Franchising & Distribution Currents

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ANTITRUST

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***Butler v. Jimmy John's Franchise, LLC*, Bus. Franchise Guide (CCH) ¶ 16,241, 2018 WL 3631577 (S.D. Ill. July 31, 2018)**

The court denied in part and granted in part a motion to dismiss alleging violations of state and federal law arising out of non-poaching clauses in a franchise agreement.

Jimmy John's Franchise, LLC (Jimmy John's) is the franchisor of a chain of sandwich shops. All the franchise agreements between Jimmy John's and its franchisees contain a "non-poaching" clause, which states that the franchisee will not "solicit or initiate recruitment of any person then employed, or who was employed within the preceding 12 months" by Jimmy John's, any of its affiliates, or any of its franchisees. If a franchisee violates this provision, it is considered a non-curable default, and grounds for termination of the franchise agreement. Under the franchise agreement, a terminated franchise owes Jimmy John's liquidated damages in the amount of three years' worth of royalties. In addition, the franchise agreement provides that all other franchisees of Jimmy John's are third-party beneficiaries of the non-poaching provision and therefore have an independent right to sue to enforce the provision. Such a suit put the at-fault franchisee at risk of paying liquidated damages of $50,000 to Jimmy John's.

To protect themselves, franchisees of Jimmy John's made their employees sign noncompete agreements, which required them to (1) refrain from working at any business that sells sandwiches for two years after their

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employment ended with Jimmy John's; (2) notify the franchisee of any employment offers by a competitor; and (3) reimburse all costs, including attorney's fees, incurred by Jimmy John's or the franchisee in enforcing the noncompete agreement.

Sylas Butler (Butler) had worked for approximately a year and a half at a Jimmy John's franchise as an in-store employee and delivery driver. Butler alleged that his manager significantly reduced his hours and that he was prevented from getting hired at another franchised location due to the noncompete that his employer forced him to sign. Thus, Butler claimed his only options were to either stay at the franchise he was at in a stagnant job or quit and start fresh at an entry-level position with a non-sandwich shop. Butler quit and then brought suit on behalf of a putative class of all current and former employees of a Jimmy John's franchise, claiming that Jimmy John's and its franchisees had violated Section 1 of the Sherman Act, the Illinois Antitrust Act, and the Illinois Consumer Fraud and Deceptive Business Practices Act.

Jimmy John's and the franchisee defendants moved to dismiss all the claims. They first argued that Butler lacked standing under Article III of the Constitution because he had failed to adequately allege an injury that he had personally suffered. The court made quick work of this argument, finding that Butler's allegations of being prevented from transferring and a depression of his wages due to the allegedly wrongful acts was an injury in fact and that the allegations, if true, demonstrated harm to the labor market, the kind of injury that the Sherman Act was meant to prevent.

Having established standing, the court turned to whether Butler had adequately pled a violation of the Sherman Act. The first step in determining collusive and anti-competitive behavior is to determine whether the alleged violation is a horizontal agreement or a vertical agreement. "Horizontal agreements—agreements made among direct competitors—are typically per se violations of [the Sherman Act] because they 'always or almost always tend to restrict competition and decrease output.'" Thus, a party pleading a horizontal violation does not need to "make any inquiry into the market context in which the restraint operates."

A vertical agreement, however, is one "made up and down the supply chain." Vertical agreements are subject to the "rule of reason" analysis, "which focuses on 'the facts peculiar to the business, the history of the restraint, and the reasons why it was imposed.'" Plaintiffs have to meet a much higher burden in establishing a vertical agreement: they "must show the existence of anticompetitive effects in the relevant product and geographical markets, in which the defendant must have market power."

Sometimes an agreement evades neat categorization as either horizontal or vertical, and a third test, the "quick-look approach," may be used. The court explained that courts "use this test where the per se framework is inappropriate—such as when the restraint is a vertical agreement—but where the anticompetitive effects of the agreement are so obvious that 'an observer with even a rudimentary understanding of economics could conclude that

the arrangements in question would have an anticompetitive effect on customers and markets.'" The quick-look approach is also used where the per se rule, applicable to horizontal agreements, would ordinarily apply but "a certain degree of cooperation is necessary if the [product at issue] is to be preserved." Under the quick-look approach, plaintiffs are not required to address the relevant markets or provide evidence of market power if they can show "no legitimate justifications for the anticompetitive behavior." The defendant is given an opportunity to respond with pro-competitive justifications, which will then shift the burden back to the plaintiff to conduct a full "rule of reason" analysis.

The court was unable to determine, at the motion to dismiss stage, which standard to apply in this case. It reasoned that the relationship between franchisor and specific franchisees is more akin to a vertical agreement, whereas the relationships among the franchisees are horizontal. The court likened the relationships amongst Jimmy John's and its franchisees to a hub-and-spoke wheel. In a "hub-and-spoke" conspiracy, the "hub" enters into agreements with each of the other entities, the spokes, which then enter into agreements that create the horizontal anticompetitive behavior. "The idea here is that since the hub orchestrated the horizontal wheel, it can be held per se liable for that horizontal agreement—even though the hub did not enter into a horizontal agreement itself."

The court noted, however, the "massive elephant in the room;" ordinarily antitrust concerns itself with *inter*brand restraints, or restraints among different brands, and not *intra*brand restrains, such as those entirely within the Jimmy John's brand. To get around that issue, Butler had pled that the Jimmy John's franchisees are vested with an unusual level of independence, which "may be much more than your typical franchise business may enjoy." The court decided that if there was evidence the franchisees are truly as independent as was pled, it would likely use a "quick look analysis." "If the evidence of franchisee independence is Herculean then the per se rule might even apply." However, if the evidence of franchisee independence was weak, or if Jimmy John's met its burden of showing a procompetitive justification in the quick-look analysis, then the "rule of reason" analysis may apply. In any event, the court held that Butler had adequately pled the Sherman Act violation to survive a motion to dismiss.

As to the state law claims for violations of the Illinois Antitrust Act and the Illinois Consumer Fraud and Deceptive Business Practices Act, the court held that neither statute was meant to reach the claims alleged by Butler arising out of his employment. The state law claims were dismissed, but the court gave Butler leave to replead.

***Deslandes v. McDonald's USA, LLC,* Bus. Franchise Guide (CCH) ¶ 16,219, 2018 WL 3105955 (N.D. Ill. June 25, 2018)**

The U.S. District Court of the Northern District of Illinois denied in part and granted in part a motion to dismiss alleging violations of state

and federal law arising out of a no-hire provision contained in a franchise agreement.

Leinani Delandes, a former employee of a McDonald's franchise in Florida, filed suit against McDonald's USA, LLC, and McDonalds's Corporation (collectively, McDonald's) in the U.S. District Court of the Northern District of Illinois, alleging that the no-hire provision in some of McDonald's standard form of franchise agreements violates Section 1 of the Sherman Antitrust Act, the Illinois Antitrust Act, and the Illinois Consumer Fraud and Deceptive Trade Practices Act. The gist of plaintiff's claims is that McDonald's and its franchisees engage in concerted activity to restrict competition among themselves for employees, which results in decreased employment costs and limits the employees' ability to earn higher wages. McDonald's filed a motion to dismiss plaintiff's claim pursuant to Federal Rule of Civil Procedure 12(b)(6).

Plaintiff alleged that, although McDonald's franchisees are independent business owners and responsible for employment matters involving their restaurants, their hiring decisions are restricted by the no-hire provision in many of the franchise agreements. This provision prohibits a franchisee from employing or seeking to employ any employee of McDonald's, its subsidiaries, or of a person operating a McDonald's restaurant (i.e., another franchisee). Plaintiff alleged that the no-hire provision promoted collusion among the franchisees, was against the franchisees' best interest by prohibiting them from hiring the best employees, and helped franchisees keep costs low by allowing them to pay below-market wages to their own employees.

Plaintiff worked for a number of years at a franchised McDonald's restaurant in Florida and was promoted several times. Her employer ultimately enrolled her in a weeklong training course at McDonald's Hamburger University, but cancelled the training when it learned she was pregnant. Upset with this decision, plaintiff applied for a position at a nearby McDonald's restaurant that was owned by one of McDonald's USA, LLC's subsidiaries (McOpCos). The position paid more than her prior position. Plaintiff was told by the store manager of the nearby McDonald's restaurant that she would like to hire her. The next day, however, a McDonald's corporate employee called plaintiff and told her she could not be hired to work at the corporate restaurant unless her employer "released" her. Plaintiff's employer refused to release plaintiff, telling her she was "too valuable."

Plaintiff contends that the no-hire provision amounts to a restraint that is either unlawful per se or under the "quick look" analysis. McDonald's disagreed, arguing the restraint at issue needed to be analyzed under the rule of reason framework, such that plaintiff would need to allege market power in the relevant market, and plaintiff's complaint did not include any such allegations.

To decide which standard to apply, the court first considered whether the restraint was horizontal as plaintiff alleged or vertical as McDonald's alleged. The court concluded that although the restraint had some vertical elements,

it was a horizontal restraint because it limited competition for employees among horizontal competitors—the McDonald's franchise restaurants and the McOpCos restaurants. The court further concluded that by including the no-hire provision in the franchise agreements, McDonald's was effectively protecting its own restaurants from horizontal competition.

The court then addressed the question of whether the alleged horizontal restraint was "naked" (i.e., without any competitive benefit) and, therefore, per se unlawful, or ancillary to an agreement that was pro-competition and, therefore, analyzed under the rule of reason or by the quick look test. The court found the restraint to be part of a franchise agreement that was "output enhancing" and, thus, pro-competitive. The court further found that because the claimed restraint was ancillary to an agreement with a pro-competitive effect, it could not be per se unlawful.

The court then turned to the question of whether the restraint could be unlawful under the quick-look analysis, which depends on whether a person with "even a rudimentary understanding of economics" would understand that the arrangement/restraint has an anticompetitive effect. In undertaking this analysis, the court noted that plaintiff had directly experienced "stagnation" in her wages as a result of McDonald's no-hire prohibition.

McDonald's argued that the no-hire restriction was pro-competitive because it promotes interbrand competition (e.g., competition between McDonald's and Burger King for customers). The court disagreed with McDonald's' theory, stating that the case is not about the sale of hamburgers to consumers, but rather about intrabrand competition for employees. The court concluded that McDonald's had effectively divided the market for employees by prohibiting restaurants from hiring each other other's current or former employees, which stifled intrabrand competition for employees. The court also rejected McDonald's argument that the restriction promoted intrabrand competition for the sale of hamburgers by encouraging franchisees to train employees for management positions. Although the court acknowledged that McOpCos and the franchisees would be concerned about training and then losing employees, the no-hire restriction was not limited to management-level employees, but applied to all employees, including entrylevel employees. The court further found that such employer concerns are universal and do not justify an unlawful market division.

Despite finding that plaintiff had adequately pleaded a Sherman Act claim under the quick-look analysis, the court noted in dicta that plaintiff may not be able to ultimately prove her claim because plaintiff would need to prove market power in a relevant market. The court noted that the relevant market for the type of employees that work at "low-skill retail or restaurant" jobs is a relatively small geographic area and that a large number of such small market areas may "cut against" certification of a nationwide class.

The court made short work of plaintiff's state law claims. The court first held that plaintiff's Illinois Antitrust Act claim was specifically excluded by the language of the statute, which does not apply to services based on "labor

which is performed by natural persons as employees of others." The court then held that plaintiff's Illinois Consumer Fraud Act claim was precluded because the statute is intended to protect consumers from fraud and not intended as an antitrust enforcement mechanism. Accordingly, both of plaintiff's state laws law claims were dismissed with prejudice.

***Hyundai Motor Am., Inc. v. Direct Techs. Int'l, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,254, 2018 WL 4110544 (W.D.N.C. Aug. 29, 2018)**

The U.S. District Court for the Western District of North Carolina denied Hyundai Motor Company America, Inc.'s (Hyundai) motion to dismiss Direct Technologies International, Inc.'s counterclaims (DTI) for failing to state a claim.

Hyundai filed suit against DTI claiming that DTI was importing and selling Hyundai-branded parts through an unauthorized distribution chain and that these parts were materially different from the genuine Hyundai parts sold in the United States. DTI in turn filed a counterclaim against Hyundai, alleging that Hyundai illegally restrained trade by requiring that only Hyundai-branded replacement parts could be used without voiding a vehicle's warranty and by tying its sales of these parts to dealership franchises for new vehicles. DTI asserted claims for (1) illegal restraint of trade in violation of Section 1 of the Sherman Act; (2) illegal monopoly in violation of Section 2 of the Sherman Act; (3) exclusive dealing arrangement in violation of the Clayton Act; (4) false advertising and unfair competition in violation of the Lanham Act; (5) unfair competition in violation of North Carolina's Unfair and Deceptive Trade Practices Act (UDTPA); and (6) unfair competition under North Carolina common law.

The court first addressed DTI's claim under Section 1 of the Sherman Act and Hyundai's argument that DTI had failed to allege a relevant market and demonstrate an actual tying relationship, a tying product, or a tied product. The court disagreed with Hyundai, finding that DTI had identified the relevant market as "the replacement part market for Hyundai automobiles" and had alleged harm to competition. The court further found that DTI had provided support for its claims in the form of a FTC warning letter and an email from Hyundai. Thus, the court held that DTI had sufficiently alleged facts and conduct by Hyundai that, accepted as true, constituted viable grounds for a Section 1 claim.

As to DTI's claim under Section 2 of the Sherman Act, Hyundai again argued that DTI had failed to allege a relevant market, as well as an actual tying relationship, tying, or a tied product, or a monopoly or market power in any of the products. The court again disagreed, concluding that DTI had alleged (1) a relevant market, (2) that Hyundai tied the sale of replacement parts for Hyundai automobiles to its dealership franchises for new vehicles, (3) that Hyundai exploited its monopoly power, and (4) that Hyundai specifically intended to maintain or enhance its dominant position and/or

attempt to monopolize the market. The court held that, if true, Hyundai's agreements with its dealers and distributors affected a substantial volume of interstate commerce in the market for replacement parts for Hyundai automobiles and that Hyundai effectively acquired a monopoly through coercing its dealers into entering these agreements. Accordingly, the court denied Hyundai's motion as to DTI's Section 2 claim.

The court then examined DTI's Clayton Act claim, which requires an allegation of injury to competition and not just to one particular competitor. Hyundai argued that DTI had not alleged a cognizable antitrust market and had not asserted that the alleged exclusive dealing agreement would impede competition. The court rejected this argument, finding that DTI had alleged that the exclusive dealing arrangement caused harm to itself, as well as to sellers and resellers, and that consumers of replacement parts for Hyundai automobiles would also be damaged by an overall reduction in competition. Therefore, the court held that DTI had alleged a probable effect to the market share of other competitors in the United States and allowed the Clayton Act claim to proceed.

The court next considered DTI's false advertising claim under the Lanham Act, which requires a plaintiff to allege an injury to a commercial interest in reputation or sales, as well as economic or reputational injury flowing directly from the deception caused by the defendant's advertising. DTI alleged that Hyundai's advertising was misleading, had deceived purchasers into believing that Hyundai warranties would be void if replacement parts sold by DTI were used in Hyundai vehicles, and caused confusion regarding the extent of the vehicle warranty. DTI further alleged that it was economically harmed because Hyundai dealers had refused to purchase parts from DTI because of Hyundai's warranty policy. Based on these allegations, the court found that DTI had adequately pled a Lanham Act claim.

With respect the UDTPA claim, Hyundai argued that DTI had failed to allege any anticompetitive conduct. The court found otherwise, noting DTI's allegations that Hyundai engaged in unfair business practices and that the claimed conduct had a tendency to deceive and be injurious to consumers, sellers, and resellers. The court further found that DTI had alleged that Hyundai's actions were in or affected commerce and proximately injured DTI. Accordingly, the court denied Hyundai's motion as to the UDTPA claim.

Finally, the court addressed DTI's common law unfair competition claim, which alleged that Hyundai's conduct had a tendency to deceive consumers, sellers, and resellers and, as a result, DTI suffered a loss in sales. In particular, DTI alleged that Hyundai's actions damaged legitimate business activities related to DTI's sale of legitimate, non-counterfeit Hyundai-branded parts for Hyundai automobiles. The court ultimately found that, because DTI's Sherman Act and the Lanham Act claims were sufficiently pleaded, the unfair competition claim was also adequately pleaded.

***Maxon Hyundai Mazda v. Carfax, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,209, 726 F. App'x 66 (2d Cir. June 1, 2018)**

The U.S. Court of Appeals for the Second Circuit affirmed the partial summary judgment granted in favor of Carfax, Inc. (Carfax), the largest provider of Vehicle History Reports (VHRs), and against more than 450 used-car dealers (plaintiffs).

Carfax moved for partial summary judgment on the single issue of whether Carfax's exclusive dealing arrangements with websites and manufacturers' Certified PreOwned Programs (CPO Agreements) violated Sections 1 and 2 of the Sherman Act. The district court found, among other things, that plaintiffs had failed to establish the requisite market foreclosure because errors in the report of plaintiffs' expert precluded any reasonable jury from adopting the expert's opinion that Carfax's exclusive dealing agreements foreclosed a sufficient portion of the VHR market. On appeal, the Second Circuit agreed with the district court's reasoning and rejected plaintiffs' challenges to the decision.

First, plaintiffs argued that the district court failed to hold Carfax to its burden on summary judgment because Carfax did not produce evidence showing that the market was not foreclosed. The court disagreed, concluding that Carfax was not required to prove the market was not foreclosed under the Sherman Act; it only needed to show that plaintiffs failed to provide evidence of the requisite market foreclosure.

Second, plaintiffs challenged the district court's conclusion that errors in the report of their expert precluded any reasonable jury from adopting the expert's conclusion that Carfax's exclusive dealing agreements foreclosed a sufficient portion of the VHR market. In addressing this argument, the court affirmed the definition of the VHR market, which was controlled by the parties' own stipulation. The court agreed with the district court's finding that plaintiffs' expert should have included in his analysis VHRs based primarily on minimum data required by the National Motor Vehicle Title Information System. The court also rejected plaintiffs' argument that the effect of the expert's failure to include non-exclusive CPO Agreements in his analysis was minimal and likely offset by other parts of his analysis that understated the degree of foreclosure. The court determined that this argument was conjectural and did not warrant overturning the district court's grant of summary judgment. Finally, the court did not find error in the district court's criticism of plaintiffs' expert's failure to consider sales to non-dealer customers for the period from 2008 to 2011 on the ground that plaintiffs' expert had the opportunity in his reply report to recalculate his estimates in light of the recently produced data regarding such sales but elected not to. Accordingly, the court found that the district court correctly determined that plaintiffs' expert erroneously defined the parameters of the VHR market.

Third, the court rejected plaintiffs' argument that the district court incorrectly determined that the competitive characteristics of the VHR market did not support a substantial foreclosure finding. Although plaintiffs pointed

to costs incurred by Carfax and its primary competitor, the court determined that plaintiffs had failed provide evidence that such costs are necessarily incurred when entering the market. The court also disregarded the evidence that some dealers preferred Carfax's competitor, but nonetheless remained Carfax's customers, on the basis that such evidence did not constitute an empirical demonstration of adverse effects on competition. Furthermore, the court found that plaintiffs had failed to show that prices were higher in the market as a whole such that harm was done to competition; the evidence only demonstrated that prices increased for VHRs sold by Carfax to franchised dealers in 2010–2012. The court held that this evidence did not itself directly demonstrate harm to competition. The court also agreed that the duration of the website arrangements was not sufficient to raise antitrust concerns and that even the longest agreements did not significantly undercut the overall conclusion that the agreements at issue were not particularly longterm to lock dealers into buying Carfax's VHRs.

Fourth, the court rejected plaintiffs' argument that the district court failed to consider whether they had demonstrated foreclosure in the relevant submarkets because plaintiffs' submarket foreclosure theory was premised on the same expert report that the court found to be deficient.

Finally, the court found that plaintiffs had failed to support their allegations of monopolization and attempted monopolization under Section 2 of the Sherman Act as they had not adduced evidence supporting their anticompetitive conduct theory.

ARBITRATION

***Alemayehu v. Gemignani*, Bus. Franchise Guide (CCH) ¶ 16,247, 2018 WL 3861161 (D. Colo. Aug. 14, 2018)**

The U.S. District Court for the District of Colorado denied a motion to lift a stay pending a decision by the Second Circuit on whether the parties could be compelled to arbitrate their dispute in Connecticut.

In January 2017, Girum Alemayehu (Alemayehu) filled out and submitted an online application to be approved as a Subway restaurant franchisee. The franchise application contained an arbitration clause requiring Alemayehu to arbitrate, in Connecticut, "any and all previously unasserted claimed, disputes or controversies arising out of or relating to my candidacy or application for the grant of a Subway franchise" from Doctor's Associates Inc. (DAI), the franchisor of Subway restaurants. DAI considered the application, but did not approve Alemayehu.

In January 2018, Alemayehu filed suit in the U.S. District Court for the District of Colorado alleging that DAI and various of its agents had refused to approve his application because of his race and ethnicity. Alemayehu asserted claims under 42 U.S.C. § 1981 and various common law theories. In response, DAI filed a petition to compel arbitration in the U.S. District Court for the District of Connecticut, which DAI argued was the only

district court with authority to compel arbitration under the Federal Arbitration Act (FAA). Alemayehu and the defendants agreed to stay the Colorado case pending a decision by the Connecticut court. On June 7, 2018, the Connecticut court denied the petition to compel arbitration, holding both that the arbitration clause was not supported by consideration and that the consideration issue was not delegated to the arbitrator. DAI appealed the Connecticut court's decision to the Second Circuit.

On June 22, 2018, Alemayehu filed a motion to dissolve the stay in the Colorado case. DAI opposed the motion and asked the Colorado court to maintain the stay pending a decision by the Second Circuit. DAI argued that a stay was mandatory under existing Tenth Circuit precedent, which provides that a district court is divested of jurisdiction while a non-frivolous appeal of a denial of an FAA petition is pending. DAI argued in the alternative that a discretionary stay was appropriate under the court's inherent powers to manage its docket. Alemayehu argued that the mandatory stay rule did not apply because the appeal was pending in a different circuit and was not an appeal of an interlocutory order, but of a final judgment entitled to res judicata effect. Alemayehu also asserted that a discretionary stay would improperly delay the proceedings.

The Colorado court concluded that a stay was mandatory under Tenth Circuit precedent, finding that the rationale undergirding the existing Tenth Circuit rule applied with equal force when an appeal is pending outside the court's home circuit and when it is an appeal of a final order. The Colorado court also concluded that even if a stay was not mandatory, a discretionary stay was appropriate. The Colorado court explained that the defendants had shown a likelihood of success on appeal, the potential loss of arbitration rights amounted to irreparable harm, and a stay created little risk of prejudice. The Colorado court ordered that the case remain stayed until the Second Circuit issued its ruling on the appeal.

John Doroghazi is lead counsel for Doctor's Associates Inc. in both the Colorado and Connecticut cases.

***Stockade Companies, LLC v. Kelly Restaurant Group, LLC*, Bus. Franchise Guide (CCH) ¶ 16,214, 2018 WL 3018177 (W.D. Tex. June 15, 2018)**
This case is discussed under the topic heading "Attorneys Fees."

ATTORNEYS FEES

***Stockade Companies, LLC v. Kelly Restaurant Group, LLC*, Bus. Franchise Guide (CCH) ¶ 16,214, 2018 WL 3018177 (W.D. Tex. June 15, 2018)**
In this case, the U.S. District Court for the Western District of Texas denied a request for attorneys' fees by a former franchisee, defendant Kelly Restaurant Group, after the franchisor, Stockade Companies, LLC (Stockade), withdrew its lawsuit without prejudice pursuant to Federal Rule of Civil Procedure 41.

Stockade is the franchisor of Sirloin Stockade, Coyote Canyon, and Montana Mike's restaurants. In June 2014, Stockade entered into fifteen franchise agreements with Kelly Restaurant Group, LLC (KRG). KRG failed to make royalty payments, and Stockade sent it a default notice demanding payment and giving KRG the opportunity to cure. When KRG failed to cure, Stockade issued a notice of termination, which included a demand that KRG cease using Stockade's proprietary marks. Despite the notice of termination, KRG continued to operate its restaurants using the Sirloin Stockade, Coyote Canyon, and Montana Mike's brand names.

Stockade sued KRG and its owner Michael Kelly (collectively the franchisees) for trademark infringement, breach of the non-competition covenant in the franchise agreements, and misappropriation of trade secrets. Stockade sought both temporary and permanent injunctions that, if granted, would enjoin the franchisees from using, or infringing upon, its trademarks and from violating the covenants not to compete. The court granted Stockade's motion for injunctive relief in part. It enjoined the franchisees' infringement of the trademarks, but did not grant the portion of the injunctive relief motion directed at enforcing the covenants not to compete. The franchisees were directed to de-identify the restaurants, which the franchisees did. The franchisees, however, kept operating their restaurants under the name "Kansas Buffets."

Stockade then filed a second motion for preliminary injunction. This time, it sought to enjoin KRG from using its confidential information, misappropriating its trade secrets, and infringing on its trade dress. The court denied the second preliminary injunction motion. Shortly thereafter, KRG filed a motion to dismiss all of Stockade's claims. A week later, Stockade voluntarily dismissed its claims without prejudice pursuant to Rule 41.

KRG then filed a motion seeking to recoup the attorneys' fees and costs spent defending the action under the theory that it was prevailing party and therefore entitled to attorneys' fees under a prevailing-party provision in the franchise agreements, as well as certain provisions of federal law and Texas law. KRG argued that Stockade voluntarily dismissed the lawsuit to avoid an unfavorable judgment on the merits. Before reaching the issue of the attorneys' fees, the court first had to determine whether the claim for attorneys' fees was arbitrable under the franchise agreement.

The court previously had addressed the issue of arbitrability of the parties' disputes, when KRG had argued that Stockade's claims for injunctive relief were arbitrable. The court recognized the broadly written arbitration clause in the franchise agreement, but also noted that the very next paragraph after the arbitration clause expressly excepted actions by the franchisor seeking injunctive relief from the scope of the arbitration provision. Thus, the court held that Stockade was not required to arbitrate its injunctive relief claims.

Based on that prior ruling, the court also held that KRG was not required to arbitrate its claim for attorneys' fees arising from Stockade's suit for injunctive relief. "Because this Court has jurisdiction over the underling claims in this case, it follows that it has jurisdiction to review the instant

claim for attorneys' fees." The court further reasoned that, given its greater familiarity with the procedural history of the case, sending the case to the arbitrator for determination of attorneys' fees alone would be costly, inefficient, and time-consuming. Thus, the court, not the arbitrator, would decide the issue of attorneys' fees.

The court then turned to the issue of whether KRG was entitled to attorneys' fees, which rested on its claim that it was a prevailing party. The court recited the general rule that for there to be a prevailing party there must be a "judicially sanctioned change in the legal relationship of the parties," meaning that one of the parties "becomes entitled to enforce a judgment, consent decree or settlement against the [other]." Thus, where a plaintiff voluntarily dismisses its claims *with* prejudice, the defendant is generally considered a prevailing party. However, where a plaintiff voluntarily dismisses its claims *without* prejudice, there is no prevailing party because voluntary dismissal of the complaint without prejudice does not alter the legal relationship between the parties. However, an exception to this rule exists under Texas law when a party voluntarily dismisses its claims to avoid an unfavorable ruling on the merits.

The court concluded that KRG had not shown Stockade dismissed its claims to avoid an unfavorable ruling on the merits. The court did not credit KRG's argument that, given the timing and the court's previous denial of the motion for preliminary injunction, Stockade must have voluntarily dismissed its claims to avoid an unfavorable ruling on the pending motion to dismiss. The court noted that the standard for the preliminary injunction—likelihood of success on the merits—is more stringent than what is necessary to survive a motion to dismiss. The court made clear that a denial of a motion for preliminary injunction did not mean the court would grant a motion to dismiss. Stockade justified its dismissal on the basis that it was more cost efficient to consolidate all of its claims under the franchise agreement in the arbitration. As a result, the court held that KRG had not established that it was the prevailing party.

The court also provided other grounds for denying KRG's attorneys' fee motion. The court noted that franchise agreements only allowed for attorneys' fees for the party instituting the legal proceeding, and KRG was the defendant. As to the Texas Uniform Trade Secrets Act, the court found that KRG had not established that Stockade's trade secrets claim was entirely baseless or specious such that it could only have been brought in subjective bad faith or for other improper purpose. Finally, as to Rule 41(d), the court relied on the Rule's plain language to find that it only allows for recovery of attorneys' fees in the event of two sequential lawsuits and does not apply when one of the actions was an arbitration.

CLASS ACTIONS

Patel v. 7-Eleven, Inc., Bus. Franchise Guide (CCH) ¶ 16,234, 322 F. Supp. 3d 244 (D. Mass. July 20, 2018)

This case is discussed under the topic heading "Labor and Employment."

CONTRACT ISSUES

***Boston Tea Co., LLC v. Bay Valley, LLC*, Bus. Franchise Guide (CCH) ¶ 16,257, 2018 WL 4211313 (S.D.N.Y. Sept. 4, 2018)**

The U.S. District Court for the Southern District of New York granted in part Bay Valley, LLC's (Bay Valley) motion to dismiss Boston Tea, LLC's (Boston Tea) complaint.

Boston Tea filed suit against Bay Valley asserting claims for breach of contract and the implied covenant of good faith and fair dealing, unfair competition, misuse of confidential information, tortious interference with contract, and tortious interference with prospective business advantage, and seeking, among other things, injunctive relief and an accounting of Boston Tea's net sales and royalty calculations from 2014 through March 2017.

Boston Tea sells tea and related products under a number of trademarks. Bay Valley is a national provider of shelf-stable foods. In 2012, Boston Tea entered into a license agreement with North American Tea & Coffee Inc., which was ultimately acquired by Bay Valley's parent company.

The license agreement provided Bay Valley with an exclusive worldwide license to sell and distribute Boston Tea's products for a fifteen-year term and prohibited Bay Valley from entering into a sublicensing agreement without Boston Tea's written consent. Boston Tea also entered into an asset purchase agreement with Bay Valley's predecessor, which expressly stated that Boston Tea retained its ownership of its intellectual property and the goodwill associated with such intellectual property.

Boston Tea alleged that Bay Valley underreported the amount of tea that it sold and consequently underpaid royalties and provided inaccurate accounting records. Boston Tea also alleged that Bay Valley entered into an unauthorized sublicense agreement with a third party, MSRF. Boston Tea further alleged that MSRF knowingly injured Boston Tea's sales, customer relations, and goodwill by selling competing products. Furthermore, Boston Tea alleged that the price that MSRF used for calculating payments to Bay Valley was the raw cost of the products, which was essentially a wholesale price, and resulted in Boston Tea receiving less royalties than it would have if Bay Valley had sold directly to retailers. Ultimately, the license agreement was mutually terminated.

Boston Tea alleged that MSRF started disparaging its business in a series of communications to Boston Tea's customers (such as PriceSmart) before and after the license agreement was terminated, including telling the customers that Boston Tea was out of business and interfering with Boston Tea's relationship with Disney. Boston Tea also alleged that MSRF failed to fill numerous orders placed on Amazon, resulting in Amazon removing Boston Tea products from its website. Further, MSRF and Bay Valley allegedly told customers that they should order a different brand of tea. Boston Tea also alleged that Bay Valley and MSRF continued to sell Boston Tea products after the termination of the license agreement and that MSRF advised retailers to order their tea from MSRF instead of Boston Tea.

In addressing Bay Valley's arguments, the court considered whether Boston Tea's complaint contained sufficient factual matter, accepted as true, to state a plausible claim for relief.

With respect to Boston Tea's breach of contract and the implied covenant of good faith and fair dealing claim, Bay Valley raised a number of arguments, including that the license agreement did not include any express sale requirements. The court found this argument to be unpersuasive. The court considered the scope of the duty of good faith and fair dealing in this particular context and held that express limitations on marketing obligations do not eliminate a licensee's obligation to use reasonable marketing efforts. It was reasonable for Boston Tea to assume that Bay Valley would market, promote, and sell Boston Tea's product in such a way that the termination provision would not be triggered. In addition, the court found evidence of bad faith in that Bay Valley deliberately did not engage in certain obvious profit maximizing strategies, including selling directly to retailers, requiring a more favorable cost calculation from MSRF, or using Boston Tea's existing e-commerce infrastructure.

The court also considered whether the relationship between Bay Valley and MSRF could be characterized as an agency relationship, as well as whether the agreement between them was a "distribution agreement" or an unauthorized sublicensing agreement. The court determined that, for both of these issues, there were questions of fact that could not be resolved at the pleading stage.

On the unfair competition claim, the court found that the complaint included sufficient allegations to suggest that Bay Valley engaged in acts that resulted in some form of business injury. While the court noted that the bounds of unfair competition were uncertain, at least some jurisprudence spoke to acts other than palming off and misappropriation as potential valid bases for an unfair competition claim. The court also found that merely because the two parties were not direct competitors under the license agreement did not mean that the unfair competition claim must be barred.

As to the misuse of confidential information claim, the court held that while confidential relationships can arise contractually, it was not clear whether such a relationship existed between the parties and their "briefing left much to be desired." Accordingly, the court denied Bay Valley's motion as to this claim, indicating Bay Valley could renew its motion to dismiss with arguments that address whether a conditional asset purchase agreement creates a confidential relationship.

The court granted the motion to dismiss in part on the issue of tortious interference with contract because Boston Tea's complaint did not identify any specific contracts with third parties that it maintained while the license agreement was in effect. The court was unwilling to extend the claim to the contracts with Disney and PriceSmart that were "owned' by Bay Valley during the pendency of the license agreement. The court, however, allowed the allegations of tortious interference with prospective business to proceed, finding that although Boston Tea was not a party to contracts with

PriceSmart and Disney during the license agreement, it still had a business connection to these parties as they actively purchased Boston Tea's products. The court found that informing these parties that the plaintiff was out of business could be evidence of intentional interference.

Lastly, the court held that injunctive relief is not a cause of action, but rather a remedy, and therefore should be dismissed in this situation. The court also dismissed the accounting claim, finding that it did not need to exercise its equitable powers as the records Boston Tea sought would likely to be produced during discovery.

In sum, the court granted the motion to dismiss as to the accounting, injunctive relief, and tortious interference with contract claims, but denied the motion as to the tortious interference with prospective business, misuse of confidential information, unfair competition, breach of contract, and the implied covenant of good faith and fair dealing claims.

***Takiedine v. 7-Eleven, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,223, 2018 WL 3141461 (E.D. Pa. June 27, 2018)**

This case is discussed under the topic heading "Termination and Nonrenewal."

DAMAGES

***Entm't USA, Inc. v. Moorehead Commc'ns, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,239, 897 F.3d 786 (7th Cir. July 26, 2018)**

The U.S. Court of Appeals for the Seventh Circuit affirmed the district court's decision after a bench trial finding that a cellular phone services seller failed to quantify its damages with reasonable certainty from a master agent's breach of a referral agreement.

Entertainment USA, Inc. (Entertainment USA) was in the business of wholesaling and licensing cell phones through a network of affiliated dealers and retail stores in central Pennsylvania. In 2006, the stores affiliated with Entertainment USA offered their customers service contracts through several different carriers, including AT&T, Sprint, and TMobile. Moorehead Communications, Inc. (Moorehead) was a Verizon master agent based in Indiana who sought to expand its operations by signing up dealers with Verizon. At the time, Entertainment USA did not have a pre-existing relationship with Verizon and could not sell Verizon phones.

The parties prepared, without the assistance of counsel, a two-page referral agreement that connected Moorehead with a number of Entertainment USA's dealers and provided that Entertainment USA would receive a referral fee for two-year phone activations and two-year upgrades. Between 2006 and 2008, Moorehead paid in excess of $70,000 in referral fees to Entertainment USA. Moorehead discontinued the referral bonuses in 2008. One of the owners of Entertainment USA started a new company and proposed a new referral agreement, which Moorehead declined.

Four years after Moorehead stopped making payments under the referral agreement, Entertainment USA filed suit alleging breach of contract, requesting an equitable accounting, and claiming unjust enrichment on the ground that Moorehead continued to benefit from the referrals. After the lawsuit was filed, Moorehead paid an additional $52,000 to Entertainment USA and then answered the complaint claiming that Entertainment USA had been paid in full. After the parties filed crossmotions for summary judgment, the only remaining issues at trial involved determining the duration of the agreement, the precise meaning of the term "activations," and any additional "directly referred" locations beyond what was stipulated to Moorehead.

The district court found that the parties intended that the referral agreement "live on as long as any referred location was producing activations" and therefore found a breach of contract, but on a much narrower basis than alleged by Entertainment USA. The district court also found that Entertainment USA's claimed damages could not be disaggregated or recalculated to match up to its theory of liability, as it was presented in such a broad manner that the court could not identify the difference between what was paid and what was due under the referral agreement. The district court also found that other exhibits in the record were not informative as Entertainment USA's figures differed significantly from those of Moorehead and the numbers that Entertainment USA relied on were purportedly based on an additional six years of data not included in the record. Accordingly, the district court held that Entertainment USA had failed to prove its contract damages with reasonable certainty and awarded zero damages. And, for the same reasons, the district court denied Entertainment USA's request for an equitable accounting.

Entertainment USA appealed the district court's decision except for the dismissal of its unjust enrichment claim. The Seventh Circuit began by stating that the standard of review is one of clear error and that the issue on appeal was whether "a reasonable trier of fact could conclude that the proffered evidence falls short of proving damages with reasonable specificity" and not what it would have found had it been sitting at the trial level.

The Seventh Circuit rejected Entertainment USA's argument that the district court had all the information needed to recalculate damages, noting the deficiencies in the summary spreadsheets provided by Entertainment USA in its written closing argument. Although mathematical certainty is not required, the court held that there must be at least a reasonable estimate that is supported by a factual basis. The court agreed with the district court that Entertainment USA's evidentiary showing fell short of this threshold. Moreover, the court noted that neither Entertainment USA nor Moorehead provided citations to the docket or trial record, which made verification of the underlying damages methodologies impossible. Finding that Entertainment USA had failed to establish that the district court committed error, let

alone a clear error, in determining the damages award after a narrow finding of liability, the court affirmed that the a zero dollar award was appropriate.

The court then reviewed the district court's decision denying Entertainment USA's request for an equitable accounting under an abuse of discretion standard, as an action for an accounting is generally a proceeding in equity and addressed to the discretion of the trial court. The court held that Entertainment USA did not have an unequal means of knowledge during the discovery process; although the damages estimate was flawed, production of a flawed estimate does not itself necessarily entail an information asymmetry. Furthermore, the court found that the contractual arrangement did not establish a fiduciary relationship, which is typically the subject of an equitable accounting under Indiana law. The fact that the quantum of damages was difficult or impossible to measure and that the accounting information could have been revealed during discovery did not by themselves support finding an abuse of such discretion. Accordingly, the court affirmed the district court's decision denying an equitable accounting.

GOOD FAITH AND FAIR DEALING

***Boston Tea Co., LLC v. Bay Valley, LLC*, Bus. Franchise Guide (CCH) ¶ 16,257, 2018 WL 4211313 (S.D.N.Y. Sept. 4, 2018)**
This case is discussed under the topic heading "Contract Issues."

***Takiedine v. 7-Eleven, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,223, 2018 WL 3141461 (E.D. Pa. June 27, 2018)**
This case is discussed under the topic heading "Termination and Nonrenewal."

INJUNCTIVE RELIEF

***Handel's Enters., Inc. v. Schulenburg*, Bus. Franchise Guide (CCH) ¶ 16,215, 2018 WL 3097416 (N.D. Ohio June 22, 2018)**
The U.S. District Court for the Northern District of Ohio granted Handel's Enterprises, Inc's (Handel's) motion for injunctive relief against Kenneth Schulenberg (Schulenberg) and others arising from Schulenberg's breach of a covenant not to compete in the parties' franchise agreement.

Pursuant to a franchise agreement, Handel's granted Schulenburg the right to operate a Handel's ice cream in Encintas, California. Under the agreement, Schulenburg was assigned a territory with a three-mile radius and was granted the right to open a second location in downtown San Diego, California. Schulenburg agreed to maintain the confidentiality of Handel's proprietary information and not to compete with Handel's during the term of the franchise and for a two-year period after the termination of the agreement.

Shortly after opening the Encinitas store, Schulenburg and Handel's began to discuss opening a second store in downtown San Diego. Handel's ultimately did not approve the location proposed by Schulenburg. Schulenburg subsequently advised Handel's that he did not believe paying a second franchise fee for a location in downtown San Diego was logical and refused to provide Handel's with a copy of the final lease for the location or pay a franchise fee. In response, Handel's sent defendants a notice of breach.

Defendants then filed an action in California state court, alleging that Handel's had violated California franchise law. Handel's removed the case to the U.S. District Court for the Southern District of California and filed a separate lawsuit in the U.S. District Court for the Northern District of Ohio, asserting claims for violations of the Lanham Act, breach of contract, and misappropriation of trade secrets, and seeking a preliminary injunction against defendants related to the alleged misappropriation of trade secrets and breach of the covenant not to compete in the franchise agreement.

The franchise agreement included an Ohio choice of law clause and, although they argued that Ohio law should not apply, defendants apparently only analyzed Ohio law. The court applied the four traditional factors in determining whether to grant the requested injunction: (1) whether Handel's was likely to succeed on the merits; (2) whether Handel's would be irreparably harmed in the absence of injunctive relief; (3) whether the injunction would cause substantial harm to defendants; and (4) whether the public interest would be served by the issuance of an injunction.

In addressing the likelihood of success factor, the court separately considered Handel's trade secret and breach of the covenant not to compete claims. With respect to the trade secret claim, defendants argued that Handel's had failed to adequately identify the documents or information that was both confidential and misappropriated and, alternatively, that Handel's had failed to establish that such documents or information are trade secrets as defined by the Ohio Uniform Trade Secrets Act. The court disagreed, finding the allegations in Handel's complaint that its Operations Manual and "System" were trade secrets were sufficient, given that the information was only known to defendants by reason of the parties' franchise relationship. The court also found that Handel's had adequately established that it took appropriate precautions to maintain the confidentiality of the trade secret information. Without further analysis, the court concluded that Handel's had "presented a strong likelihood of success on the merits" of its trade secret claim.

The court also determined that Handel's was likely to prevail on its noncompete under Ohio law, which requires that the covenant goes no further than necessary to protect the legitimate interest of the party seeking to enforce the covenant, does not impose undue hardship on the person against whom the covenant would be applied and would not injure the public. The court noted that the covenant in the franchise agreement was reasonable in terms of its geographical scope (limited to the territory granted under the franchise agreement) and duration. The court further found that enforcing

the covenant would not injure the public as the public would not be deprived of ice cream if defendants were prohibited from competing with Handel's "during the duration of the agreement and for a short period of time *after* the [a]greement is terminated."

The court then turned to the irreparable harm factor, finding that Handel's had made a "strong showing" it would suffer irreparable harm in the absence of an injunction. Without identifying the evidence presented by Handel's, the court held that market confusion coupled with the loss of "fair competition" and damage to the relationships with other franchisees are the types of injuries for which monetary damages are difficult to calculate and that loss of goodwill from existing and prospective customers also constitutes irreparable harm.

With respect to the harm caused to defendants factor, defendants argued that they would suffer undue hardship if an injunction were issued because of their obligations under the lease and because they had invested substantial resources into opening their store in downtown San Diego. The court rejected these arguments, ruling this harm was "self-inflicted" and that defendants had prior notice Handel's would seek to enjoin the opening of the second store but nonetheless proceed with opening the store.

Finally, the court found that the public interest factor weighed in favor of granting the requested injunctive relief "because enforcement of contractual duties is in the public interest."

JURISDICTION

Pascarelli v. Koehler, Bus. Franchise Guide (CCH) ¶ 16,222, 816 S.E.2d 723 (Ga. Ct. App. 2018)

The Georgia superior court granted a motion to dismiss for lack of personal jurisdiction, concluding that the operation of a website did not give rise to sufficient minimum contacts with the state for the court to exercise jurisdiction over the defendant.

Plaintiffs Frank and Marina Pascarelli, residents of Georgia, filed suit in Georgia superior court against Marriott International, Inc. (Marriott), James Koehler, a Marriott franchisee in Caspar, Wyoming (Koelher), and others for negligence arising from injuries allegedly caused by bedbugs during Mr. Pascarelli's stay at the Caspar Marriott Courtyard Hotel while on business for the Centers for Disease Control. Pascarelli allegedly chose the Courtyard Hotel because it was a "preferred" hotel with the CDC and made his reservations online.

All defendants moved to dismiss the Pascarellis' claim on the ground of lack of personal jurisdiction. The court granted the motion as to all defendants with the exception of Marriott, finding that Koehler's Internet activity in Georgia did not establish the required minimum contacts to impose personal jurisdiction and, if even if it did, it would be contrary to the constitutional guarantee of due process to permit the Pacarellis to pursue their claims against

Koehler in Georgia. The Pasarellis' subsequently sought interlocutory review of the trial court's ruling with respect to Koehler. The appellate court concluded that the trial court did not err and affirmed the judgment.

The relevant facts were seemingly uncontested: (1) Marriott maintains a website which permits a prospective guest to review individual hotels and includes a centralized reservation system; (2) Koehler does not maintain his own website, and his individual marketing focuses on Wyoming and Colorado; and (3) from 2010 to 2013, residents of Georgia generated less than one percent of the annual revenue for Koehler's hotel.

As an initial matter, the court reviewed Georgia's Long Arm Statute and the generally applicable law, which collectively provide that: (1) Georgia may exercise personal jurisdiction over a nonresident where the nonresident transacts "any business" in the state; (2) this jurisdiction only reaches "to the maximum extent permitted by procedural due process"; and (3) due process is satisfied if the nonresident has purposefully done some act or consummated a transaction in the state, if the underlying claim arises from that act or transaction, and the exercise of jurisdiction "does not offend traditional fairness and substantial justice."

In Georgia, specific personal jurisdiction based on online interactions via an Internet website are evaluated on a "sliding scale" test in which the key inquiry is the degree to which the website is "passive," such that a defendant simply posts information on the website or "interactive" such that the "user can exchange information with the host computer" via the website. The court concluded that Marriott's website was "neither entirely passive nor entirely interactive," and therefore the court needed to examine the degree of interactivity and the nature of the commercial information exchanged on the website.

In analyzing Marriott's website, the court considered cases applying Georgia law and noted a distinction in cases in which goods are ordered through a website and then transmitted to Georgia. In those circumstances, the Georgia resident is able to bring about the transmission of goods into Georgia simply by placing an order via the website. The court distinguished this circumstance from a hotel website that enables an online reservation, but the resident must then travel outside the state to actually use the service provided by the hotel.

The court was also persuaded by the reasoning in cases from other jurisdictions involving a hotel's website in which the Internet "presence" with online reservation capabilities was found not to establish the requisite minimum contacts for tort claims occurring outside the forum. The court further noted the lack of evidence on whether Koehler advertised or otherwise sought business in Georgia.

***Servpro Intellectual Prop., Inc. v. Zerorez Franchising Sys., Inc.*, Bus. Franchise Guide (CCH) ¶ 16,227, 2018 WL 3364372 (N.D. Tenn. July 9, 2018)**

The U.S. District Court for the Northern District of Tennessee granted a motion to dismiss for lack of personal jurisdiction in an action against a

Nevada franchisor that had allegedly provided and used infringing materials on a franchisee's website. The defendant franchisee's separate motion to dismiss for failure to state a claim was granted as to the claim for induced trademark infringement, but was denied as to the trademark infringement and unfair competition claims.

Zerorez Franchising Systems, Inc. (Zerorez) sells goods and services in the carpet and living surface cleaning industry. Zerorez licenses its intellectual property to franchisees throughout the United States. Zeroholding, LLC (Zeroholding), a Nevada corporation, with a principal place of business in Tennessee, owns and operates one such franchise. Plaintiffs Servpro Intellectual Property Inc. and Servpro Industries, Inc. (collectively, Servpro) own the trademark on the phrase "Here to Help" in the fields of cleaning services and remediation.

Servpro alleged that a website controlled by Zerorez (the Nashville Website) displayed the phrase "ZEROREZ® Nashville Is Here To Help!" and infringes on Servopro's trademark. Servpro further alleged that Zerorez was liable for trademark infringement with respect to similar phrases that appeared on other Zerorez franchisees' websites that Zerorez controls and for inducing trademark infringement by providing the infringing material to its franchisees. Servpro alleged that Zeroholding was liable for trademark infringement because it purportedly benefits from the Nashville website and for inducing trademark infringement. Finally, Servpro alleged that both Zerorez and Zeroholding had violated Tennessee common law for unfair competition.

The court began by addressing Servpro's argument that Zerorez had waived the defense of personal jurisdiction by entering a general appearance based on *Gerber v. Riordan*, 649 F.3d 514 (6th Cir. 2011). The court dismissed Servpro's argument that *Gerber* creates a bright-line rule, holding that the relevant inquiry is whether Zerorez's "conduct prior to raising the defense has given the plaintiff a 'reasonable expectation' that the defendant will defend the suit on the merits" or whether Zerorez has caused the court to "go to some effort that would be wasted if personal jurisdiction is later found lacking."

The court then examined whether it had jurisdiction over the defendants. The court held that there must be personal jurisdiction as to each individual defendant and as to each asserted claim, and that a district court will look towards the applicable state long-arm statute to determine the appropriate limitations. The court then distinguished between general personal jurisdiction, where the claim does not need to arise from defendant's contacts within the forum state, and specific jurisdiction, where the claim arises from the defendant's contacts within the forum state. In either case, the plaintiff bears the burden of demonstrating jurisdiction by a preponderance of the evidence.

The court found that it lacked general jurisdiction for two reasons. First, Servpro's failure to argue in favor of general jurisdiction over Zerorez was

interpreted as a concession that there was no general jurisdiction. Second, Servpro did not allege that Zerorez had any connection with Tennessee beyond the connections related to this case, and such connections alone were not "continuous and systemic" enough to establish general jurisdiction because they occurred during a narrow period of time and only concerned Zeroholding and the Nashville Website.

The court also concluded that it lacked specific jurisdiction over Zerorez because none of the three required elements of specific jurisdiction was present, namely: (1) Zerorez purposefully availed itself of Tennessee; (2) Servpro's claims arose out of Zerorez's connections with Tennessee; and (3) the exercise of jurisdiction would be reasonable.

The "purposeful availment" element is analyzed under the "stream of commerce plus" inquiry, which requires that the defendant take actions "purposely directed toward the forum state." The evidence supported a finding that Zerorez only purposefully availed itself of doing business in Tennessee by registering the Nashville Website domain name and by agreeing to establish a franchise in Nashville. The court found that the remainder of the allegations in the complaint were either not supported by any evidence or not relevant to the purposeful availment analysis.

The court then addressed whether Servpro's cause of action "arose from" Zerorez's connections with Tennessee. The "arises from" element is subject to a lenient standard, requiring only that the cause of action have a substantial connection with the defendant's instate activities. The court found that while Zerorez's contacts with Tennessee were connected with Servpro's claims, the connections were too attenuated to be substantial. Although Zerorez registered the domain name and contracted to establish a franchisee prior to the appearance of the phrase "Here to Help" on the Nashville Website, the court held that it was otherwise not connected with that appearance. Furthermore, Zerorez did not control the content of the Nashville Website, and Zeroholding, which did control that content, was independently owned and operated. The court found it unnecessary to determine whether the element of reasonableness of exercising jurisdiction was satisfied.

The court then addressed Zeroholding's motion to dismiss Servpro's complaint for failure to state a claim upon which relief can be granted. To withstand a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to state a claim to relief that is plausible on its face.

The court first examined Zeroholding's arguments that there was no likelihood of confusion and fair use. The court held that they were affirmative defenses, which generally cannot form the basis for motion to dismiss and the exception to this rule—that the affirmative defense is apparent on the face of the complaint—was not applicable.

Zeroholding also argued that it was not liable for other defendants' and third parties' alleged use of the "Here to Help" trademark. Servpro did not oppose this argument, and the court determined that the complaint failed to allege vicarious liability or contributory liability against Zeroholding for the

actions of Zerorez or any other Zerorez franchises. The court therefore dismissed the claim against Zeroholding for induced trademark infringement.

LABOR AND EMPLOYMENT

A.H. v. The Wendy's Co., Bus. Franchise Guide (CCH) ¶ 16,251, 2018 WL 4002856 (M.D. Pa. Aug. 22, 2018)

The U.S. District Court for the Middle District of Pennsylvania denied a motion to dismiss the amended complaint of a cashier at a franchised Wendy's restaurant who claimed she was harassed and groped by a supervisor who later pled guilty to criminal assault.

The cashier filed suit against the franchisee, as well as the franchisor and its affiliates (collectively, the Wendy's Defendants), alleging claims under Title VII of the Civil Rights Act of 1964 (Title VII) and the Pennsylvania Human Relations Act (PHRA). The court denied the Wendy's Defendants' motion, finding that plaintiff had plausibly alleged both joint employer and agency theories of liability based on the contents of the franchise agreement and her specific allegations regarding the control exercised by the Wendy's Defendants. The court also held that plaintiff's claims were not barred for failing to exhaust her administrative remedies.

Plaintiff was hired as a cashier at a Wendy's restaurant owned and operated by Quality Served Fast, Inc. (QSF), a Wendy's franchisee. At the time, plaintiff was fifteen years of age. Her supervisor began making verbal sexual advances towards her shortly after she was hired, which subsequently turned physical. This conduct continued for several months until plaintiff's father contacted the police. The supervisor was arrested and ultimately pled guilty to harassment and disorderly conduct.

In May 2017, the employee filed a discrimination claim with the Equal Employment Opportunity Commission (EEOC) and the Pennsylvania Human Relations Commission naming the franchisee and the Wendy's Defendants as respondents. In its letter acknowledging receipt of the claim, as well its subsequent Notice of Right to Sue, the EEOC identified the respondent as "Quality Served Fast, Inc. D/B/A Wendy's." The employee then filed suit, asserting claims against, among others, the Wendy's Defendants in their capacity as alleged employers under Title VII and the PHRA. The Wendy's Defendants moved to dismiss plaintiff's claims on the ground that, as the franchisor, they were not plaintiff's employer.

Both Title VII and the PHRA define employers generally based on the number of persons employed (fifteen or more under Title VII and four or more under the PHRA). Although plaintiff was directly employed by QSF, she argued that she was also employed by the Wendy's Defendants under joint employer and agency theories of liability.

A joint employment relationship exists when a party retains sufficient control over the terms and conditions of the employment of employees who are employed by another employer. In determining whether such a relationship

exists, the court considers three main factors, though each need not be present: "(1) authority to hire and fire employees, promulgate work rules and assignments, and set conditions of employment, including compensation, benefits, and hours; (2) day-to-day supervision of employees, including employee discipline; and (3) control of employee records, including payroll, insurance, taxes, and the like."

With respect to the first factor, plaintiff alleged that she was required to sign a conduct policy that identified activities that the Wendy's Defendants considered "to be a business abuse or contrary to acceptable business practice." She also had to sign several other policies identified as Wendy's rules and regulations. Additionally, the franchise agreement provided that the "Franchisee shall operate the Restaurant in strict conformity with such methods, standards, and specifications as Franchisor may from time to time prescribe in the Manual or otherwise in writing." The court that these allegations were sufficient at the pleading stage to suggest that the Wendy's Defendants set the conditions of employment and workplace rules.

As to the second factor, plaintiff alleged that at the onset of her employment she was required to undertake a training course "authored" by the Wendy's Defendants and that the Wendy's Defendants provided continual in-service training of employees. Additionally, the Wendy's Defendants had the right under the franchise agreement to conduct periodic inspections and provide advisory assistance per the terms of the franchise agreement.

For the final factor, plaintiff argued the franchise agreement required the Wendy's Defendants to provide QSF with reporting forms for use in operation of the business and gave the Wendy's Defendants the right to examine the franchisee's "books, records, and tax returns," suggesting some control over employee records.

Weighing all three factors, the court concluded that the employee had stated enough facts to establish a basis for finding that the Wendy's Defendants were her joint employer.

The court next addressed plaintiff's agency theory. An agency relationship, similar to a joint employer relationship, is established when a third party has a right to control an employee's conduct either directly or through the third party's control over the employee's employer. In the franchisee-franchisor context, the court looks to the nature and extent of control set forth in the franchise agreement and the parties' practice. Based on its analysis of plaintiff's joint employer theory of liability, along with the franchise agreement's "nebulous and generally phrased" provisions that provide the Wendy's Defendants with broad discretionary powers over the franchisee, the court held that plaintiff had also adequately alleged claims based on an agency theory of liability.

Finally, the court briefly addressed whether plaintiff had exhausted her administrative remedies prior to filing suit. The Wendy's Defendants argued that the Right to Sue letter issued by the EEOC only extended to QSF, even though that the employee expressly named the Wendy's Defendants in the

charge submitted to the EEOC. The court refused to penalize plaintiff for the EEOC's failure to specifically identify the Wendy's Defendants in the Right to Sue letter.

***Flores de Jesus v. Subway IP Inc.*, Bus. Franchise Guide (CCH) ¶ 16,233, 2018 Wage & Hour Cas. 2d (BNA) 254,060 (S.D.N.Y. July 17, 2018)**
The U.S. District Court for the Southern District of New York granted a motion for leave to file an amended complaint by a former employee of a Subway franchisee seeking monetary damages for alleged violations of the Federal Labor Standards Act (FLSA) and New York Labor Law (NYLL). According to plaintiff, he and others were not paid minimum wage, overtime, and "spread of hours" pay when required. Plaintiff further alleged that tips were withheld during certain circumstances and that defendants violated wage statement, notice, and recordkeeping provisions of the NYLL.

During the deposition of defendant Subway IP, Inc.'s (Subway) Federal Rule of Civil Procedure 30(b)(6) designee, plaintiff learned that Franchise World Headquarters (FWH) and Doctor's Associates Incorporated (DAI), two wholly owned subsidiaries of Subway, may be liable as "franchisor employers." Plaintiff sought to file an amended complaint adding FWH and DAI as defendants.

Federal Rule of Civil Procedure 15(a) provides that leave to amend a pleading will be freely granted "when justice so requires." Although this threshold is low, leave may be denied if the non-moving party establishes "undue delay, bad faith or dilatory motive on the part of the movant, repeated failure to cure deficiencies by amendments previously allowed, undue prejudice to the opposing party by virtue of allowance of the amendment, futility of the amendment, etc." Here, FWH and DAI argued that plaintiff's proposed amendment should be denied on the basis that he unduly delayed in seeking to add them to the lawsuit and that the amendment would be futile.

In considering whether a plaintiff has unduly delayed in seeking an amendment, the plaintiff is expected to provide an explanation for the delay, although the mere fact that the plaintiff could have moved earlier is insufficient to establish undue delay. Here, while plaintiff waited until the completion of the deposition which resulted in his discovery of FWH and DAI's potential liability and their purported role in the franchisee's business, the deposition was adjourned twice at Subway's request, and the deposition in question occurred at the end of the discovery period. The court accepted the plaintiff's explanation that he waited for the deposition to conclude, so he could review the transcript and determine which facts support the proposed amendment. Although Subway argued that plaintiff should have been aware of FWH and DAI earlier in the matter, the court accepted that plaintiff was within his rights to confirm FWH and DAI's role through the testimony of the Rule 30(b)(6) designee.

The court then addressed whether the delay in seeking to amend the complaint prejudiced defendants. In analyzing potential prejudice, the court

considers whether the amendment will require the opponent to expend significant additional resources for discovery and trial, significantly delay the resolution of the matter as a whole, or prevent the plaintiff from bringing a timely action in another jurisdiction. Given that neither a summary judgment briefing schedule nor a trial date had been set, the court found that the amendment would not significantly delay the resolution of the matter. And although defendants argued that the amendment would necessitate further discovery, the court held that this fact on its own cannot justify denying leave.

With respect to the futility argument, the court analyzed "whether the amendment states a claim upon which relief can be granted." In the context of a franchisor-franchisee relationship under the FLSA, a plaintiff must allege sufficient facts to suggest that the franchisor exerted control over plaintiff's employment at the franchised business. Control can be formal or functional. In his proposed amended complaint, plaintiff alleged various ways in which FWH and DAI exercised control over the Subway franchise and its employees:

> [They] benefitted from Plaintiff's work, maintained the authority to inspect the Subway franchise where he worked, maintained the right to terminate the franchise for violation of the franchise agreement and/or for violation of the law, guided franchisees in how to hire and train employees, maintained requirements as to layout, provided materials for franchisees to give to employees directing them how to perform their jobs, and had the ability to review records as to the records of hours and wages worked by employees such as Plaintiff.

The court explained that these allegations were sufficient to plausibly establish that FWH and DAI exercised formal control over employment such that they could be held liable as employers. Therefore, the court held that the proposed amendment was not futile.

***McDonald's USA, LLC, A Joint Employer, et al. and Fast Food Workers Committee and Service Employees International Union*, Bus. Franchise Guide (CCH) ¶ 16,232 (N.L.R.B., Div. of Judges New York Branch Office July 17, 2018)**

In an exhaustive order, Administrative Law Judge Esposito (ALJ), on behalf of the U.S. National Labor Relations Board (NLRB), denied motions to approve settlement agreements between the General Counsel of the NLRB (General Counsel), McDonald's USA, LLC (McDonald's), and multiple McDonald's franchisees.

The underlying case raised a number of issues. The core issue, however, was whether McDonald's, as a franchisor, is a joint employer of the employees of its franchisees. The General Counsel based its joint employer allegations on alleged retaliatory actions due to employee participation in the "Fight for $15." According to the NLRB, McDonald's had "coordinated and directed the activities of its franchisees' response to the Fight for $15 campaign, which included the violations of the [National Labor Relations] Act alleged here." The NLRB alleged that McDonald's sought to protect its

own and its franchisees' "mutual interest in warding off union representation" from the employees and did so by providing resources and support for franchisees throughout the country in a way that made McDonald's a joint employer.

In deciding whether to approve the settlement agreements, the ALJ first went through, in exhaustive detail, the procedural history of the case, including a discussion of the 150 days of hearings that had occurred. It noted that McDonald's and the franchisees had raised evidentiary issues that "have been simply extraordinary," elaborating that "McDonald's took deliberate strategic positions regarding evidentiary and procedural issues that obstructed the creation of the record and prolonged the hearing." Examples included the refusal of McDonald's to present more than one witness per day, even where the individual witness testified for two hours or less, the unilateral cancellation of pre-scheduled hearing dates by McDonald's, and the taking of extreme positions by McDonald's regarding document authentication, even for documents that it had produced. At the time the parties submitted the informal settlement agreements for approval, just a few hearing days remained.

A. *The Settlement Agreements*

The settlement agreements require the posting of a notice in English at the franchisees' locations, along with mailing notice of the settlement to the last known addresses of former employees employed within the prior six months. It provided compensation for twenty individuals who had brought discrimination complaints, including back pay and future pay for three discriminatees who had lost their jobs.

The settlement agreements also included a process for addressing alleged breaches of the settlement occurring within nine months after of approval. The process allowed both McDonald's and the franchisee an opportunity to cure, but if the breach was not cured, a complaint would be filed/amended before the NLRB to include both the new allegations and allegations regarding joint employer status. In addition, a "Special Notice" would be mailed to the last known address of all of the franchisees' employees alerting them to the new allegations. As discussed below, it was unclear what role McDonald's was to play in curing any alleged noncompliance.

The settlement agreements called for the creation of a $250,000 settlement fund to be used "for the benefit of any and all potential discriminatees who may be entitled to a monetary remedy" after a breach. However, according to the ALJ, there was a lack of clarity regarding McDonald's role in establishing and overseeing the fund. There was also a lack of clarity regarding the discretion that McDonald's had in making payments out of the fund. If money still remained in the fund at the end of fifteen months, it would revert to McDonald's.

Finally, the settlement agreements required the General Counsel to request the withdrawal of the complaint within ten days of the settlement agreements being approved.

B. *Evaluating the Settlement Agreements*

To evaluate the informal settlement agreements, the ALJ applied the analysis set out in *Independent Stave Co.*, 287 NLRB 740 (1987). Under this analysis, the Board evaluates

> all the surrounding circumstances including, but not limited to, (1) whether the charging party(ies), the respondent(s), and any of the individual discriminatee(s) have agreed to be bound, and the position taken by the General Counsel regarding the settlement; (2) whether the settlement is reasonable in light of the nature of the violations alleged, the risks inherent in litigation, and the stage of the litigation; (3) whether there has been any fraud, coercion, or duress by any of the parties in reaching the settlement; and (4) whether the respondent has engaged in a history of violations of the Act or has breached previous settlement agreements resolving unfair labor practice disputes.

Regarding the first prong, the ALJ noted that the position of the General Counsel is nondispositive. Furthermore, while the General Counsel was supportive of the proposed settlement agreements, the ALJ gave that position no weight because there was an apparent disagreement between the parties regarding the exact terms of the proposed settlement agreements. Considering this disagreement, the ALJ questioned whether a meeting of the minds had even occurred.

With respect to the second prong, the ALJ found that the settlement agreements were not reasonable based on the nature of the allegations, the risks of litigation, and the state of the litigation involved. The ALJ considered the remedial effect of the settlement agreements on McDonald's, concluding that it did not "constitute anything approaching" the effect of a finding of joint employer status. The ALJ compared the settlement agreements to a settlement approved in an unrelated case where the alleged joint employer had agreed to act as "guarantor" of its subsidiary. There was nothing approaching a guarantee present here, and that weighed against approval of the settlement.

McDonald's argued that a guarantee would be inappropriate in this case, given that its relationship with its franchisees is very different from a relationship with a wholly owned subsidiary. The ALJ did not find this argument persuasive. Instead, he determined that McDonald's had the authority necessary to guarantee the franchisees' performance under the settlement agreements because the franchise agreements gave McDonald's the right to inspect the restaurants and to terminate noncomplying franchisees. The ALJ was also troubled by McDonald's positions that it could control the settlement fund but that it had no control over the franchisees' behavior.

Next, the ALJ found that the settlement agreements were not reasonable because they were enforceable only through a complicated default process. As a result, the enforceability of the settlement agreements was substantially less effective than an ALJ or NLRB order. The ALJ also questioned the form of the settlement agreements because, in the eyes of the ALJ, McDonald's was a "repeated offender" due to prior violations by one of its subsidiaries.

The ALJ disapproved of the provision of the settlement agreements requiring the General Counsel to withdraw the complaints within ten days of the approval of the settlement. This practice was not in keeping with usual NLRB procedure, which would be for the General Counsel to indefinitely adjourn the case until after McDonald's had fully complied with the terms of the settlement. Given the status of the case, including the "unprecedented and enormous resources expended," the ALJ felt that an informal settlement with unusual procedures was manifestly unreasonable.

The ALJ further concluded that the settlement agreements were unreasonable because they were unlikely to completely resolve the action. The complicated default process, already evident in disagreements regarding the obligations of the parties under the settlement agreements, and the history of the litigation itself, caused the ALJ to believe it was inevitable that the settlement agreements as proposed would encourage future litigation.

In analyzing the settlement agreements, the ALJ also criticized the provisions requiring notice of a breach. First, the ALJ highlighted that the notices would include only the allegations of breach and none of the allegations of the underlying action. Second, the notices did not contain the specific remedial assurances usually seen in notices. Third, the notices contained nonadmissions clauses, in which McDonald's disclaimed being a joint employer. The NLRB, however, does not allow these kind of clauses in NLRB notices to employees "under any circumstances." Fourth, the methods of disseminating the notices were inadequate—there was no requirement for electronic posting of the notices via e-mail, intranet, or Internet. Finally, the ALJ noted that the settlement agreements were not materially different than prior settlement offers, and noted that, if approved, the settlement agreements meant that the three-year, 155-day proceeding had served no purpose.

The ALJ next considered McDonald's conduct. It concluded that McDonald's conduct weighed against approving the settlements. According to the ALJ, it was no mere bystander to the allegations at issue in the case. Instead, evidence showed that McDonald's had actively coordinated with its franchisees to respond to the "Fight for $15." Yet, the settlements placed very little onus on McDonald's.

The risks of litigation also weighed against finding that the settlement agreements were reasonable. The case, to date, was already "the largest case ever adjudicated" by the NLRB. Thus, the ALJ commented that the "General Counsel's decision to pursue settlement, and accept the Settlement Agreements . . . literally days before the close of the monumental record in this case is simply baffling." Furthermore, the testimony yet to be adduced would be crucial to McDonald's position that its actions had been for "brand protection."

While the case was pending there had been several changes in the state of the law regarding not only joint employer status but also the burden of the General Counsel to prove joint employer status. In February 2018, the NLRB had reinstated a standard that was highly advantageous to the General

Counsel's case. Under the *Browning-Ferris* standard, the General Counsel did not need to prove McDonald's "actual exercise, as opposed to possession, of authority over terms and conditions of employment" at the franchisees' locations and did not need to show "direct and immediate" control over the employees. As a result of this change, the General Counsel was in a better position to establish joint employer liability and, therefore, should have been disincentivized from settling based on terms similar to those offered before the law changed. The ALJ said, in light of these risks, it was unclear why the General Counsel would accept such a paltry settlement.

The ALJ did concede that the settlement agreements adequately compensated the individual discriminatees. However, the General Counsel had not brought the action to remedy the claims of the individual discriminatees. Instead, the General Counsel brought the case mainly to resolve the question of whether McDonald's was a joint employer with all of its franchisees. Indeed, the vast majority of the evidence presented had been about the joint employer issue. "Thus, while approval of the Settlement Agreements would result in immediate relief for the alleged discriminatees, the remainder of the proposed settlement is paltry and ineffective given the scope of the allegations, the resources necessary in order to present the case, and the case's ultimate purpose." After considering each of these grounds, the ALJ determined that the settlement agreements were not a reasonable resolution of the case and found the second prong of the *Independent Stave* analysis weighed against approving the settlements.

The ALJ found that the third and fourth prongs of the *Independent Stave* analysis weighed in favor of approving the settlement agreements. There was no contention or evidence of fraud, coercion, or duress in reaching the settlement agreements. Furthermore, there was no prior history of violations.

Based upon its lengthy analysis, and in particular the first and second prongs of the *Independent Stave* analysis weighing against approval, the ALJ refused to approve the settlement agreements and ordered that the proceedings should continue.

***Patel v. 7-Eleven, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,234, 322 F. Supp. 3d 244 (D. Mass. July 20, 2018)**

The U.S. District Court for the District of Massachusetts addressed four motions. First, the court denied a motion to remand a case, concluding that non-diverse plaintiffs were fraudulently joined in order to preclude federal jurisdiction. Second, the court also denied the corporate defendant's motion to dismiss. Third, the court granted the individual defendants' motion to dismiss. Finally, the court denied the class plaintiffs' motion for injunctive relief, seeking to prevent the defendants from obtaining releases from individual class members.

Several Massachusetts 7-Eleven franchisees filed a putative class action against 7-Eleven, Inc. (7-Eleven) and two 7-Eleven market managers in Massachusetts Superior Court, alleging violations of the Massachusetts

Independent Contractor Law, Massachusetts Wage Act, and Massachusetts Minimum Wage Law. 7-Eleven subsequently removed the case to the U.S. District Court for the District of Massachusetts. The gist of plaintiffs' claims was that they and other Massachusetts 7-Eleven franchisees who performed "services as store managers and convenience store clerks" were wrongfully misclassified as independent contractors instead of as employees and were, therefore, deprived of benefits to which they were entitled under Massachusetts law, including a minimum wage and protection from improper wage deductions.

Before the court were four motions: (1) plaintiffs' motion to remand; (2) 7-Eleven's motion to dismiss plaintiffs' Minimum Wage Law claim; (3) the individual defendants' motion to dismiss; and (4) plaintiffs' emergency motion to enjoin 7-Eleven from obtaining releases from the putative class members.

In their motion to remand, plaintiffs argued that removal was improper because the individual defendants defeated diversity jurisdiction and the "local controversy" exception to the Class Action Fairness Act (CAFA) applies such that there is no federal question jurisdiction. In response, 7-Eleven asserted that the individual defendants were "middle managers" who were "fraudulently joined" so as to defeat diversity jurisdiction and that their actions were too insignificant to implicate the local controversy exception.

Under the fraudulent joinder doctrine, a plaintiff cannot destroy diversity jurisdiction by joining a "makeweight, non-diverse" defendant. The allegations in the complaint involving the individual defendants were limited to their residence, job title, and assertion that they "exercised extensive control over the plaintiffs' work." And the complaint did not seek any relief from either of the individual defendants. Further, under the Massachusetts Independent Contractor Law and Wage Act, individuals are only liable if they have responsibilities "similar to those performed by a corporate president or treasurer." The court found that allegations against the individual defendants were insufficient to state a claim under any of the relevant statues and did not satisfy the requisite pleading requirements. Accordingly, the court concluded that the individual plaintiffs were fraudulently joined and that diversity jurisdiction existed, and thus denied the motion to remand. Because the court found that there was diversity jurisdiction, it declined to address the parties' arguments regarding CAFA's local controversy exception.

In support of its motion to dismiss, 7-Eleven argued that plaintiffs did not adequately plead that any plaintiff had ever received less than the minimum wage. The court disagreed, finding that the complaint included allegations that plausibly supported their claim that they were employees rather than independent contractors and further alleged that franchisees frequently worked more than fifty hours per week and that their take-home pay was less than minimum wage. In addition, the complaint alleged that 7-Eleven deducts various fees and payments from plaintiffs' "wages." Based on these allegations, the court found that they were not so "threadbare or speculative

that they fail to cross the line between the conclusory and factual" and therefore were sufficient to state a plausible claim for relief. As a result, the court denied 7-Eleven's motion to dismiss.

The individual defendants' motion to dismiss fared better. As noted above, the complaint alleged no facts against the individual defendants other than their place of residence, job title, and that they "exercised extensive control over the plaintiffs' work." The court found that these allegations were insufficient to allow it to "draw the [necessary] reasonable inference that the defendant is liable for the misconduct alleged." And because plaintiffs were unable to identify any facts that they could allege if granted leave to amend that would state a cognizable claim for individual liability, the court found that it would be futile for plaintiffs to amend their complaint and, therefore, dismissed the claims against the individual defendants with prejudice.

The court then turned to plaintiffs' motion to enjoin 7-Eleven from obtaining releases from potential class members. The 7-Eleven franchise agreements provided that franchisees must, among other things, execute a general release as a condition to renewing their franchise. Beginning in 2019, 7-Eleven intended on providing franchisees with a new form of franchise agreement in which most franchisees would pay an increased amount to 7-Eleven (the 7-Eleven Charge). Shortly after plaintiffs' lawsuit was filed, 7-Eleven distributed 2019 renewal agreements to all of its Massachusetts franchisees, including franchisees whose agreements were not terminating in 2019. That document included a comprehensive general release of claims, including any claims arising under the statutes at issues in plaintiffs' lawsuit, and it specifically stated that the claims asserted in the lawsuit would be released. 7-Eleven also informed its franchisees that, as an alternative to the normal renewal process, it would offer its existing franchisees the option to maintain their current 7-Eleven Charge for an additional term. Plaintiffs contended that this proposal was intended to "coerce" putative class members into waiving their rights under the Massachusetts Wage Act "in exchange for the promise that 7-Eleven would not punish them in the future" by requiring them to pay the increased 7-Eleven Charge.

The court started its analysis by noting that courts have both a duty and broad discretion to exercise control over a class action so as to prevent potential abuse. The court also noted that an attempt to circumvent the Massachusetts Wage Act would constitute a serious potential abuse, that contracts that release or waive wage claims are subjected to heightened scrutiny, and that, if plaintiffs were to prevail on their claims, the purported release would be void. Nonetheless, the court denied plaintiffs' motion to enjoin 7-Eleven from obtaining releases from the putative class members.

As an initial matter, the court found that release was adequately supported by consideration because 7-Eleven is not required to renew its franchise agreements with any franchisee and was not threatening to terminate any existing agreements. The court further found that plaintiffs had not established that the requested injunctive relief was necessary because (1) if

plaintiffs were to prevail at trial, the court could award them damages, and (2) the court could invalidate releases at any stage of the proceeding. Thus, the court concluded that monetary damages and posttrial injunctive relief would make the plaintiffs whole. In dicta, however, the court expressed its "serious concerns" about the release, which it construed as applying to future wage claims and thus was arguably unenforceable. The court elected not to further address that issue because it was not before the court and would ripen only if plaintiffs were to prevail on their claims.

NONCOMPETE AGREEMENTS

Handel's Enters., Inc. v. Schulenburg, Bus. Franchise Guide (CCH) ¶ 16,215, 2018 WL 3097416 (N.D. Ohio June 22, 2018)

This case is discussed under the topic heading "Injunctive Relief."

ORAL AGREEMENTS

JTH Tax, Inc. v Aime, Bus. Franchise Guide (CCH) ¶ 16,245, 2018 WL 3770028 (4th Cir. Aug. 8, 2018)

In an unpublished opinion, the U.S. Court of Appeals for the Fourth Circuit reversed the district court's finding that a franchisee was entitled to recover lost profits from JTH Tax Inc. and SiempreTax + LLC (collectively, Liberty Tax). The court also affirmed the district court's decision rejecting the franchisee's fraud claim.

Liberty Tax offers tax preparation and filing services to customers through franchises across the United States. Gregory Aime and related entities (Aime) operated nine tax preparation businesses in the New York City area pursuant to franchise agreements with Liberty Tax. Under the agreements, Aime was required to maintain an Electronic Filing Identification Number (EFIN) from the IRS, which was necessary to file customers' tax returns electronically.

The IRS suspended Aime's EFIN in January 2016 due to suspected fraudulent activity. Although it had the contractual right to do so, Liberty Tax elected not to terminate its agreements with Aime. Instead, Liberty Tax and Aime entered into an agreement (PSA) pursuant to which Liberty Tax purchased and assumed control over Aime's business for approximately $1.1 million. The contract provided Aime with the option to buy back his business pursuant to a "separate purchase and sale agreement between the parties," subject to Liberty Tax's "standard sales and approval process" if Aime obtained a new EFIN by a specific date.

John Hewitt, the President and CEO of Liberty Tax, learned from one Aime's former employees whom Liberty Tax had hired to oversee the businesses that Aime was unlikely to be able to meet the buyback deadline. Hewitt told the employee that he would extend the deadline and, at Hewitt's request, the employee communicated the extension to Aime.

Liberty Tax and Aime's relationship deteriorated, and both parties brought claims for breach of the PSA. Aime also alleged that Liberty Tax committed fraud in agreeing to extend the buyback deadline without intending to permit him to repurchase the franchises. While the litigation was pending, Aime received a new EFIN prior to the extended buyback deadline.

Following a bench trial, the district court held that Liberty Tax was the party that first breached the PSA by failing to pay rent and expenses related to the franchises, and the court extended the deadline for Aime to repurchase his franchises through Hewitt's communication to the employee. The court awarded approximately $2.75 million dollars to Aime, which included lost profits and certain expenses that Liberty Tax owed under the PSA. The court denied Aime's fraud claim on the ground that it was not sufficiently distinct from the breach of contract claims, as well as his claims for punitive damages and attorney's fees.

Both parties appealed—Liberty on the judgment in favor of Aime and Aime on the district court's denial of his fraud claim and attorney's fees. The Fourth Circuit held that although the district court did not err in determining that Liberty Tax had breached the PSA, it had erred in determining that Aime was entitled to lost profits based on the purported extension of the buyback deadline.

The central issue on appeal was whether the extension of the buyback deadline in the PSA was valid. Under Virginia law, an extension of an option requires "some new and sufficient consideration." The court found that the consideration on the part of Liberty Tax was the promise to extend the buyback deadline, but there was no corresponding promise on Aime's part.

Aime argued that he had provided consideration for the buyback extension in three respects: (1) paying certain expenses and utilities relating to the franchises and a call center because Liberty Tax was obligated to pay these items; (2) paying rent for the franchises beyond the initial buyback deadline contained in the PSA; and (3) his additional efforts to secure a new EFIN, which would not have occurred had there not been an extension offered by Liberty Tax.

The court found that Aime had no independent obligation to perform any of these acts, and that none of them could serve as consideration because no evidence suggested that they were bargained for. The court also held that Aime's claim that it was obvious and foreseeable he would undertake these steps in light of the deadline extension did not constitute consideration, but rather potentially promissory estoppel, and that a cause of action for promissory estoppel is not recognized under Virginia law.

The court distinguished similar cases on the ground that the parties' conduct in those cases amounted to a reciprocal exchange of promises, even if attenuated, which was the element lacking in this case. The court thus ruled that Liberty Tax's offer to extend the deadline was in effect an unenforceable gratuitous promise.

The court then addressed Aime's cross-appeal of the dismissal of his fraud claim against Liberty Tax. Under Virginia law, fraud in the inducement occurs when a party to a contract makes a false representation of a material fact, constituting an inducement to enter into the contract on which the other party had a right to rely. However, the misrepresentation must be of a pre-existing fact and cannot ordinarily be predicated on unfulfilled promises or statements as to future events. The court held that the evidence did not reflect a misrepresentation by Liberty Tax of a preexisting fact before entering into the PSA with Aime, despite Liberty Tax's subsequent mischief. For these reasons, the court affirmed the district court's decision rejecting Aime's fraud claim.

The court concluded by affirming the damages awarded by the district court flowing from Liberty Tax's breach of the PSA by failing to pay or reimburse certain expenses related to the businesses. However, because the court held that there was no valid extension of the buyback deadline, Aime was not entitled recover any lost profits resulting from Liberty Tax's refusal sell back the franchises. Accordingly, the case was remanded to the district court to enter damages consistent with this decision.

RELEASES

***Patel v. 7-Eleven, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,234, 322 F. Supp. 3d 244 (D. Mass. July 20, 2018)**

This case is discussed under the topic heading "Labor and Employment."

STATUTE OF LIMITATIONS

***Heiman v. Bimbo Foods Bakeries Distrib. Co.*, Bus. Franchise Guide (CCH) ¶ 16,255, 902 F.3d 715 (7th Cir. 2018)**

In this case, the Seventh Circuit affirmed the U.S. District Court for the Northern District of Illinois's decision that the claims brought by JTE, Inc. (JTE) against Bimbo Foods Bakeries Distribution Co. (Bimbo Foods) were barred by the applicable statute of limitations.

Bimbo Foods sells baked goods. For a number of years, John Heiman and then later his company, JTE, distributed products for Bimbo Foods in the Chicago area. The parties' agreement had no fixed duration and included a New York choice of law provision. According to JTE, the parties' relationship took a turn for the worse in 2008 when Bimbo Foods started to fabricate curable breaches in an effort to force JTE out as the distributor, including filing false reports regarding out-of-stock items and poor customer service. JTE also alleged that on occasion Bimbo Foods employees removed products distributed by JTE from store shelves, photographed the empty shelves as evidence of a breach, and then replaced the products. When confronted about these actions, Bimbo Foods promised JTE that the "misconduct"

would not be repeated. Notwithstanding, Bimbo Foods allegedly continued to engage in such conduct. In 2011, after JTE refused to sell its distribution rights, Bimbo Foods unilaterally terminated the parties' agreement based on JTE's purported breaches of the agreement. Shortly afterwards, Bimbo Foods allegedly forced JTE to sell its distribution rights to a third party,

Heiman and JTE filed suit against Bimbo Foods in May 2017 alleging claims for breach of contract and tortious interference with contract. In response, Bimbo Foods filed a motion to dismiss based on Federal Rule of Civil Procedure 12(b)(6) on the grounds that (1) Heiman was not a real party in interest because he was not a party to the distribution agreement, and (2) the statute of limitations had run on JTE's claims. The district court agreed. JTE then appealed the court's rulings with respect to the statute of limitations.

The Seventh Circuit started with JTE's breach of contract claim and first addressed whether the law of Illinois or New York applied. The court noted that Illinois generally honors choice of law provisions for purposes of determining parties' substantive legal rights, but views statute of limitations to be procedural in nature and, therefore, governed by Illinois law.

The statute of limitations in Illinois for breach of a written contract is ten years, unless the action is based on the sale of goods, in which case the statute of limitations is four years. The parties agreed that JTE's breach of contract claim accrued in October 2011. Thus, the key issue was whether the distribution agreement was a contract for services, in which case JTE's breach of contract claim was timely, or a contract for the sale of goods, in which case JTE's claim was barred. JTE argued that the question of whether the agreement was for the sale of goods or services was a substantive question and, therefore, governed by New York law. The court disagreed, finding that the question was not one of contract interpretation, but one of statutory interpretation and, thus, Illinois law applied. Under Illinois law, as well as New York law, courts look to the "primary purpose" of the contract to determine which statute of limitations applies. The court noted that "'virtually every jurisdiction that has addressed this issue' has concluded that dealership agreements are 'predominantly for the sale of goods'" and found that JTE had failed to explain how or why the agreement with Bimbo Foods was distinguishable. Accordingly, because the agreement was for the sale of goods, the court held that JTE's breach of contract claim was time-barred.

The court then turned to JTE's tortious interference claim. The parties agreed that the statute of limitations for such claims is five years, but disagreed as to when JTE's claim accrued. JTE argued that its claim did not accrue until it had discovered the "full extent" of Bimbo Foods' misconduct in 2014 based on Illinois's fraud-discovery rule. Bimbo Food argued that JTE admitted that it knew the claimed breaches of contract were false as of 2011 and, therefore, could not rely on the fraud-discovery rule to toll the statute of limitations. The court agreed with Bimbo Foods, finding that JTE was not disputing that it may have been damaged, but "only that it could

not be sure." In fact, JTE knew Bimbo Foods had engaged in "wrongful conduct" at the time of the forced sale in 2011. And under Illinois law, the fraud-discovery rule does not apply if there is "some indication of wrongdoing." The court thus held that JTE knew or should have known of its right to sue Bimbo Foods, but instead "slumbered on its" rights, and so its tortious interference claim was also barred by the statute of limitations. In dicta, the court also noted that JTE's tortious interference claim was defective because a party cannot interfere with its own contract.

STATUTORY CLAIMS

***GJ&L, Inc. v. CNH Indus. Am., LLC*, Bus. Franchise Guide (CCH) ¶ 16,229, 2018 WL 3349700 (S.D. Ga. July 9, 2018)**

The United States District Court for the Southern District of Georgia denied a motion for summary judgment, concluding that there were issues of fact for trial as to whether the plaintiff's business met the definition of a heavy equipment dealership under Georgia's Regulation of Agricultural Manufacturers, Distributors, and Dealers.

This case arises out of a dispute regarding the relocation of a heavy-equipment dealership in violation of a dealership agreement. Defendant CNH Industrial America, LLC (CNH) is a manufacturer of heavy equipment. Plaintiff GJ&L sought permission to move one of its two dealerships, which sells CNH equipment, to a new location. CNH was only willing to permit the move if GJ&L signed a new agreement, one with terms that GJ&L perceived to be less favorable to it. Despite its failure to get the requisite permission, GJ&L opened a new store location. In response to GJ&L's choice to operate its dealership in an unapproved location, CNH stopped reimbursing it for warranty services provided on equipment sold at that dealership.

GJ&L sued CNH, claiming that its refusal to approve the relocation violates Georgia's Regulation of Agricultural Manufacturers, Distributors, and Dealers. To succeed on its claim, GJ&L needed to "show that the products it sells are equipment primarily designed for or primarily used in agriculture, horticulture, irrigation for agriculture or horticulture, and other such equipment which is considered tax exempt and sold by the franchised equipment dealer." CNH challenged the classification of the equipment as being "primarily designed for or primarily used" in agriculture. When making sales, GJ&L was supposed to enter certain information, including how customers would use the products, in an electronic settlement system. CNH relied on GJ&L's own records showing that only 1.3% of its sales were designated in the sales system for use in agriculture. GJ&L responded that it had coded everything "other construction" as a way to shirk its reporting duty and, therefore, the 1.3% figure was not accurate. Because there was a dispute regarding the credibility of GJ&L's records, the court concluded that an issue of fact for the jury existed and denied the motion for summary judgment.

GJ&L also argued that the phrase "other such equipment which is considered tax exempt," meant that equipment did not need to be used for agriculture to fall within the scope of the Georgia statute so long as the equipment was tax exempt. The court dismissed this argument as out of hand, holding that that phrase "refers to equipment used in practices similar to" agriculture, horticulture, etc.

***Money Mailer, LLC v. Brewer*, Bus. Franchise Guide (CCH) ¶ 16,225, 2018 WL 3156901 (W.D. Wash. June 28, 2018)**

In a dispute between Money Mailer Franchise Corporation (MMFC) and a former franchisee (Brewer), the U.S. District Court for the Western District of Washington granted in part and denied in part Brewer's motion for summary judgment on his claims against MMFC and its affiliated company (MMLLC).

MMFC is a direct-mail advertising franchisor. Pursuant to his franchise agreement with MMFC, Brewer was required to contract directly with MMLLC for the purchase of mailing production services and materials. Although MMFC and MMLLC are separate entities, a significant overlap exists between the companies, including shared officers and employees, and MMLLC billed and collected charges, fees, and royalties from franchisees on behalf of both companies (collectively, Money Mailer). At the time that he entered into his franchise agreement in 2011, Brewer was told that printing costs would average $115 per spot (10,000 printed ads) and that other production costs averaged approximately $2,245 per month to production.

Beginning in 2012, Brewer began complaining about errors on the invoices that he received from MMLLC and also allegedly began to suspect that Money Mailer was not providing freight services at cost. Brewer filed counterclaims against MMFC and MMLLC in 2015 alleging that Money Mailer marked up charges for printing services without adequate disclosure and that such undisclosed markups violated the Washington Franchise Investment Protection Act (FIPA) and the Washington Consumer Protection Act (CPA). Documents produced by Money Mailer in discovery revealed that the markup for printing costs was in excess of 100% and was one of Money Mailer's "Key Financial Metrics."

Under FIPA, it is an unfair or deceptive act for a person to "[s]ell, rent, or offer to sell to a franchisee any product or service for more than a fair and reasonable price." Money Mailer argued that its integrated printing-insertion-mailing methodology provided such overwhelming benefits to the franchisees that the prices charged for printing services were reasonable. The court disagreed, finding as a matter of law that a markup of more than two times is not a "fair and reasonable" price and that to hold otherwise "would allow undisclosed profit centers and vitiate FIPA's essential purpose to protect franchisees 'from oppressive practices historically associated with sale of franchises.'" Further, in dicta, the court commented that "it is likely" that a Washington court would find that *any* markup on the costs of materials would to be a violation of FIPA. The court also rejected Money Mailer's

argument that Brewer's FIPA claims were barred by the CPA's four-year statute of limitations and/or the doctrine of laches, holding that it was Money Mailer's burden to prove these defenses and there was no evidence that Brewer knew or should have known that Money Mailer was overcharging for printing services before discovery in the case revealed the facts. Accordingly, the court found that Brewer had established a violation of FIPA and was entitled to a summary judgment.

The court next addressed question of whether Brewer has a private right of action for violations of FIPA's reasonable price provision. Money Mailer argued that FIPA only provides a right to seek damages, etc. where a person "sells or offers to sell a franchise in violation of this chapter. . . ." The court agreed, noting that Brewer had not alleged that Money Mailer violated FIPA in the offer and sale of the franchise, neither party had cited to any relevant legislative history, and the limited case law supported Money Mailer's position. Therefore, and notwithstanding Money Mailer's violation of FIPA's reasonable price provision, the court held that Brewer was not entitled to summary judgment on his FIPA claim.

The court then turned to Brewer's CPA claim. Brewer argued that a violation of FIPA also constitutes an unfair or deceptive act under CPA. The court held, however, that Brewer had not attempted to prove that all of the five elements of a CPA claim were satisfied and, therefore, denied summary judgment on this claim.

TERMINATION AND NONRENEWAL

Takiedine v. 7-Eleven, Inc., Bus. Franchise Guide (CCH) ¶ 16,223, 2018 WL 3141461 (E.D. Pa. June 27, 2018)

The U.S. District Court for the Eastern District of Pennsylvania granted a motion to dismiss with leave to replead, holding that Pennsylvania law does not provide for a claim for the breach of the duty of good faith and fair dealing and, by extension, claims for constructive termination.

Takiedine had been a 7-Eleven franchisee for over forty years and was still operating several stores when he sued 7-Eleven, Inc. (7-Eleven) in the U.S. District Court for the Eastern District of Pennsylvania alleging, among other things, breach of contract and constructive termination. He claimed that 7-Eleven was attempting to force older franchisees like him to terminate their franchise agreements so that it could enter into agreements with new franchisees on more favorable terms. In furtherance of that purported agenda, 7-Eleven purportedly failed to adequately handle store maintenance and repairs (which were the responsibility of 7-Eleven under the franchise agreements), falsely asserted that Takiedine had violated the franchise agreements, and created hostile business conditions by forcing him to purchase goods from expensive preferred vendors.

7-Eleven moved to dismiss, arguing that there could be no constructive termination because Takiedine continued to operate his stores. It also argued that

he had failed to adequately plead a breach of contract claim because he did not attach the franchise agreements to his complaint, and there was no way to assess whether the alleged actions of 7-Eleven actually violated any terms of the franchise agreements. The court granted the motion to dismiss, but gave Takiedine leave to amend the breach of contract claim by attaching agreements.

The court held that that Pennsylvania does not allow good faith and fair dealing claims when the franchisee continues to operate the franchises. First, the court recognized that Pennsylvania law provides that "in the context of franchise agreements, a franchisor has a duty to act in good faith and with commercial reasonableness *when terminating a franchise* for reasons not explicit in the agreement." The court acknowledged that, in several cases, in dicta, the Pennsylvania Supreme Court had hinted at a broader obligation to deal with franchisees in a good faith and commercially reasonable manner outside the context of termination. Despite these hints, the court ruled that it could not conclude that Pennsylvania law had changed and, in keeping with prior decisions from the federal district courts in Pennsylvania, it concluded that the duty of good faith is limited to terminations.

As further support for this conclusion, the court looked to analogous areas of the law where "the severance of a legal relationship is not constructive until it actually occurs." In employment law, for example, an employee is not constructively discharged until she is actually terminated. Similarly, a tenant is not constructively evicted until he has abandoned the property. Finally, under the Petroleum Marketing Practices Act, a franchisee must actually abandon the franchise to claim constructive termination. The court further acknowledged that a bright-line rule promotes predictability for litigants.

As to the breach of contract claims, the court held that it needed to review the franchise agreements to evaluate whether Takiedine has stated a viable claim for breach of contract. Therefore, it granted the motion to dismiss with leave to replead with the franchise agreements attached.

TORTIOUS INTERFERENCE

***Boston Tea Co., LLC v. Bay Valley, LLC*, Bus. Franchise Guide (CCH) ¶ 16,257, 2018 WL 4211313 (S.D.N.Y. Sept. 4, 2018)**

This case is discussed under the topic heading "Contract Issues."

TRADEMARK INFRINGEMENT

***Hyundai Motor Am., Inc. v. Direct Techs. Int'l, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,254, 2018 WL 4110544 (W.D.N.C. Aug. 29, 2018)**

This case is discussed under the topic heading "Antitrust."

***Servpro Intellectual Prop., Inc. v. Zerorez Franchising Sys., Inc.*, Bus. Franchise Guide (CCH) ¶ 16,227, 2018 WL 3364372 (N.D. Tenn. July 9, 2018)**

This case is discussed under the topic heading "Jurisdiction."

UNFAIR COMPETITION/UNFAIR AND DECEPTIVE PRACTICES

***Butler v. Jimmy John's Franchise, LLC*, Bus. Franchise Guide (CCH) ¶ 16,241, 2018 WL 3631577 (S.D. Ill. July 31, 2018)**
This case is discussed under the topic heading "Antitrust."

***Hyundai Motor Am., Inc. v. Direct Techs. Int'l, Inc.*, Bus. Franchise Guide (CCH) ¶ 16,254, 2018 WL 4110544 (W.D.N.C. Aug. 29, 2018)**
This case is discussed under the topic heading "Antitrust."

***Money Mailer, LLC v. Brewer*, Bus. Franchise Guide (CCH) ¶ 16,225, 2018 WL 3156901 (W.D. Wash. June 28, 2018)**
This case is discussed under the topic heading "Statutory Claims."

VICARIOUS LIABILITY

***New Star Realty, Inc. v. Jungang PRI USA, LLC*, Bus. Franchise Guide (CCH) ¶ 16,213, 816 S.E.2d 501 (Ga. Ct. App. 2018)**
In this case, the Georgia Court of Appeals reviewed New Star Realty, Inc.'s (NSR) motion for judgment notwithstanding the verdict (JNOV) following a jury trial in which NSR was found liable under a negligence theory for the acts and omissions of its franchisee (New Star Georgia).

New Star Georgia was a franchisee of NSR, a residential and commercial real estate investment business. Jeongha Lee (Lee) was the owner of New Star Georgia. Jueun Yeo (Yeo) was New Star Georgia's senior vice president and one of its most productive agents. Yeo was also part owner in and the managing member of Jungang PRI USA, LLC (Jungang), a real estate investment company. Yeo's brother and a company with which he was affiliated were the other owners of Jungang.

In 2007, Lee told Yeo and others about property for sale near a Kia Motor plant in Georgia. After investigating the property, Yeo and her brother agreed that Jungang should invest in a deal to purchase the property. Lee told Yeo that the draft purchase and sale agreement for the property required a $1 million earnest money deposit. After being assured by Lee that the deposit would be placed in New Star Georgia's escrow account and was fully refundable if the deal did not close, Jungang wired $1 million to New Star Georgia's escrow account. Jungang never received a copy of the purchase and sale agreement, the deal did not close, and Lee misappropriated the funds. After Lee complained about the outstanding funds to the owner of NSR on several occasions, NSR terminated New Star Georgia, and New Star Georgia ceased operations. Lee was ultimately convicted of felony theft and sentenced to prison.

Jungang subsequently filed a complaint against several defendants, including New Star Georgia, one of its brokers, and NSR. At trial, Jungang alleged that NSR was (1) vicariously liable for the negligence of New Star Georgia under theories of actual and apparent agency, and (2) directly negligent

in selling a franchise to Lee and with respect to the hiring, training, and supervision of New Star Georgia's office manager. The jury found in favor of Jungang, and NSR filed a motion for judgment notwithstanding the verdict, which the trial court denied. On appeal, NSR contended that there was no evidence to support the jury's finding that it was vicariously liable for the acts and omissions of NSR relating to the escrow fund and that it owed no legal duty to Jungang as a matter of law with respect to such funds and therefore could not be directly negligent.

The court first addressed NSR's actual agency argument, noting that under Georgia law (1) an agency relationship requires that the purported principal control the time, manner, and method of the alleged agent; and (2) a franchisor is permitted to exercise a certain degree of control over a franchisee's business to protect its brand without becoming vicariously liable for the acts of a franchisee and its employees. The court found that the evidence at trial failed to support a finding of actual agency because the franchise agreement did not include any provisions giving NSR supervisory control over the day-to-day activities of New Start Georgia and, in fact, stated that New Star Georgia was responsible for its business operations. The court held that the evidence confirmed NSR did not actually exercise such control in general, and with respect to the escrow account in particular. The only evidence of control was that New Star Georgia took its "marching orders" from NSR with respect to uniforms, logo, brand of cars being used by the real estate agents, advertising, and sales and marketing methods. Citing a number of Georgia cases, the court found that a franchisor's exercise of control over such matters "does not equate to managing the daily operations of a [franchisee's] business."

The court next reviewed plaintiff's apparent or ostensible agency theory, which requires that (1) the purported principal held out another as its agent; (2) the plaintiff reasonably relied on the alleged agent based on the principal's representations; and (3) the reliance led to injury. The court found sufficient evidence to establish that NSR held New Star Georgia out to the public as its apparent agent, but that plaintiff failed to establish either that Jungang justifiably relied on the apparent agency relationship or that such reliance caused its injuries. The court noted that Yeo was aware of the franchise relationship between NSR and New Star Georgia, New Star made its own hiring decisions, which knowledge was imputed to Jungang, and thus there could be no justifiable reliance. The court further found that no evidence suggesting that Jungang relied on an apparent agency relationship between NSR and New Star Georgia in making its decision to invest in the property and, therefore, failed to establish that any reliance led to its injury.

Finally, the court turned to whether NSR was directly liable for the loss of the escrow funds because it failed to exercise ordinary care in selecting Lee as a franchisee and in its failure to provide adequate education, training, and supervision of New Star Georgia. With respect to Jungang's "negligent franchising" theory, the court held that Jungang had failed to identify any

Georgia statute or common law principle establishing that a franchisor owes a legal duty to third parties in the selection of a franchisee. The court further noted that even if there were such a duty, no evidence indicated that NSR knew or should have known that Lee had a propensity to misappropriate funds. The court was equally unpersuaded by Jungang's negligent hiring, training, and supervision argument, finding that no such claim existed because NSR was not the employer of the franchisee of New Star Georgia's employees.

Accordingly, the court reversed the trial denial of NSR's motion for judgment notwithstanding the verdict and remanded the matter to the trial court to enter judgment in NSR's favor on Jungang's claims.