)(1)-(3).

[23] *Id.* § 2301.476(d)-(k).

Tesla lobbyists hoped to roll back such prohibitions on a bill that was recently up for debate in the Texas legislature.[24] Tesla's proposal would have permitted electric car manufacturers to sell a limited number of vehicles directly to consumers in Texas,[25] which would have allowed Tesla to take orders at company-owned galleries.[26] The bill died without action, however, and cannot be reintroduced until 2015.[27] As a result, Texas consumers remain limited to ordering a Tesla online from California.[28]

B. New York and Massachusetts: Prohibitions on Some Direct Sales

Franchise laws commonly prohibit manufacturers from operating stores if they also sell through independent franchised dealers, with at least forty-eight states prohibiting such conduct.[29] Their purpose is to protect dealers in the event a franchisor licenses to them and subsequently opens a retail outlet in direct competition.[30] This type of franchise law covers only franchisors and franchisees, rather than all manufacturers and dealers, as in North Carolina and Texas.

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[24] *See* H.B. 3351, 83d Leg. (Tex. 2013) (proposing to allow electric vehicle companies to own their own dealerships in Texas); S.B. 1659, 83d Leg. (Tex. 2013) (companion Senate bill).
[25] *See* Tex. H.B. 3351; Tex. S.B. 1659.
[26] *See* Ramsey & Bauerlein, *supra* note 8, at B2.
[27] *Id.*
[28] *Id.*
[29] Amy Wilson, *Tesla's Musk: I'll Take the Store Fight Federal*, AUTOMOTIVE NEWS (Apr. 15, 2013, 12:01 AM), http://www.autonews.com/article/20130415/RETAIL07/304159943/-axzz2cArcDANP.
[30] Ramsey & Bauerlein, *supra* note 8, at B1.

New York's franchise law provides an example of this type of regulation. The Franchised Motor Vehicle Dealer Act grants affiliated franchisees a private right of action for franchisors' violations of the statute.[31] Franchisors are prohibited from operating as a new motor vehicle dealer,[32] with "franchisor" defined as "any manufacturer [or] distributor . . . which enters into or is presently a party to a franchise with a franchised motor vehicle dealer."[33] The Act further prohibits franchisors from "directly or indirectly coerc[ing] or attempt[ing] to coerce any franchised motor vehicle dealer" "to acquire any interest in any additional motor vehicle dealer in this state," with the exception of limited circumstances.[34]

Similarly, Massachusetts's franchise law covers only franchisors and their affiliated franchisees. In the interest of prohibiting unfair competition, the statute provides that it is a violation for a "manufacturer, distributor or franchisor representative . . . to own or operate, either directly or indirectly . . . a motor vehicle dealership located in the commonwealth of the same line make as any of the vehicles manufactured, assembled or distributed by the manufacturer or distributor."[35] While this language may appear to establish a blanket prohibition on direct sales, the term "of the same line make" has been interpreted to require an affiliated relationship, creating a private right of action only in the event of a dispute

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[31] N.Y. VEH. & TRAF. LAW § 469(1) (McKinney 2012).
[32] *Id.* § 415(7)(f) ("The commissioner shall not issue any certificate of registration authorized by this section to any franchisor . . . except that the commissioner may renew such certificate previously issued . . . prior to May second, two thousand two.").
[33] *Id.* § 462(8).
[34] *Id.* § 463(1), (2)(bb).
[35] MASS. GEN. LAWS. ch. 93B, § 4(c)(10) (2012); *id.* § 3(a) (creating a violation for unfair competition).

between affiliated franchisees and manufacturers.[36] Part III discusses this interpretation in greater depth.

Recently, dealers have attempted to strengthen franchise laws in New York and Massachusetts in order to block direct sales from manufacturers like Tesla. The proposed bill in New York would prohibit all manufacturers from operating dealerships, as in North Carolina and Texas.[37] The State Assembly adjourned in June 2013, however, without passing the bill and could not reconsider it until reconvening in January 2014.[38] In Massachusetts, Tesla and the Massachusetts State Automobile Dealers Association ("MSADA") are supporting competing bills to clarify the state's policy on direct sales.[39] Tesla's favored bill would explicitly permit a manufacturer to own dealerships if it does not also sell through independent franchisees, while the dealers' bill would prohibit all manufacturers from selling directly to consumers.[40] The

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[36] Mass. State Auto. Dealers Ass'n, Inc. v. Tesla Motors MA, Inc., No. NOCV201201691, 2012 WL 7985774, at *6 (Mass. Super. Ct. Dec. 31, 2012) (denying reconsideration).

[37] *New York Lawmakers Set Aside Dealer Bill Fought by Tesla*, AUTOMOTIVE NEWS (June 21, 2013, 4:08 PM), http://www.autonews.com/apps/pbcs.dll/article?AID=/20130621/OEM/130629962/new-york-lawmakers-set-aside-dealer-bill-fought-by-tesla-axzz2cArcDANP.

[38] *Id.*

[39] *See* H.B. 241, 2013-14 Leg., 188th Gen. Ct. (Mass. 2013) (supported by Tesla); S.B. 129, 2013-14 Leg., 188th Gen. Ct. (Mass. 2013) (supported by the Massachusetts State Automobile Dealers Association); *see also* Amy Wilson, *Tesla Plays Hardball*, AUTOMOTIVE NEWS (Mar. 18, 2013, 12:01 AM), http://www.autonews.com/article/20130318/RETAIL07/303189964/tesla-plays-hardball - axzz2cArcDANP.

[40] Michelle Jones, *Tesla Motors Inc. (TSLA) Lobbies for Direct Sales in Massachusetts*, VALUE WALK (June 7, 2013, 10:02 AM),

legislation is pending and open for consideration before the current session adjourns in July 2014.[41]

C. Federal Franchise Regulations

Federal franchise law does not pose an independent barrier to manufacturers seeking to sell automobiles directly to consumers. The Federal Automobile Dealer Franchise Act of 1956 ("Act")[42] grants dealers a private right of action in federal court against automobile manufacturers for violations of franchise agreements.[43] As it provides,

> An automobile dealer may bring suit against any automobile manufacturer engaged in commerce, in any district court of the United States in the district in which said manufacturer resides . . . by reason of the failure of said automobile manufacturer . . . to act in good faith in performing or complying with any of the terms or provisions of the franchise, or in terminating, canceling, or not renewing the franchise with said dealer.[44]

Where in conflict with state law, however, the Act provides that it "shall not invalidate any provision of the laws

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http://www.valuewalk.com/2013/06/tesla-motors-inc-tsla-lobbies-for-direct-sales-in-massachusetts.

[41] Wilson, *supra* note 39.

[42] 15 U.S.C. § 1221 (2012) [hereinafter *Franchise Act*].

[43] Gerald R. Bodisch, *Economic Effects of State Bans on Direct Manufacturer Sales to Car Buyers* *7 n.20 (ECON. ANALYSIS GRP., COMPETITION ADVOCACY PAPER NO. EAG 09-1 CA, 2009), *available at* http://www.justice.gov/atr/public/eag/246374.htm.

[44] *Franchise Act* § 1222.

of any State except insofar as there is a direct conflict between an express provision of this chapter and an express provision of State law which can not be reconciled."[45]

These provisions suggest that federal franchise law generally does not create an independent hurdle to direct sales by manufacturers. The express terms of the Act create a private right of action for a dealer against a manufacturer for failing to comply with the terms of a franchise agreement. Unless that contract specifically precludes manufacturer sales, the Act does not appear to create a federal private right of action for what may otherwise be solely a violation of state law. This interpretation is further supported by the Act's presumption against federal preemption unless in express conflict with state law. Since the Act does not expressly prohibit direct sales, it does not appear to prevent enabling state legislation from being passed or preclude courts from interpreting state laws to allow such conduct.

Similarly, the Act would be further inapplicable to manufacturers that do not also contract with independent dealers. For Tesla and similar producers, there are no franchise agreements in existence, and consequently, no basis from which a dealer could bring a breach of contract claim under the Act. The Ninth Circuit has interpreted the Act accordingly, noting that "[i]t is obvious that the Act does not apply until a manufacturer–dealer relationship has been created."[46]

Just as the Act does not preclude state laws in favor of direct sales, there is nothing within the Act that would contradict a federal law if enacted to prevent states from

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[45] *Id.* § 1225.
[46] Stansifer v. Chrysler Motors Corp., 487 F.2d 59, 63 (9th Cir. 1973).

blocking such sales. The Act itself is silent on manufacturer sales, providing only a private right of action in the event a franchisor breaches its contract with a franchisee. A federal law permitting the direct sale of automobiles—or even just those with electric engines—that travel in interstate commerce will likely be well within Congress' regulatory power under the Commerce Clause.[47] At this point, such legislation is mere conjecture, but Tesla has suggested that continued difficulty in the state arena could drive it to increase lobbying at the federal level in support of such a law.[48]

III. POLICY IMPLICATIONS OF DIRECT-SALES PROHIBITIONS

A. Effects on Consumers

Proponents of restrictions on direct sales—primarily consisting of franchised new-vehicle dealers—typically highlight the need for dealerships that offer valuable services to consumers and manufacturers.[49] Dealers provide inventory maintenance, local marketing, and warranty repair services, which manufacturers rely on to create an attractive market for their vehicles.[50] Consumers depend on dealers for detailed product information, test-drive opportunities, repairs,

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[47] *See* Swift & Co. v. United States, 196 U.S. 375 (1905) (holding the Commerce Clause gives Congress the power to regulate goods that flow through the stream of interstate commerce).
[48] Wilson, *supra* note 29.
[49] John T. Delacourt, *New Cars and Old Laws: An Examination of Anticompetitive Regulatory Barriers to Internet Auto Sales*, 3 J.L. ECON. & POL'Y 155, 156-57 (2007).
[50] *Id.* at 157-58.

replacement parts, accessories, and financing.[51] Consumers also benefit from regulatory functions that dealers perform, including proper title conveyance, vehicle registration, accurate odometer disclosure, obtaining of license plates, and provision of safety information.[52] Dealers provide a wider social benefit as well, improving public safety and ensuring vehicles are safe to drive by checking fluid levels, brakes, transmission systems, and other operating functions.[53]

Recent polling data, however, suggests that consumers are interested in direct sales, both online and elsewhere.[54] The attraction undoubtedly stems, at least in part, from projected cost savings from removing the middleman from transactions.[55] Distribution accounts for an estimated thirty percent of average vehicle costs.[56] Projections suggest that direct sales would save consumers between $1,500 and $2,600 per vehicle—equaling between six to ten percent of the total price—attributable to "inventory, field support, sales commissions, advertising, and overhead" costs that dealers add

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[51] *Id.* at 158.
[52] *Id.* at 183-84.
[53] *Id.* at 183.
[54] *Id.* at 156 n.2 (citing a 2001 Consumer Federation of America poll in which seventy-eight percent of respondents indicated that "consumers should have the ability to purchase cars directly from manufacturers or third parties using the Internet," seventy-eight percent reporting that they oppose "laws that require all car sales to go through car dealerships," and only nineteen percent felt the other way).
[55] *See* Bodisch, *supra* note 43, at *5 (noting that while cost savings are important, almost half of surveyed new car buyers in the United States would rather buy directly from the manufacturer to avoid the bargaining process with dealers, "*even if it didn't save any money*" (emphasis in original)).
[56] *Id.* at *1.

to the final purchase price.[57] While some may wish to pay a premium for a dealer's value-added services, others may prefer to purchase those services elsewhere in the market, and some argue that open franchise laws would promote consumer choice and competition.[58]

B. Effects on Dealers

The central purpose of franchise laws is to protect dealers from unfair competition by manufacturers.[59] Opponents of online vehicle sales point to the dealers' sizeable investments in real estate, facilities, and inventory, as well as the manufacturers' greater market power, in support of upholding franchise laws.[60] The average dealer invests just over $1 million in facilities and holds about $5 million in inventory.[61] Franchise laws limit a manufacturer's ability to undercut its franchisees' prices,[62] reflecting a "widely circulated (but unsubstantiated) belief" that manufacturers would otherwise abuse their bargaining power to the detriment of the dealers.[63] Such possibilities, however, would be relevant

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[57] *See* Delacourt, *supra* note 49, at 179, 186; *see also* Bodisch, *supra* note 43, at *4 (breaking down cost savings and attributing thirty-seven percent of savings to improvements from matching supply with consumer demand, twenty-six percent to lower inventory, seventeen percent to fewer dealerships, seventeen percent to lower sales commissions, and two percent to lower shipping costs).
[58] Bodisch, *supra* note 43, at *4, *6.
[59] Empie, *supra* note 8, at 851; Delacourt, *supra* note 48, at 163.
[60] Delacourt, *supra* note 49, at 179.
[61] *Id.* at 163 n.29 (citation omitted).
[62] *Id.* at 167.
[63] Carla Wong McMillian, *What Will It Take to Get You in a New Car Today?: A Proposal for a New Federal Automobile Dealer Act*, 45 GONZ. L. REV. 67, 68 (2010).

only for manufacturers that sell vehicles both directly and through franchises. Tesla, on the other hand, is not in a position to undercut dealer prices, since it does not sell through franchises.

Some also suggest that direct sales would encourage free riding on dealers' value-added services, particularly if manufacturers sell through the Internet[64] or other venues that offer fewer services than traditional dealers do. For example, a consumer might test drive a vehicle at a dealership and then purchase it online from the manufacturer at a discount.[65] Free riding would undercut the financial viability of independent dealers and drive them out of business, thereby reducing consumer choice by eliminating a market player that once offered desirable services. As with issues over market power, however, free riding would only be a concern for manufacturers with both direct and franchise sales. A potential customer cannot test drive a Tesla at an independent retail outlet.

To the extent direct sales would increase competition in the automobile retail market, independent dealers would suffer the most direct harm from amending franchise laws to permit manufacturer sales. It is reasonable to assume such market entrants, like Tesla, would pose a competitive challenge to independent dealers. They avoid a layer of cost that is otherwise added to the supply chain and may be able to control operations in a more streamlined manner. Even if blanket prohibitions were simply amended to look more like franchise laws in New York and Massachusetts, increased competition should be expected from producers like Tesla that were

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[64] Delacourt, *supra* note 49, at 179-80.
[65] *Id.*

previously excluded from the market entirely, posing a competitive threat to manufacturers and dealers alike.

Tesla contends, however, that the market for electric cars is too small to threaten dealer interests if an exception was made to allow direct sales of electric cars only, as it proposed in Texas.[66] Tesla sells ten thousand automobiles annually, a small percentage of the fourteen to fifteen million new cars sold nationwide.[67] In Texas, more than a million automobiles are sold annually, of which about one thousand are Teslas.[68] That number is expected to increase only to between 1500 and 2000 annually if Tesla is permitted to sell directly in Texas—a number Tesla's founder and CEO, Elon Musk, describes as "tiny potatoes."[69] Similarly, there have been fewer than a hundred Tesla buyers in North Carolina as of June 2013.[70] Further, considering the broader implications of a generally open automobile market, an economist suggests that the dealers' concerns are overstated, highlighting the role of competition among manufacturers in reducing incentives for opportunistic behavior and encouraging cooperation with dealers to resolve free-riding issues.[71]

IV. COURT FAILURES AND SUCCESSES IN CHALLENGING DIRECT-SALE PROHIBITIONS

There is strong precedent upholding the type of franchise laws that exist in North Carolina and Texas. Laws

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[66] Henry, *supra* note 1.
[67] *Id.*
[68] *Id.*
[69] *Id.*
[70] Siceloff, *supra* note 2.
[71] Bodisch, *supra* note 43, at *6-7.

that generally prohibit all manufacturer sales impose an equal burden on in-state and out-of-state producers, and they pass scrutiny under the Commerce Clause, the Equal Protection Clause, the Due Process Clause, and the First Amendment. Fifth Circuit decisions, which upheld these laws, followed clear Supreme Court precedent, and any federal challenge would likely require reconsideration by the Court in order to succeed. In New York and Massachusetts, however, courts face franchise laws that only govern the relationship between franchisors and their franchisees. When unaffiliated dealers challenged Tesla in those states, their suits were dismissed for lack of standing, as they did not have the requisite relationship with Tesla to challenge its activities.[72]

This Part begins by examining Ford's court failures in federal district court and the Fifth Circuit, using those decisions to illustrate the constitutional issues of such laws and implications for Tesla's legal challenges in such states. It then analyzes Tesla's recent court victories in New York and Massachusetts. The primary lessons of these cases is that the judiciary is a promising outlet for Tesla in states with franchise laws that only govern relationships between franchisors and franchisees. Where the law is ambiguous, Tesla and others seeking to implement an exclusively direct-to-consumer model should frame legislation accordingly when bringing or responding to court challenges. The legislature, however, likely provides a more pragmatic venue to challenge prohibitions in states that outlaw all direct sales.

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[72] *See* Mass. State Auto. Dealers Ass'n, Inc. v. Tesla Motors MA, Inc., No. NOCV201201691, 2012 WL 7985777, at *4-7; *In re* Greater N.Y. Auto. Dealers Ass'n v. Dep't of Motor Vehicles, 969 N.Y.S.2d 721, 726–27 (Sup. Ct. 2013).

A. Bases for Court Failures in the Fifth Circuit

The first case to challenge state laws restricting direct-to-consumer sales, *Ford Motor Co. v. Texas Department of Transportation*, arose in the Western District of Texas.[73] The case dealt with the constitutionality of Texas restrictions on Ford Motor Co.'s online sales of used vehicles. Since May 1998, Ford operated a website that allowed customers to view available pre-owned vehicles, including a no-haggle price set by Ford, and have them shipped to a specific dealership for viewing and test driving.[74] Ford would transfer the vehicle to the dealership, which took title by assignment, and the dealer had the option to purchase it at wholesale or return it to Ford if the potential customer declined to buy it.[75] Dealership participation was voluntary, but dealers agreed to honor the no-haggle prices and not show customers other options until they rejected the vehicles sent by Ford.[76]

The Texas Department of Transportation filed an administrative complaint against Ford, contending its actions violated the Texas Motor Vehicle Commission Code ("Code").[77] The Code prohibited anyone from acting as a dealer without a license, particularly manufacturers like Ford, who are forbidden from obtaining a license.[78] Ford brought suit in the district court to challenge the basis of those

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[73] 106 F. Supp. 2d 905 (W.D. Tex. 2000).
[74] *Id.* at 907.
[75] *Id.*
[76] *Id.*
[77] *Id.*
[78] TEX. REV. CIV. STAT. ANN. art. 4413(36), § 4.01(a) (West 1999) (repealed 2003) (requiring dealers to be licensed); TEX. REV. CIV. STAT. ANN. art. 4413(36), § 5.02C(c) (West 1999) (repealed 2003) (prohibiting manufacturers from operating as a dealer).

administrative proceedings, arguing that restricting Ford's online sales violated the dormant Commerce Clause, the Equal Protection Clause, the Due Process Clause, and the First Amendment.[79] Ultimately, the court rejected each of Ford's arguments on summary judgment, and the Fifth Circuit affirmed on similar grounds.

If Tesla attempts to bring similar constitutional challenges to overturn blanket prohibitions on direct sales, it will face an uphill battle to distinguish the reasoning underlying *Ford*. It may succeed, however, as *Ford* is distinguishable from Tesla's situation. There, the district and circuit court upheld the Code in the context of a manufacturer simultaneously selling through franchises and company-owned stores. It did not challenge the franchise restrictions from the perspective of a manufacturer like Tesla, which does not contract with independent dealers. This difference between Tesla and Ford could be a decisive distinguishing factor in a future legal challenge, but such arguments may require revisiting existing Supreme Court precedent.

i. The Dormant Commerce Clause

Ford first challenged the Texas statute under the dormant Commerce Clause and contended that restrictions on Ford's sales unconstitutionally discriminated against out-of-state Internet sellers in favor of in-state franchised dealers, causing an undue burden on interstate commerce.[80] They also argued that the Texas policy did not further a legitimate state interest, since the information Ford provided online was not

[79] *Ford Motor*, 106 F. Supp. 2d at 908, 909.
[80] *Id.* at 908.

misleading or inaccurate, and there was no evidence that Ford competed against Texas dealers.[81]

The Fifth Circuit stated that the Commerce Clause, which grants Congress explicit power to regulate interstate commerce, "has long been understood to have a 'negative' aspect that denies the States the power unjustifiably to discriminate against or burden the interstate flow of articles of commerce."[82] Under the first of two prongs underlying dormant Commerce Clause jurisprudence, legislation is "virtually per se" unconstitutional if it discriminates against out-of-state producers, either facially, in purpose, or in effect.[83] Under the second tier, a nondiscriminatory law is unconstitutional if it unduly burdens interstate commerce,[84] triggering a lower standard of scrutiny under which courts employ the balancing test set forth in *Pike v. Bruce Church, Inc.*[85] Under this test, courts "will uphold a nondiscriminatory statute . . . 'unless the burden imposed on [interstate] commerce is clearly excessive in relation to the putative local benefits.'"[86] The *Pike* test is a rejection of the *Lochner* era,[87]

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[81] *Id.*

[82] Ford Motor Co. v. Tex. Dep't of Transp., 264 F.3d 493, 499 (5th Cir. 2001) (quoting Or. Waste Sys., Inc. v. Dep't of Envtl. Quality, 511 U.S. 93, 98 (1994)).

[83] *Or. Waste*, 511 U.S. at 100-01.

[84] *See* Hunt v. Wash. State Apple Adver. Comm'n, 432 U.S. 333, 348-54 (1977) (overturning a facially neutral restriction on the apple market for burdening and discriminating against interstate commerce); Pike v. Bruce Church, Inc., 397 U.S. 137, 142 (1970) (creating undue burden test).

[85] 397 U.S. at 142; *see* David S. Day, *The "Mature" Rehnquist Court and the Dormant Commerce Clause Doctrine: The Expanded Discrimination Tier*, 52 S.D. L. Rev. 1, 1 (2007) (discussing the two-tier doctrine).

[86] United Haulers Ass'n, Inc. v. Oneida-Herkimer Solid Waste Mgmt. Auth., 550 U.S. 330, 346 (2007) (citing *Pike*, 397 U.S. at 142).

representing a permissive approach to economic regulation under which courts refuse to "rigorously scrutinize economic legislation passed under the auspices of the police power."[88]

The district court upheld the Texas regulation against attack under both prongs of dormant Commerce Clause doctrine. While the court declined to provide a detailed rationale, it held that general prohibitions on direct sales did not amount to unconstitutional discrimination against out-of-state manufacturers and that Texas's regulatory scheme did not unduly burden interstate commerce.[89] The court recognized that Texas has a valid state interest in "equaliz[ing] the market power between manufacturers and dealers," and that in response, the Texas legislature enacted a statutory scheme based on valid legislative findings to pursue that goal.[90] Thus, the court rejected Ford's argument that its sales were protected by virtue of being conducted over the Internet, reasoning that the form of the sale was irrelevant for determining whether Ford's sales were appropriately regulated.[91]

On de novo review, the Fifth Circuit affirmed the dismissal of Ford's arguments under the dormant Commerce Clause, relying on controlling Supreme Court precedent.[92] In *Exxon Corp. v. Maryland*, the Court confronted a Maryland

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[87] For a discussion of the *Lochner* period and its role in modern jurisprudence, see Cass R. Sunstein, *Lochner's Legacy*, 87 COLUM. L. REV. 873 (1987).
[88] *United Haulers*, 550 U.S. at 347.
[89] Ford Motor Co. v. Tex. Dep't of Transp., 106 F. Supp. 2d 905, 909 (W.D. Tex. 2000).
[90] *Id.* at 908.
[91] *Id.* at 909.
[92] Ford Motor Co. v. Tex. Dep't of Transp., 264 F.3d 493, 500-01 (5th Cir. 2001) (citing Exxon Corp. v. Maryland, 437 U.S. 117 (1978)).

statute that forbade oil producers and refiners from operating retail gas stations.[93] Seven oil companies, three of which sold exclusively through company-owned gas stations, challenged the law's constitutionality under the dormant Commerce Clause and the Due Process Clause.[94] Like Ford, Exxon argued that the statute unduly burdened interstate commerce, contending that its effect was "to protect in-state independent dealers from out-of-state competition."[95] After finding the Maryland statute did not discriminate against out-of-state producers, the Court held that it also did not unduly burden interstate commerce, reasoning that "[s]ome refiners may choose to withdraw entirely from the Maryland market, but there is no reason to assume that their share of the entire supply will not be promptly replaced by other interstate refiners."[96] As the Court concluded, "interstate commerce is not subjected to an impermissible burden simply because an otherwise valid regulation causes some business to shift from one interstate supplier to another."[97]

The Fifth Circuit accordingly found the Texas statute nondiscriminatory, reasoning that it placed equal burdens on in-state and out-of-state manufacturers.[98] Subsequently applying the *Pike* balancing test, the court rejected Ford's arguments about economic consumer harm as irrelevant[99] and

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[93] *Exxon*, 437 U.S. at 119-20.
[94] *Id.* at 120-22.
[95] *Id.* at 125.
[96] *Id.* at 127.
[97] *Id.*
[98] Ford Motor Co. v. Tex. Dep't of Transp., 264 F.3d 493, 502 (5th Cir. 2001).
[99] *Id.* at 503 ("It may be true that the consuming public will be injured . . . but . . . that argument relates to the wisdom of the statute, not its burden on commerce.").

held that Ford failed to show that the statute excessively burdened interstate commerce or even decreased the number of out-of-state vehicles sold in Texas.[100] In doing so, the Fifth Circuit recognized legitimate state interests in "prevent[ing] vertically integrated companies from taking advantage of their incongruous market position" and "prevent[ing] frauds, unfair practices, discrimination, impositions, and other abuses of [Texas] citizens."[101] The court declined to "second guess the empirical judgment of lawmakers concerning the utility of legislation," finding sufficient evidence that Ford might have commanded a sufficiently powerful market position to justify the statute's asserted purpose.[102]

If Tesla brings a dormant Commerce Clause challenge, it will face the same hurdles that Ford confronted, especially the binding precedent in *Exxon*. While the Fifth Circuit rejected Ford's attempt to distinguish *Exxon* as an anomaly in response to the gas crisis, finding "no significant factual or legal distinction between *Exxon* and the instant case,"[103] Judge Jones noted, in concurrence, that it may be time for the Supreme Court to revisit its holding.[104] As she reasoned,

> Texas's outright prohibition on retail competition from out-of-state auto manufacturers is about as negative toward interstate commerce as legislative action can get. If, as the Court says, its negative commerce

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[100] *Id.*
[101] *Id.*; TEX. REV. CIV. STAT. ANN. art. 4413(36), § 5.02C(c) (West 1999) (repealed 2003) (internal quotation marks omitted).
[102] *Ford Motor*, 264 F.3d at 503-04 (citing CTS Corp. v. Dynamics Corp. of Am., 481 U.S. 69, 92 (1987) (internal quotation marks omitted)).
[103] *Id.* at 500-01.
[104] *Id.* at 512 (Jones, J., concurring).

> clause jurisprudence intends to prevent "economic protectionism" of local businesses, and to stop states from imposing higher (in this case prohibitive) costs on products from out-of-state sources, then Ford's . . . program ought not to be stymied by parochial state legislation.[105]

Concluding that the "Texas statute appears to reflect a genre of state laws favoring local automobile dealers over out-of-state manufacturers," she reflected that "perhaps the Supreme Court will give us further guidance."[106]

Even without seeking to overturn *Exxon*, Tesla might distinguish it on other grounds. In *Exxon*, the Court relied on the undifferentiated commodity nature of the gasoline market.[107] Even if consumers could no longer buy gasoline from certain producers, the Court reasoned, another producer will step in to fill the supply gap.[108] In essence, even if particular manufacturers were burdened or disadvantaged, the overall interstate market would not be, because one gallon of gasoline is the same as any other. Ford faced the same dynamic, as they offered automobiles that were similar to other manufacturers, and being limited to selling through independent dealers would not necessarily decrease the supply of Ford vehicles. In contrast, Tesla could argue that similar electric cars would otherwise be unavailable in states with such restrictions for two reasons: (1) other suppliers do not offer comparable products, and (2) electric cars generally cannot be

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[105] *Id.*
[106] *Id.*
[107] *See* Exxon Corp. v. Maryland, 437 U.S. 117 (1978).
[108] *Id.* at 127.

profitably sold through dealers.[109] In these ways, a Tesla is unlike gasoline or a Ford. Of course, Tesla would have to support its latter claim with hard data that dealerships present an economically unsustainable model for selling electric cars. This would allow Tesla to argue that such statutes burden the interstate market in all electric vehicles, rather than just disadvantage Tesla—something that Ford failed to argue—and move beyond the consumer-benefit arguments that courts have repeatedly reminded all parties are better addressed to legislatures.

ii. The Equal Protection Clause

Ford also challenged the Texas statute under the Equal Protection Clause, asserting there was no rational basis to differentiate dealers from manufacturers and that there was no rational basis to treat its website differently from a competitor's website.[110] In support of the first claim, Ford argued in the district court that there was no evidence the statute reduced the disproportionate market power of manufacturers.[111] For the second claim, Ford pointed out that its competitor, General Motors ("GM"), was permitted to contract with an independent company to operate its used vehicle website, GM Driversite, through which GM offered similar "no haggle" prices and services.[112] Simply by contracting with a website operator, GM successfully brought its operations within the limits of Texas franchise law.

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[109] Henry, *supra* note 1.
[110] *Ford Motor*, 264 F.3d at 510.
[111] Ford Motor Co. v. Tex. Dep't of Transp., 106 F. Supp. 2d 905, 909 (W.D. Tex. 2000).
[112] *Id.*

For an economic regulation to survive an equal protection challenge, the state must show that there is a rational basis to treat similarly situated individuals differently.[113] There must be a reasonable connection between a legitimate or conceivable state interest and the policy at hand, but this highly deferential standard of review permits legislatures to implement under-inclusive policies to address public issues one step at a time. As the Supreme Court noted more than sixty years ago, "[i]t is no requirement of equal protection that all evils of the same genus be eradicated or none at all."[114]

The district court dismissed Ford's equal protection argument by finding a rational basis for the Texas regulations. First, the court recognized a legitimate state interest in "ameliorat[ing] the disparity in power between manufacturers and dealers."[115] It found a reasonable relationship between that interest and the Texas policy forbidding direct sales, reasoning that "[m]anufacturers have more power, not merely because they are large companies . . . but because they control a dealer's supply of vehicles."[116] Similarly, it was permissible for the state to treat Ford's online activities differently from GM's, because an independent company operated GM Driversite in accordance with statutory requirements.[117] The Fifth Circuit rejected Ford's equal protection challenge on the same grounds, finding a rational basis for the statute based on the same reasoning contained in its dormant Commerce Clause analysis—to prevent manufacturers from enjoying disproportionate market power and avert fraud, among

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[113] *See* Ry. Express Agency, Inc. v. New York, 336 U.S. 106, 110 (1949).
[114] *See id.*
[115] *Ford Motor*, 106 F. Supp. 2d at 910.
[116] *Id.*
[117] *Id.*

others—and dismissed the idea that Ford and GM were "mirror images" but received differential treatment under the law.[118]

If Tesla mounts an equal protection challenge, it might successfully distinguish *Ford* on rational basis grounds. The Fifth Circuit recognized a legitimate state interest in diminishing the market-power disparity between dealers and manufacturers, on the basis that manufacturers control a dealer's supply of vehicles.[119] If Tesla is not in a position to restrict supply because that supply line does not exist, it could argue there is no rational connection between the state's asserted interest and the restriction on its sales. Unlike Ford, which was competing with its own dealers, Tesla is not in a position to threaten the state's interest in managing the power imbalance between manufacturers and affiliated dealers. While the Supreme Court found a reasonable connection between the law and its purpose in *Exxon*, it did not squarely address the reasoning behind that connection, even though it upheld the law as applied to manufacturers that sold exclusively through company-owned gas stations.[120]

iii. The Due Process Clause

Ford next asserted the statute was unconstitutionally vague in violation of substantive due process.[121] To survive a vagueness challenge, a law must "give the person of ordinary intelligence a reasonable opportunity to know what is

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[118] Ford Motor Co. v. Tex. Dep't of Transp., 264 F.3d 493, 510-11 (5th Cir. 2001).
[119] *Ford Motor*, 106 F. Supp. 2d at 910.
[120] Exxon Corp. v. Maryland, 437 U.S. 117, 124-25 (1978).
[121] *Ford Motor*, 106 F. Supp. 2d at 910 (citing Vill. of Hoffman Estates v. Flipside, Hoffman Estates, Inc., 455 U.S. 489 (1982)).

prohibited, so that he may act accordingly."[122] While the district court recognized that the Texas statute lacked full clarity by failing to define the activities it prevented, it ruled that Ford nevertheless should have reasonably known that its activities would constitute a violation.[123] The Fifth Circuit affirmed the district court's findings, holding that Ford's vagueness challenge failed because it was clear what conduct the statute prohibited.[124]

Ford did not raise the substantive due process argument that the Texas regulation violated its economic liberty. Had it done so, however, *Exxon* would likely have foreclosed that position as well. Faced with a statute that precluded oil producers from operating retail outlets, whether or not they also sold through franchised dealers, the Supreme Court upheld the law against a substantive due process attack. The Court dismissed the challenge in a single paragraph, noting that "it is, by now, absolutely clear that the Due Process Clause does not empower the judiciary 'to sit as a superlegislature to weigh the wisdom of legislation.'"[125] While the Court did not directly address the rational connection of the law to producers that exclusively sold through company-owned gas stations, it observed that the legislature was "[r]esponding to evidence that producers and refiners were favoring company-owned stations

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[122] Grayned v. City of Rockford, 408 U.S. 104, 108 (1972).
[123] *Ford Motor*, 106 F. Supp. 2d at 911 ("[T]he Court finds that Ford, by setting the price, accepting a refundable deposit from the consumer on the vehicle, and holding title to the vehicle until the consumer has accepted the price set by Ford, should reasonably have known that its conduct in operating the [s]howroom would implicate the provisions of § 5.02C(c).").
[124] Ford Motor Co. v. Tex. Dep't of Transp., 264 F.3d 493, 510 (5th Cir. 2001).
[125] *Exxon*, 437 U.S. 117 at 124 (citing Ferguson v. Skrupa, 372 U.S. 726, 731 (1963) (internal quotation marks omitted)).

in the allocation of gasoline and that this would eventually decrease the competitiveness of the retail market."[126] The Court, therefore, held that the statute "bears a reasonable relation to the State's legitimate purpose in controlling the gasoline retail market."[127] Accordingly, a substantive due process challenge by Tesla would likely fail as well, unless the Court revisits its holding in *Exxon*.

iv. The First Amendment

Ford brought its fourth and final constitutional challenge on First Amendment grounds, arguing the statute improperly suppressed its legitimate commercial speech.[128] Ford characterized the speech contained in its website as lawful, arguing that it simply "propose[d] a commercial transaction" and did not disperse "misleading or inaccurate" content.[129] Ford argued that even if Texas had a substantial interest in preventing manufacturers from competing against dealers, it did not have one in blocking Ford's website because Ford did not compete with dealers through its website.[130]

In *Central Hudson Gas & Electric Corp. v. Public Service Commission*, the Supreme Court created a four-part test to evaluate the constitutionality of restrictions on commercial speech.[131] First, courts must consider whether the speech at issue falls within the ambit of the First Amendment, which protects commercial speech only if it pertains to lawful activity

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[126] *Id.*
[127] *Id.* at 125.
[128] *Ford Motor*, 106 F. Supp. 2d at 911.
[129] *Id.*
[130] *Id.* at 911-12.
[131] 447 U.S. 557, 566 (1980).

and is not deceptive.[132] If the speech is protected, the court then identifies whether there is a substantial governmental interest being asserted, requiring that there be a "real" non-speculative harm that the restriction would materially alleviate.[133] If the first two prongs are satisfied, the court must further "determine whether the regulation directly advances the governmental interest asserted, and whether it is not more extensive than is necessary to serve that interest."[134]

The district court dismissed Ford's First Amendment argument on two grounds. First, because Ford's speech concerned unlawful activity—a manufacturer acting as a dealer, in violation of a constitutionally valid Texas law—the state was permitted to restrict it.[135] Second, the court held that even if Ford's speech were found lawful, satisfying the first *Central Hudson* factor, the restriction would be upheld under the other three.[136] Texas's interest in remedying the power imbalance between manufacturers and dealers constituted a substantial interest, with unfair competition as the "concrete, nonspeculative harm."[137] In other words, the court found that the prohibitions were narrowly tailored to directly advance that interest by excluding manufacturers from the retail market and ultimately rejected Ford's argument that it did not compete with dealers, since its activities affected what prices the dealers can set for similar vehicles.[138]

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[132] *Id.*
[133] Edenfield v. Fane, 507 U.S. 761, 770-71 (1993).
[134] *Cent. Hudson*, 447 U.S. at 566.
[135] *Ford Motor*, 106 F. Supp. 2d at 912.
[136] *Id.*
[137] *Id.*
[138] *Id.* at 913.

The Fifth Circuit affirmed the district court's dismissal under the first *Central Hudson* factor, holding that Ford's commercial speech concerned unlawful activity and that any restriction was incidental to Texas's valid prohibition on manufacturer sales.[139] Ford had argued before the Fifth Circuit that its commercial speech would be unlawful under *Central Hudson* only if a valid statute other than the one challenged prohibited it.[140] The court identified controlling precedent, however, in which the Supreme Court rejected similar arguments to uphold a picketing injunction against a First Amendment challenge.[141] As in that case, Ford's speech was "part of an integrated course of conduct" that violated valid state law, and Ford did not render its conduct permissible simply by incorporating an element of speech.[142] Accordingly, unless Tesla can show that the restrictive statutes are invalid on other grounds, the First Amendment would not independently protect its sales activities that incorporate an element of commercial speech. Such speech concerning unlawful behavior would similarly fail the first prong of the *Central Hudson* test.

B. Bases for Court Successes in New York and Massachusetts

Associations of automobile dealers recently brought suits in New York and Massachusetts to prevent Tesla from

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[139] Ford Motor Co. v. Tex. Dep't of Transp., 264 F.3d 493, 507 (5th Cir. 2001).
[140] *Id.* at 505-06.
[141] *Id.* at 506-07 (citing Giboney v. Empire Storage & Ice Co., 336 U.S. 490 (1949) (holding that where speech is integral to conduct prohibited by a constitutionally valid statute, an abridgment of such speech does not violate the First Amendment)).
[142] *Id.* at 507.

operating retail outlets in their states. In both cases, the state trial courts dismissed the dealers' suits for lack of standing, holding that state franchise laws solely governed the relationship between franchisors and their franchisees.[143] Unaffiliated dealers—lacking any contractual relationship to Tesla—had not suffered the requisite injury under the statute to challenge Tesla's activities.[144] The courts' willingness to dismiss such suits provides a roadmap for Tesla in other jurisdictions, particularly following the case of Massachusetts,[145] where the statutory text[146] presented interpretative ambiguity allowing the court to go either way. In such states, Tesla's ability to frame legislation as protecting only affiliated dealer–manufacturer relationships will be a decisive factor in reaching favorable judicial outcomes.

i. New York

In 2012, Tesla Motors New York LLC ("Tesla-NY") registered with the Department of Motor Vehicles in New York to operate two stores as a dealer in White Plains and Garden City, New York.[147] Less than three months later, the Greater New York Automobile Dealers Association ("GNYADA") and Brian Miller, an automobile dealership owner, brought suit against the DMV, Tesla, and Tesla-NY.[148] They sought to

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[143] *See* Mass. State Auto. Dealers Ass'n, Inc. v. Tesla Motors MA, Inc., No. NOCV201201691, 2012 WL 7985777, at *4-7 (Mass. Super. Ct. Nov. 9, 2012); *In re* Greater N.Y. Auto. Dealers Ass'n v. Dep't of Motor Vehicles, 969 N.Y.S.2d 721, 726–27 (Sup. Ct. 2013).
[144] *See Mass. State Auto. Dealers*, 2012 WL 7985777, at *4-7; *Greater N.Y. Auto. Dealers*, 969 N.Y.S.2d at 726–27.
[145] *Mass. State Auto. Dealers*, 2012 WL 7985777.
[146] MASS. GEN. LAWS ch. 93B, § 15(a) (2012).
[147] *Greater N.Y. Auto. Dealers*, 969 N.Y.S.2d at 723-24.
[148] *Id.* at 724.

revoke Tesla-NY's new dealership registrations, claiming that Tesla-NY was simultaneously a franchisee of Tesla and owned by Tesla, in violation of two New York statutes prohibiting franchisors from owning new-vehicle dealerships.[149]

Tesla moved to dismiss the suit for lack of standing.[150] In order to bring suit, a plaintiff must have standing to raise a claim, which requires a showing of "an actual legal stake in [the] outcome and an injury in fact worthy and capable of judicial resolution."[151] To bring a claim against a governmental body like the DMV, the plaintiff's injury must be distinct from that suffered by the general public.[152] In the case of an association bringing suit, it must show that at least one member has standing—requiring a showing of injury in fact and that the injury falls within the zone of interests protected by the statute in question—as well as that the association is representative of the asserted organizational purpose and that participation by individual members would not be required.[153]

The trial court embraced Tesla's view of New York's franchise law. Setting the tone for its opinion, the court began with the somewhat hostile announcement that "[m]anufacturers and dealers cannot utilize the Franchised Dealer Act as a means

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[149] *Id.* at 723-24; *see* N.Y. VEH. & TRAF. LAW §§ 415(7)(f), 463(2)(bb) (McKinney 2009).
[150] *Greater N.Y. Auto. Dealers*, 969 N.Y.S.2d at 724 (citing Mahoney v. Pataki, 772 N.E.2d 1118, 1122 (N.Y. 2002)).
[151] *Id.* at 726 (citing Mittelmark v. Cnty. of Saratoga, 925 N.Y.S.2d 235, 236 (App. Div. 2011)).
[152] *Id.* (citing *In re* Transactive Corp. v. N.Y. State Dep't of Soc. Servs., 706 N.E.2d 1180, 1183 (N.Y. 1998)).
[153] *Id.* (citing N.Y. State Ass'n of Nurse Anesthetists v. Novello, 810 N.E.2d 405, 407 (N.Y. 2004)).

to sue their competitors."[154] The court unequivocally held that "there must be a franchise relationship between the franchisor and the franchisee" in order to bring suit.[155] GNYADA and Miller, lacking any franchise relationship to Tesla, did not have standing to challenge Tesla's operation of its dealerships.[156]

In support of its holding, the court dismissed the notion that GNYADA or Miller met any of the standing requirements to bring suit. First, the court held that they did not show any special injury different from the public at large, as required to sustain a claim against the DMV.[157] Indeed, their only asserted injury was "an increase in business competition which, considered alone, is insufficient to confer standing."[158] This injury was not, as the court reasoned, within the "zone of interest" that the statute was designed to protect.[159] Consequently, the court placed Tesla outside the reach of New York franchise law—lacking any franchisees, Tesla had not created the type of contractual relationship that would give any entity standing to sue under the statute.

ii. Massachusetts

A similar case arose over Tesla's operation of a gallery and its application for a license to sell vehicles in Natick,

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[154] *Id.*
[155] *Id.*
[156] *Id.* at 726-27.
[157] *Id.* at 727.
[158] *Id.* (citing *In re* Sun-Brite Car Wash, Inc. v. Bd. of Zoning & Appeals, 508 N.E.2d 130, 134 (N.Y. 1987)).
[159] *Id.* (citing *In re* Lasalle Ambulance Inc. v. N.Y. State Dep't of Health, 665 N.Y.S.2d 747, 748 (App. Div. 1997)).

Massachusetts.[160] At its gallery, potential customers could view a Tesla, use interactive displays, purchase Tesla apparel, and discuss vehicle attributes with employees of Tesla-MA.[161] At the time of suit, Tesla had applied for a license to sell automobiles at its Natick gallery but had not yet received one or sold any vehicles through its gallery.[162] The Massachusetts State Automobile Dealers Association, Inc. ("MSADA") and several individual dealers brought suit against Tesla, contending that Tesla was acting as a dealer by advertising automobiles at its gallery, even though customers could not make in-store purchases.[163] The dealers sought a temporary restraining order and a preliminary injunction to prevent Tesla from doing anything beyond displaying a locked automobile in an unstaffed showroom.[164]

While the New York court faced a different standard of review than the Massachusetts court did, with the latter facing a balancing test that presumptively cuts against the issuance of a preliminary injunction, both cases were dismissed on the same grounds due to a lack of standing.[165] Notably, the

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[160] Mass. State Auto. Dealers Ass'n, Inc. v. Tesla Motors MA, Inc., No. NOCV201201691, 2012 WL 7985777, at *2 (Mass. Super. Ct. Nov. 9, 2012).
[161] *Id.*
[162] *Id.*
[163] Complaint at 3, 6, 8, 9, Mass. State Auto. Dealers Ass'n, Inc. v. Tesla Motors MA, Inc., No. NOCV201201691, 2012 WL 8006605 (Mass. Super. Ct. Oct. 16, 2012).
[164] *Id.* at 16-17.
[165] The procedural posture of the two cases differed, as the New York court granted a motion to dismiss brought by Tesla, while the Massachusetts court denied the dealers' motion for a preliminary injunction. *Compare Mass. State Auto. Dealers*, 2012 WL 7985777, at *3 (holding that dealer–plaintiffs lacked standing because they lacked a relationship with Tesla outside of being business competitors, after balancing "the risk of

Massachusetts court did not even engage in the three-part balancing test used to weigh the equities of a preliminary injunction, moving immediately to the question of standing.[166] As an initial matter, the court found that MSADA and one of the individually named plaintiffs lacked standing, noting that the statute grants a private right of action only to a "manufacturer, distributor or motor vehicle dealer" who suffers the requisite harm.[167] As for the remaining plaintiffs, all of whom were motor vehicle dealers, the court denied them standing because they were unaffiliated with Tesla.[168]

The court began its analysis with the interpretive history of Massachusetts's franchise law. Prior to a 2002 revision of the law, the Massachusetts Supreme Judicial Court in *Beard Motors, Inc. v. Toyota Motor Distributors, Inc.* held the statute did not confer standing on an automobile dealer that was unaffiliated with a defendant distributor.[169] *Beard Motors* identified the legislative purpose behind the law, which was a desire to protect franchisees and dealers from harm derived from "the inequality of their bargaining power and that of their *affiliated manufacturers and distributors*[.]"[170] Dealers consequently lacked standing to sue an unaffiliated

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[irreparable] harm in light of the party's chance of success on the merits"), *with* Greater N.Y. Auto. Dealers Ass'n v. Dep't of Motor Vehicles, 969 N.Y.S.2d 721, 726–27 (Sup. Ct. 2013) (holding that under New York law, dealer–plaintiffs only have standing to sue manufacturers with whom they have a working relationship, a question evaluated on the merits under Tesla's motion to dismiss).

[166] *See Mass. State Auto. Dealers*, 2012 WL 7985777.

[167] *Id.* at *4 (citing MASS. GEN. LAWS. ch. 93B, § 15(a) (2012)) (internal quotation marks omitted).

[168] *Id.* at *4-7.

[169] 480 N.E.2d 303, 306-07 (Mass. 1985).

[170] *Id.* at 306 (emphasis added).

manufacturer, because any harm was not "within the area of legislative concern."[171]

The court next rejected the idea that the 2002 revisions changed the statute's limited standing provisions. While the court acknowledged that the law's plain language suggested an expansion of standing based on the textual change from "[a]ny franchisee or motor vehicle dealer" to "[a]ny manufacturer, distributor or motor vehicle dealer," it rejected the idea that the language in the statute conferred standing on unaffiliated parties.[172] As in *Beard Motors*, the court primarily relied on the purpose behind the law, finding injuries by unaffiliated dealers to be outside the zone of protected interests.[173] The court noted that judicial decisions after 2002 did not suggest a different analysis.[174] In 2008, the First Circuit also relied on *Beard Motors* for its analysis of the statutory purpose behind Massachusetts's franchise law and found that no Massachusetts appellate court has suggested that the 2002 amendments altered that purpose.[175]

It appears that a motivating factor behind the court's decision was the belief that allowing unaffiliated dealers to use franchise laws in this way would harm the public by stifling competition in the automobile market. The court concluded its opinion by noting that a purpose behind Massachusetts's

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[171] *Id.* at 306–07.
[172] *Mass. State Auto. Dealers*, 2012 WL 7985777, at *5-6 (citing MASS. GEN. LAWS ch. 93B, § 12(A) (2001) (repealed 2002) and MASS. GEN. LAWS ch. 93B, § 15(a) (2012)).
[173] *Id.* at *4-7 (citing *Beard Motors*, 480 N.E.2d at 306-07).
[174] *Id.* at *5.
[175] Wagner & Wagner Auto Sales, Inc. v. Land Rover North Am., Inc., 547 F.3d 38, 42 (1st Cir. 2008).

franchise law is to benefit the public.[176] It warned that the dealers' interests are "frequently at odds" with those of the public, with the latter generally benefiting from increased competition.[177] As the Massachusetts Supreme Judicial Court held, the franchise law "was not intended to provide all dealers with a statutory right to seek protection from potential competition."[178] In future cases, Tesla can, and should, argue that its interpretation of franchise law benefits the public interest, which is discussed in detail in Part II. Tesla should remember, however, that it won in Massachusetts because the court viewed Tesla's position as aligned with the intent of its legislature, not simply or necessarily because the court itself believed Tesla's was the most efficacious policy.

V. CONCLUSION

Tesla's court victories in Massachusetts and New York suggest that it should look closely at which states prohibit all direct sales, as opposed to those that only forbid manufacturers from competing against their own dealers. In the latter, the judiciary has been receptive to the argument that Tesla should be permitted to sell directly to consumers. Tesla is unlikely to be successful, however, in states with laws like North Carolina's or Texas's, where there are strong precedent upholding blanket prohibitions on direct sales by manufacturers. While there may be some room for Tesla to distinguish unfavorable case law, constitutional challenges based on the dormant Commerce Clause, the Equal Protection

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[176] *Mass. State Auto. Dealers*, 2012 WL 7985777, at *6-7 (citing Am. Honda Motor Co. v. Bernardi's, Inc., 735 N.E.2d 348, 354 (Mass. 2000)).
[177] *Id.* (citing *Am. Honda*, 735 N.E.2d at 354 (internal quotation marks omitted)).
[178] *Am. Honda*, 735 N.E.2d at 356.

Clause, the Due Process Clause, or the First Amendment are unlikely to succeed without the Supreme Court revisiting its holding in *Exxon*.

Even if Tesla is unable to overcome state laws through judicial challenges in the most restrictive states, its legislative lobbying strategy is promising. Tesla has been offering test drives of its Model S outside legislatures around the country, giving state representatives the chance to experience a Tesla firsthand. North Carolina House Speaker Thom Tillis and Governor Pat McCroy were among those given test drives,[179] which may have contributed to the exclusion of proposed changes to North Carolina's law that would have illegalized online sales.[180] It is no coincidence that two Massachusetts state legislators took a spin as well, one of whom introduced the pending pro-Tesla legislation to allow direct sales.[181] Such firsthand experience may also account for the willingness of legislators to introduce such a bill in Texas, where the bill's author noted during a hearing, "I'd like to say I've driven one of these cars and it was awesome."[182]

As Tesla pursues its legislative strategy, it would be wise to remember that the dealers' arguments likely resonate deeply with lawmakers around the country. During a legislative hearing on the issue, the President of the North Carolina Automobile Dealers Association illustrated the political obstacles a small electric car company faces when confronting a vast network of dealers by stating: "You tell me they're

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[179] Siceloff, *supra* note 2.
[180] *Id.*
[181] Jones, *supra* note 40.
[182] Henry, *supra* note 1 (quoting State Representative Eddie Rodriguez).

gonna support the little leagues and the YMCA?"[183] His comment points to the political clout that automobile dealers often have in local communities. Dealers' wide geographic coverage and their position as an American icon carry power in terms of votes and message, factors often seen as decisive in legislative decision-making.[184] Whether Tesla will shake up franchise laws in states like North Carolina and Texas will depend on its ability to maneuver a difficult political landscape. Enticing legislators with Model S test drives, however, appears to have been a good start.

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[183] Will Oremus, *North Carolina May Ban Tesla Sales to Prevent "Unfair Competition,"* SLATE (May 13, 2013, 6:55 PM), http://www.slate.com/blogs/future_tense/2013/05/13/north_carolina_tesla_ban_bill_would_prevent_unfair_competition_with_car.html.

[184] *See* DAVID P. BARON, BUSINESS AND ITS ENVIRONMENT 165 (4th ed. 2003); *see also* Steven P. Croley, *Theories of Regulation: Incorporating the Administrative Process*, 98 COLUM. L. REV. 1, 34-41 (1998) (providing an overview of public choice theory).