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Dealer Management System Providers Join the Fray in Dispute Over Proper Scope of State Dealer Laws

By Brandon Bigelow, Caleb Schillinger, and Eric Walz

The two leading Dealer Management System ("DMS") providers in the United States—CDK Global, LLC ("CDK") and The Reynolds & Reynolds Company ("Reynolds")—have filed suit in federal court in Arizona seeking to block an amendment to that state's dealer statute that would require them to give free access to their systems to certain third parties. The recent change to the Arizona dealer statute is notable because it goes beyond the dealer-manufacturer relationship to regulate private arrangements between automobile dealers and other parties. The arguments made by the DMS providers against the Arizona law will be familiar to automobile manufacturers who have brought challenges to state dealer statutes in the past; if successful, these arguments may have an impact on the scope of these statutes going forward.

The Relationship Between Dealers and DMS Providers. Under their agreements with manufacturers, dealers promise to engage in the active and effective sale and service of new motor vehicles and parts to consumers in their area. The efficient performance of this obligation requires dealers to keep track of vital business information including accounting, payroll, inventory, sales, parts, service, finance, and insurance. Because much of this is heavily regulated consumer and financial data, dealers use specially-designed computerized dealer management systems to perform these functions. Dealers license the software and hardware that comprise these systems from CDK, Reynolds, or another DMS provider.

Other businesses called "integrators" collect DMS data and make it compatible with vendor applications; vendors then use DMS data that has been processed by an integrator to provide additional services to dealers for a fee. Because DMS data is heavily regulated and the DMS platform uses proprietary software, the agreements between DMS providers and dealers typically prohibit dealers from allowing third parties (like integrators and vendors) to access DMS software and data without the provider's permission. These restrictions have been the subject of recent antitrust lawsuits brought by dealers, integrators, and vendors.

DMS Providers Challenge the Amended Arizona Dealer Statute. In April 2019, Arizona enacted the Dealer Data Security Law (the "DMS Law")—codified at Sections 28-4651 to 28-4655 of the Arizona Revised Statutes—which amended the Arizona dealer statute to add provisions regulating the relationship between dealers and DMS providers. The new statutory provisions, which were due to go into effect on August 27, 2019, require DMS providers to give access to their proprietary systems to any third party identified by an automotive dealership as an authorized integrator, and prohibit DMS providers from charging a fee for such access.

In late July 2019, CDK and Reynolds filed a complaint for declaratory judgment and sought preliminary injunctive relief prohibiting enforcement of the DMS Law by the Arizona Department of Transportation. In a strongly worded complaint, CDK and Reynolds allege that the DMS Law was "falsely described to legislators as a consumer-protecting data privacy

measure"; that the amendment to the dealer statute was in fact "drafted and pushed through by the Arizona Automobile Dealers Association"; and that "[f]ar from protecting consumers, the DMS Law necessarily puts consumers' data at extremely high risk . . . ." CDK and Reynolds contend that the DMS Law is preempted by federal copyright law, the Computer Fraud and Abuse Act, the Gramm-Leach-Bliley Act, and other federal statutes; runs afoul of the Contracts Clause, Dormant Commerce Clause, and Due Process Clause of the U.S. Constitution; and also invades the First Amendment rights of CDK and Reynolds and constitutes a forced taking of their property without just compensation.

In early September 2019, the court entered an order approving a proposed briefing schedule by the parties and prohibiting the Department of Transportation from enforcing the DMS Law pending resolution of the motion for preliminary injunction. Soon thereafter, the Arizona Automobile Dealers Association ("AADA") intervened in the case, and in late September 2019, the AADA and the Department of Transportation filed their responses, arguing that although CDK and Reynolds owned their DMS platforms, dealers owned the data stored on that platform; emphasizing the requirements imposed by the DMS Law on integrators to take appropriate steps to protect dealer data received from DMS platforms; and dismissing the statutory and constitutional arguments made by CDK and Reynolds as misplaced. The court has granted CDK and Reynolds until October 28, 2019 to prepare and file a consolidated reply; no hearing on the motion for preliminary injunction has yet been set.

OEMs Should Watch This Space. The constitutional arguments made by CDK and Reynolds will be familiar to manufacturers who have in the past challenged dealer statutes for overreaching and intruding into private arrangements between parties. In particular, the Dormant Commerce Clause and Contracts Clause arguments presented by CDK and Reynolds are reminiscent of the arguments made in *Alliance of Automobile Manufacturers v. Gwadosky*, 430 F.3d 30 (1st Cir. 2005), in which the First Circuit rejected constitutional challenges to a provision of the Maine dealer statute prohibiting manufacturers from imposing a surcharge to recover the cost of compliance with that law's warranty reimbursement requirements. The DMS providers' challenge to the DMS Law presents the first serious constitutional challenge to a state dealer law since Gwadosky, and bears watching in the coming months.

Brandon Bigelow and Caleb Schillinger are partners and Eric Walz is an associate in Seyfarth Shaw's Franchise and Distribution Practice Group. The Seyfarth Shaw Franchise and Distribution Practice Group represents automobile manufacturers in their disputes with dealers. The case is *CDK Global, LLC et al. v. Brnovich et al.*, No. 2:19-cv-04849-GMS, pending in the United States District Court for the District of Arizona. If you have any questions, please contact Brandon at *bbigelow@seyfarth.com,* Caleb at *cschillinger@seyfarth.com* or Eric at *ewalz@seyfarth.com*.