No. 04-163

IN THE

Supreme Court of the United States

LINDA LINGLE, GOVERNOR OF THE STATE OF HAWAII, and MARK J. BENNETT, ATTORNEY GENERAL OF THE STATE OF HAWAII,

Petitioners,

v.

CHEVRON USA, INC.,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR THE SERVICE STATION DEALERS OF AMERICA AS AMICUS CURIAE IN SUPPORT OF PETITIONERS

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INTERESTS OF AMICUS CURIAE[1]

The Service Station Dealers of America ("SSDA") is a national nonprofit trade association which represents the interests of independent service station dealers located throughout the United States. SSDA was formed in 1948, and represents 20 state and regional affiliates, which in turn represent over 15,000 independent dealers in over 25 states. These independent dealers have a vital interest in supporting legislation such as Act 257, Haw. Rev. Stat. § 486 H-10.4 (1997), which is intended to provide long-term benefits to the citizens of Hawaii by ensuring that the State's retail market is preserved from the oligopoly that has already seized control of the State's wholesale market for gasoline.

REASONS FOR REVERSING LOWER COURT RULING

The constitutional arguments for reversing the lower courts' ruling have been fully laid out in Appellant's brief and will not be repeated here. SSDA will address only the lower courts' assumptions that there is no reason to believe that oil companies would attempt constructive eviction by charging high rents to their lessee-dealers and that, in any event, the Petroleum Marketing Practices Act (PMPA), 15 U.S.C. §§ 2801-2806, "already prevents an oil company from raising rents for the purpose of driving dealers out of business and converting the premises to company-operated stations." *Chevron U.S.A., Inc. v. Cayetano,* 198 F. Supp.2d 1182, 1193 (D.Haw. 2002). *See also Chevron USA, Inc. v.*

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[1] In compliance with Rule 37.6 of this Court, amicus curiae, the Service Station Dealers of America, states that no counsel for any party authored this brief in whole or in part, and that no party or entity other than this amicus curiae, its members or its counsel made a monetary contribution to the preparation or submission of this brief.

Bronster, 363 F.3d 846, 856 (9th Cir. 2004). SSDA submits that these assumptions are insupportable.

Major oil companies like Chevron enjoy enormous leverage over lessee-dealers such as those in Hawaii because they are the dealers' landlords, licensors and exclusive suppliers. This provides them with the ability to destroy their dealers' economic viability. The Senate Report accompanying the passage of the PMPA expressed concern with this problem of supplier dominance that is peculiar to the petroleum industry:

> The franchise relationship in the petroleum industry is unusual, in fact perhaps unique, in that the franchisor commonly not only grants a trademark license but also controls, and leases to the franchisee, the real estate premises used by the franchisee. In addition the franchisor almost always is the primary, even exclusive, supplier of the franchisee's principal sale item: motor fuel.

S.Rep. No. 731, 95th Cong., 2nd Sess., 17 (1978).

Typically, lessee-dealers sink significant expenditures into their businesses based upon the reasonable assumption that their franchise and lease relationships will not be arbitrarily terminated or non-renewed. Their "reasonable expectations" in that regard were also noted in the PMPA Senate Report:

> It is also important to note that often the reasonable expectations of the parties to a motor fuel franchise are that the relationship will be a continuing one. This expectation by the franchisee, in particular, is often the

> result of, and fostered by, statements and actions of the franchisor. As a result, non-renewal of a motor fuel franchise relationship at the expiration of its term can be almost as punitive as termination of the franchise during its term. The reasonable expectations of the franchisee, rather than any definitive contract rights, are destroyed.

Id. at 18.

The district court recognized the crucial role independent service station dealers play in maintaining interbrand and intrabrand competition in what otherwise would be an oligopolistic market, such as Hawaii. It found that "[f]ewer lessee-dealer stations in the market means that retail prices will increase." 198 F. Supp.2d at 1192. The district court explained:

> In the first place, fewer lessee-dealers means greater concentration at the retail level, which means less intra-brand and interbrand competition. In the second place, the fewer lessee-dealers there are, the easier it is for wholesale gasoline suppliers to engage in cooperative pricing, leading ultimately to higher wholesale and retail prices.

Id. This significant finding of fact was not challenged by the court of appeals.

The State of Hawaii has a legitimate interest in preserving what competition remains in an increasingly oligopolistic marketplace. If the lower courts' assumptions that oil companies will not attempt to use high rents to eliminate independent lessee-dealers and that, in any event, the dealers are protected from constructive eviction by the PMPA are unfounded, then the legislature had a reasonable basis for protecting independent dealers from constructive eviction as a means of preventing the upward impact on retail prices that the district court found would otherwise occur as the result of diminished intrabrand and interbrand competition.

SSDA believes itself qualified to comment upon the lower courts' assumptions based upon its extensive knowledge of nationwide conditions in the retail gasoline market. In fact, what has been occurring throughout the retail gasoline market over the past twenty years, coupled with the failure of the PMPA effectively to address the issue of constructive eviction, directly contradicts these assumptions.

That major oil companies have, in fact, too often targeted their own dealers for extinction has been recognized by congressional report. Senate Report No. 102-450 (1992) warned of the oil companies' abuse of their pricing power to evict lessee-dealers in order to convert their stations to company-operation. The report observed:

> Oil companies need not engage in an overt "retail below wholesale" inversion in order to drive their dealers and distributors out of business. Instead, they simply raise the dealers' costs through increased rent, credit card charges, forced 24-hour operation, and the imposition of other costs of doing business that render the superior marketing efficiency of independent dealers and distributors meaningless.

Id. at 5.

Describing the intentions of one major oil company to decimate its own dealers, as detailed in its own Strategic Planning Unit document, the Senate Report recounted ARCO's plans for the future of its "dealer apparatus":

> The "dealer apparatus" would have their costs raised by the implementation of "economic rents" which would raise rents by a factor of 300 to 400 percent. This increase would have two primary effects -- it would make the company indifferent, to a degree, to the sales of motor fuel by the dealers, and it would result in hundreds of dealers being forced out and replaced by company-operated stations. ARCO then planned to "keep prices low until the politic resistance fades," and after that time, a "period of lasting accepting profitability would occur."

Id. at 6. Summarizing the unhealthy market trend that it perceived, the Senate Report concluded, "Any market in which the most efficient marketers are being driven out of business is not a healthy, competitive market." *Id.* at 4.

Two recent federal decisions found that Exxon had abused its pricing power methodically to drive its own lessee-dealers out of business. In *Mathis v. Exxon Corp.*, 302 F.3d 448, 459 (5th Cir. 2002), the Fifth Circuit found that Exxon's Houston and Corpus Christi, Texas dealers had presented "ample evidence" to document Exxon's use of its pricing power to replace independent dealers with company-operations in Houston, and with jobber-supplied locations in Corpus Christi. The court said:

> Although Exxon decided to move to CORS [company-operated locations] in Houston and jobbers in Corpus Christi, this decision was not communicated to its franchisees. Because of profits from their other sales, CORS could, and did, sell gas for less than the franchise dealers paid to Exxon for their gas. And the jobbers delivered Exxon gas to their dealers for less than Exxon franchisees were required to pay for their delivered gas, but Exxon prohibited its franchisees from buying at this lower price from the jobbers.
>
> The loss of competitive position and profit to plaintiff franchisees was inevitable and foreseeable to Exxon. Although Exxon witnesses denied receiving complaints, its dealers testified that they had complained often and for years, without success, until the very eve of trial.

Id.

In *Allapattah Services, Inc. v. Exxon Corp.*, 61 F. Supp.2d 1308, 1313 (S.D. Fla. 1999), *aff'd*, 333 F.3d 1248 (11th Cir. 2003), the district court denied Exxon's motion for summary judgment directed against a claim asserted by a nationwide class of Exxon lessee-dealers that Exxon had evicted numerous of its dealers "by secretly dividing its dealers into 'keepers' and 'non-keepers,' while internally recognizing that its pricing practices were driving the 'non-keepers' out of business." Ultimately, the jury found for the dealer class after reviewing Exxon's own internal documentation, which confirmed its intent to price many of its own dealers out of business.

Significantly, in *Mathis* and *Allapattah* Exxon's design to destroy its own lessee-dealers was *not* challenged under the PMPA but under Uniform Commercial Code § 2-305, which subjects the sale of goods pursuant to open-price-term contracts (such as dealer supplier agreements) to a standard of commercial reasonableness. That provision is not applicable, however, to excessive rent demands made by oil companies on a non-negotiable basis at the time of lease renewal, with the intent and/or effect of making it impossible for the lessee-dealer to continue to operate his or her station.

Recent decisions, unfortunately, have weakened the ability of independent dealers even to utilize U.C.C. § 2-305 as a defense to their suppliers' efforts to convert their stations to company-operation. Rejecting the Fifth Circuit's prediction in *Mathis* concerning its interpretation of state law, the Supreme Court of Texas held in *Shell Oil Co. v. HRN, Inc.*, 144 S.W.3d 429, 435 (Tex. 2004), that an oil company's subjective intent to drive its dealers out of business and convert their locations to company operation is irrelevant for purposes of U.C.C. § 2-305, so long as its prices remain in the range of prices charged by other refiners in the marketplace. In increasingly oligopolistic markets, like Hawaii, this restrictive interpretation of §2-305 affords the dealer little if any protection against abusive pricing schemes intended to convert his or her station to company operation.

It is no accident that PMPA challenges ultimately were not pursued in *Mathis* or *Allapattah*. Contrary to the assumptions made by the courts below, the PMPA has proven wholly ineffective in protecting independent dealers targeted for extinction through non-competitive pricing or through non-negotiable high rent demands made at the time of lease renewal. This is so because the pertinent statutory provision, 15 U.S.C. § 2802(b)(3)(A), only grants relief to a dealer who can prove that his or her supplier's renewal terms were consciously formulated so as to frustrate the continuation of the franchise relationship. As a result, so long as the oil company is not stupid enough to concede the true purpose of its pricing or rent demands, the dealer is very unlikely to secure relief under the PMPA. *See, e.g., Duff v. Marathon Petroleum Co.*, 863 F. Supp. 622, 628 (N.D. Ill. 1994), *aff'd*, 51 F.3d 741 (7th Cir. 1995) ("Under the PMPA, Marathon does not need to prove that the rent increases were reasonable, only that they were made in the ordinary course of business and not as a pretext for termination of the franchise."); *Ackley v. Gulf Oil Corp.*, 726 F. Supp. 353, 368 (D. Conn.), *aff'd*, 889 F.2d 1280 (2d Cir. 1989) (rent increases of up to 761% not challengeable because it is not sufficient that rent formula "operate unreasonably in a particular case"); *Brown v. Magness Co.*, 617 F. Supp. 571, 575 (S.D. Tex. 1985) ("The fact that new provisions in a franchise agreement may make the station unprofitable for the lessee is not of itself determinative of an improper purpose, nor does the fact that the new terms are presented on a take-it-or-leave-it basis constitute lack of good faith.") (internal citations omitted); *Meyer v. Amerada Hess Corp.*, 541 F. Supp. 321, 330 (D. N.J. 1982) (upholding rental increase of over 300%).

Loading the dice further against dealers seeking to challenge exorbitant rent demands presented to them on a non-negotiable basis by their oil company landlords, two circuits have recently held that dealers cannot sign leases "under protest" and commence PMPA litigation, but must risk non-rescindable notice of termination in order to mount a court challenge. *Abrams Shell v. Shell Oil Co.*, 343 F.3d 482 (5th Cir. 2003); *Dersch Energies, Inc. v. Shell Oil Co.*, 314 F.3d 846 (7th Cir. 2002). This means that if the dealer is unable to unmask the oil company's hidden intent, he or she is out of business.

Further undermining the willingness or ability of independent dealers to mount a PMPA challenge is the virtually universal practice of oil companies of inserting in their form franchise agreements prevailing party attorneys-fees provisions or one-sided provisions requiring the dealer to pay the oil company's attorneys fees if his or her challenge is unsuccessful. To the dealer alone such attorneys fees are ruinous.

The net result of all this is that, in the real world, attempts by independent dealers to use the PMPA to challenge their suppliers' unreasonable take-it-or-leave-it rent proposals are rarely even attempted much less successful, which is totally inconsistent with the lower court's erroneous assumption that the PMPA "prevents an oil company from raising rent for the purpose of driving dealers out of business and converting the premises to company-operated stations." *Chevron U.S.A,,* 198 F. Supp.2d at 1193. In the real world, that simply is not so.

Unfortunately, SSDA lacks the resources and ability to document the extent through which the ranks of independent dealers have been thinned by the oil companies' exorbitant non-negotiable rent demands and predatory pricing policies. Based upon its observation of the industry, however, SSDA submits that the impact has been very substantial. Typical of the extensive anecdotal evidence that it has received is the recent report from its New England affiliate:

> Shell has raised rent so much in Massachusetts and New Hampshire that the dealer population has been reduced by about 40% in the past three years. There is only one dealer left on Cape Cod, a few years ago

> there were dozens. Dealers exhausted their working capital, then resorted to loans and equity loans. Most eventually lost their businesses, some had buyers, but still went bankrupt because of the lengthy, cumbersome, subjective approval process [required by Shell to obtain its consent to assignment].
>
> Exxon is similar, many dealers got fed up and turned in the keys. All along intending to sell the business as a substantial part of their retirement savings.

Given the PMPA's failure to address effectively the issues of constructive termination and economic non-renewal, a number of states have implemented measures to protect independent service station dealers from extinction. Most notable are restrictions on refiner-operated service stations. By restricting the ability of major oil companies to operate service stations themselves, such laws eliminate the oil companies' motive for driving independent dealers out of business through high rent demands or other pricing schemes. At least five jurisdictions impose such restrictions on refiners' ability to convert independent service stations to company operation. *See* CONN. GEN. STAT. ANN. § 14-344a (West 2004); DEL. CODE ANN. tit. 6, § 2905 (2004); D.C. ST. § 36-302.02 (West 2001); MD. CODE ANN., BUS. REG. § 10-311 (2004); VA. CODE ANN. § 59.1-21.16:2 (West 2004). In addition, Nevada requires any refiner operating more than thirty service stations in the state to lease one station to an independent dealer for every two directly owned service stations. *See* NEV. REV. STAT. ANN. § 597.440 (West 2004).

Other states, such as Alabama, Missouri, Florida, Utah and North Carolina, have passed legislation restricting oil companies from competing unfairly with independent dealers through company-operated stations. *See* ALA. CODE § 8-22-1 *et seq.* (2004); MO. ANN. STAT. § 416.615 (West 2004); FLA. STAT. ANN. § 526.304 (West 2004); UTAH CODE ANN. § 13-16-4 (2001); N.C. GEN. STAT. § 75-82 (2004). These statutes attempt to restrict the oil companies from pricing their dealers out of business by unfairly favoring their company-operated locations.

Any doubt about these states' ability to enact legislation intended to promote competition in the petroleum market to the ultimate benefit of the motoring public should have been laid to rest by this Court's opinion in *Exxon Corp. v. Governor of Maryland*, 437 U.S. 117 (1978). In upholding the constitutionality of the Maryland divorcement statute, which precluded oil companies from displacing independent dealers with company-operated stations, this Court stated:

> The evidence presented by the refiners may cast some doubt on the wisdom of the statute, but it is, by now, absolutely clear that the Due Process Clause does not empower the judiciary "to sit as a 'super legislature to weigh the wisdom of legislation' . . ." *Ferguson v. Skrupa*, 372 U.S. 726, 731 (citation omitted) . . . . Regardless of the ultimate economic efficacy of the statute, we have no hesitancy in concluding that it bears a reasonable relation to the State's legitimate purpose in controlling the gasoline retail market, and we therefore reject appellants' due process claim.

Id. at 124-25.

Simultaneous with the enactment of Act 257 at issue here, Hawaii repealed Hawaii Rev. Stat. § 486 H-10, a divorcement statute that was analogous to the Maryland provision upheld by this Court in *Exxon*. Hence, the present statute represents no more than an alternative method of addressing the problem previously addressed by the divorcement statute. Indeed, Act 257 is less burdensome than its predecessor because it frees major oil companies to operate competing company-operated locations. Far from a renegade measure, the new statute represents a compromise, allowing oil companies to operate service stations while simultaneously protecting independent dealers from outrageous rent demands. In *Exxon's* language, "[r]egardless of the ultimate economic efficacy of the statute,. . .it bears a reasonable relation to the State's legitimate purpose in controlling the gasoline retail market. . . ." *Id.* at 125.

SSDA respectfully submits that due deference should be shown to Hawaii's determination that independent dealers should be preserved from extinction in order to promote interbrand and intrabrand competition in the retail gasoline market. This is particularly so because the lower court's assumptions that oil companies will not use high rents to eliminate lessee-dealers and that those dealers are adequately protected by the PMPA are debatable at best; and, the district court itself recognized the substantial linkage between preserving interbrand and intrabrand competition at the retail level and protecting Hawaii's citizens against the threat of oligopolistic price gouging. *Chevron U.S.A.*, 198 F.Supp.2d at 1193. SSDA respectfully submits, therefore, that the lower courts' invasion of Hawaii's legislative province should be reversed.

Respectfully submitted,

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