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2018 Judicial Update

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Employment Issues: Franchisor Liability to Franchisees and Their Employees

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The past year saw continued efforts by franchisees, employees of franchisees, and governmental entities to hold franchisors liable for labor and employment violations involving franchisees or their employees. Such actions frequently arise under the Fair Labor Standards Act ("FLSA"), 29 U.S.C. § 201, *et seq*.,1 but can involve a variety of federal and state employment statutes or common law theories.

Section I discusses recent decisions in misclassification cases that seek to find that franchisees are not independent contractors but are the franchisor's employees.

Section II addresses cases brought by employees of a franchisee in which the plaintiffs seek to hold the franchisor liable for employment-related violations or torts by the franchisee or its other employees.2 Such cases generally allege that the franchisor is directly liable as the plaintiff's "joint employer" or vicariously liable on an agency theory.

Section III addresses recent joint employment developments at the National Labor Relations Board ("NLRB"), including the overturning, reinstatement, and potential re-overturning of *Browning-Ferris*, and the pending settlement of the NLRB's joint employment action against McDonald's USA.

Finally, Section IV discusses federal and state legislative efforts to clarify when a franchisor can be deemed the joint employer of its franchisees' employees, including the pending federal Save Local Business Act.

I. Misclassification: Franchisor as Employer of its Franchisees.

A. *Saleem v. Corporate Transportation Group, Ltd.,* 854 F.3d 131 (2d Cir. 2017).

Plaintiffs were drivers of black cars for hire in New York. Defendants (collectively, "CTG") each owned a "base license" that allowed them to operate a black-car "dispatch base" in New York and to sell franchises to individual drivers. Under New York City rules, black cars must be affiliated with a dispatch base, which serves as the franchisor. The franchisees sued CTG, alleging they were employees entitled to overtime pay under the FLSA and New York Labor Law. After the case was conditionally certified as a collective action under FLSA, the district court granted CTG

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1 The FLSA requires that most employees in the United States be paid at least the federal minimum wage for all hours worked and overtime pay at time and one-half the regular rate of pay for all hours worked over 40 hours in a workweek. The FLSA exempts certain employees who exercise managerial functions and meet other requirements.

2 Though the standard for liability is similar, customer lawsuits that seek to hold the franchisor liable for the tortious conduct of a franchisee or its employees is beyond the scope of this paper.

summary judgment, holding the drivers were independent contractors—not employees—under the "economic realities" test.

The Second Circuit affirmed on appeal, concluding the record shows plaintiffs were not CTG's employees but were independent contractors in business for themselves. The franchise agreement stated that franchisees are independent contractors. Though not dispositive, the court found this to be evidence the parties' beliefs about the nature of their relationship. Moreover, the plaintiffs independently determined (1) the manner and extent of their affiliation with CTG—whether to rent or purchase a franchise, and at what level; (2) whether to work exclusively for CTG accounts, provide rides for CTG's competitors, or develop their own clientele; (3) the degree to which they would invest in their driving businesses; and (4) when, where, and how regularly to provide rides for CTG clients.

In affirming that the franchisees were independent contractors, the Second Circuit noted that plaintiffs had discretion to select the franchise option that best fit their business plans: plaintiffs decided which dispatch base (franchisor) to partner with; whether to rent or buy a franchise; and which level of a franchise to purchase (different options carried different franchise fees, ranging from a nominal amount up to $60,000). Franchisees had the right to terminate their franchise agreements at will, while CTG could only terminate for cause. While franchisees were required to process payment for CTG clients through CTG's system, franchisees were otherwise free to drive non-CTG clients in several ways. Franchisees were allowed to drive for competing black-car dispatch bases, drive personal clients they solicited, or pick up passengers via street hail. "First, on its face, a company relinquishes control over its workers when it permits them to work for its competitors. Second, when an individual is able to draw income through work for others, he is less economically dependent on his putative employer." As a matter of economic reality, plaintiffs' affiliation with CTG was but one means by which they generated income from their driving businesses. Moreover, "Plaintiffs invested heavily in their driving businesses—another indication that they were 'in business for themselves'"—by purchasing the franchise, vehicle, fuel, repairs, maintenance, registration, insurance, parking, and other fees. Further evidence of the franchisees' independence was the fact that some franchisees drove their own cars while others hired someone else to drive for them. In addition, franchisees set their own schedules, deciding when, where, and how often to work (with some taking off several weeks without telling CTG). CTG provided no direction or incentives for plaintiffs to drive at certain times, on particular days, or in specific areas. "Plaintiffs accepted and rejected (despite the penalty of being placed at the end of the queue) varying numbers of job offers [from CTG], a fact indicative of the discretion and independence associated with independent contractor status."

In light of this evidence, the Second Circuit concluded: "In sum, Plaintiff black-car drivers exercised their business acumen in choosing the manner and extent of their affiliation with CTG; were able to work for rival black-car services, cultivate their own clients, and pick up street hails; made substantial investments in their businesses; and determined when, where, and how regularly to work. They owned or operated enterprises which were flexible and adaptable to market conditions. In short, based on

the record here, these driver-owners were small businessmen." Contrary to plaintiffs' argument, the fact that CTG negotiated rates with clients, charged a per-ride fee to drivers, and enforced a Rulebook did not make the franchisees employees. "While Defendants did exercise direct control over certain aspects of the CTG enterprise, they wielded virtually no influence over other essential components of the business, including when, where, in what capacity, and with what frequency Plaintiffs would drive." Here, the opportunity for profit or loss was determined by the drivers to a greater degree than by Defendants. "In short, the *economic* reality was that Plaintiffs, with the assistance of CTG and as a 'subscriber to its services,' operated like small businesses; they decided to affiliate with Defendants based on *their* perceived economic interests, and not those of CTG."

While a win for the franchisor (CTG), *Saleem* likely provides little guidance or assurance to other franchisors seeking to avoid misclassification claims. Most franchise systems do not provide their franchisees with the extensive flexibility, including the ability to work for the franchisor's competitors or not to work at all, offered by CTG.

B. ***National Maintenance Contractors, LLC v. Employment Dep't*, 406 P.2d 133 (Or. Ct. App. 2017).**

National Maintenance Contractors ("NMC") is a Washington-based franchisor with approximately 60 Oregon-based franchisees that provide janitorial, landscaping, carpet and duct cleaning, and maintenance services to NMC's customers. The Oregon Employment Department determined that NMC was the "employer" of its franchisees in Oregon and levied assessments for unemployment insurance taxes. The Office of Administrative Hearings upheld the Employment Department's decision and NMC appealed to the Oregon Court of Appeals. The Oregon Court of Appeals affirmed, holding "the franchisees at issue in this case were not free from [NMC's] direction and control" and therefore they were not independent contractors but were NMC's employees for unemployment insurance tax purposes.

The determination of whether an individual is an independent contractor or "employee" under Oregon law turns on whether the putative employer controls the means and manner of the individual's provision of services, or merely maintains the controls necessary to effectuate the desired result. While noting that "franchises are unique business arrangements that can differ in many important ways from a traditional employment relationship," the court concluded "there is nothing in the nature of a franchise that requires a modification of those terms ["employer" and "employee"] beyond their traditional definition."

According to the Court of Appeals, NMC "retained control over the means by which their franchisees delivered on their contractual obligations to customers." A key consideration in the "control over the means" analysis is an individual's ability to choose the tools used. Here, "the franchisees had no independent control over the tools of their trade. Rather than simply requiring that whatever tools used delivered the desired result—a clean building—NMC controlled the type *and brand* of equipment that was used down to even the buckets and sponges." While acknowledging that sometimes

specific equipment is necessary to achieve a result associated with the franchise system—"Perhaps a certain brand of mower, and only that brand, leaves a distinctive pattern in the grass that is associated with the franchise"—the court affirmed the finding that NMC was exercising control over the means of franchisees' services, not merely the desired results thereof.

The Court of Appeals also affirmed the finding that NMC retained direction and control over the manner in which its franchisee performed the services. Here, NMC solely negotiated all contracts with customers, prepared all account specifications, and then walked through the customer's premises with the franchisee and provided mandatory instructions regarding the customer's specifications. NMC controlled who performed the services by requiring the franchisee to perform or supervise all work. The court also emphasized that NMC imposed mandatory training for all franchisees, regardless of experience, and that failure to complete training could result in termination. Further, NMC's training and manuals instructed franchisees on approved cleaning techniques: "Of note, these techniques were not simply recommendations, or a list of techniques NMC had determined were efficient in helping the franchisee achieving the desired result. Rather, the materials taught approved techniques for cleaning and the franchisees were tested on that material." NMC's operations coordinators inspected the franchisee's performance at each account at least monthly.

Based on this evidence, the Court of Appeals affirmed the ALJ's holding that the franchisees were NMC's employees, not independent contractors, because NMC controlled the means and manner of the performance of franchisees' services.

C. *Acosta v. Jani-King of Oklahoma, Inc.*, No. CIV-16-1133-W, 2017 WL 3841488 (W.D. Okla. June 9, 2017).

Contending that Jani-King's franchisees are really "employees" under FLSA, the U.S. Department of Labor ("DOL") filed an injunctive action to require Jani-King to comply with the FLSA's record-keeping requirements. As reported at last year's Judicial Update, the federal Western District of Oklahoma dismissed the DOL's original complaint against Jani-King on March 20, 2017, but granted the DOL leave to amend. *See Perez v. Jani-King of Oklahoma, Inc.*, No. CIV-16-1133-W, 2017 WL 3841487 (W.D. Okla. Mar. 20, 2017).

On June 9, 2017, the federal court dismissed the DOL's Amended Complaint as well because it did not distinguish between franchisees that are entities and franchisees that are individuals. Under the FLSA, the term "employee" means "any *individual* employed by an employer." 29 U.S.C. § 203(e)(1) (emphasis added). Under the statute, the term "individual" is distinct from and narrower than the broader term "person," which includes individuals, corporations, partnerships, and other entities. The court held that business entities cannot be "employees" under the FLSA because Section 203(e)(1) refers to "employees" as "individuals" and not as "persons." Because the DOL's Amended Complaint did not distinguish between entity franchisees (which could not be employees) and individual franchisees (who could be employees), the

court held that the DOL failed to state a plausible FLSA violation. Having already allowed the DOL to amend once, the court dismissed the FLSA action with prejudice.

D. *Haitayan v. 7-Eleven, Inc.*, Case No. 2:17-cv-07454, 2018 WL 1626248 (C.D. Cal. Mar. 14, 2018).

Multiple 7-Eleven franchisees filed a putative class action under the FLSA and California law, claiming they were misclassified by the franchisor as independent contractors. Plaintiffs sought hundreds of thousands of dollars in overtime pay and business expenses for each franchisee. The federal Central District of California dismissed the misclassification claims, finding the franchisees did not and could not plead facts sufficient to show that they were employees of 7-Eleven.

The plaintiffs argued that the franchise agreement creates an employment relationship because 7-Eleven exerts control over certain details of store operations, such as temperature, operating hours, and types of sources of products sold in the stores. Plaintiffs also alleged that 7-Eleven requires franchisees to complete unpaid initial training. The court disagreed, finding "the type or degree of control alleged by plaintiffs is wholly insufficient to make them employees." Notably, the plaintiffs' allegations did not show that 7-Eleven exercised control over employees' wages and hours, hiring practices, or other working conditions.

Recognizing the nature of franchising, the court noted that the business format franchising relationship permits the franchisor to exercise the control necessary to protect its trademarks, brand, and goodwill. According to the court, requiring 7-Eleven franchisees to complete training and setting standards for how they operate their franchised stores is necessary to ensure uniformity among all 7-Eleven stores. The system-wide "controls" alleged "do not exceed what is necessary to protect 7-Eleven's trademark, trade name and good will." The plaintiffs' allegations regarding improper control all related to the franchisor's right to protect and control its brand, service standards, merchandise selection, and hours of operation. However, the court found that such uniformity ultimately benefitted the franchisees because of the increased goodwill it brought to the brand. Also weighing against an employment relationship was the fact that franchisees could terminate their franchise agreements upon 72 hours' not**ice, while 7-Eleven could only terminate "for cause."**

E. *Roman v. Jan-Pro Franchising International, Inc.*, No. C 16-05961 WHA, 2017 WL 2265447 (N.D. Cal. May 24, 2017).

Jan-Pro Franchising International operates a three-tier franchising structure that offers cleaning and janitorial services. Jan-Pro sells exclusive rights to use its "Jan-Pro" trademarks to regional master franchisees that became responsible for the Jan-Pro business in a geographic territory and that have the right to sell cleaning and janitorial services franchises in that territory. Regional master franchisees in turn sell "unit franchises," under which the purchasers (franchisees) gain the exclusive right to service certain accounts provided to them by the regional master franchisee.

Regional masters provide initial training and ongoing business development, billing and collection, and revenue disbursement services to franchisees.

Multiple unit franchisees filed a putative class action against Jan-Pro, contending they were improperly classified as independent contractors rather than as employees of Jan-Pro. Plaintiffs sought minimum wages and overtime protections under California law. The regional master franchisees were not parties to the case.

Martinez v. Combs, 49 Cal. 4th 35 (2010) sets forth three alternative definitions of "to employ" under California labor law: (1) to exercise control over the wages, hours, or working conditions; (b) to suffer to permit to work; or (3) to engage, thereby creating a common law employment relationship. *Patterson v. Domino's Pizza, LLC,* 60 Cal. 4th 474 (2014) provides the analytical framework for the common-law definition of employment (the third prong) in the franchise context: to be liable, a franchisor must "retain[] or assume[] a general right of control over factors such as hiring, direction, supervision, discipline, discharge, and relevant day-to-day aspects of the workplace behavior of the franchisee's employees."

Applying "the *Martinez* standard, with the gloss of *Patterson* when considering the common-law definition of employment," the Northern District of California granted summary judgment for Jan-Pro finding the plaintiff unit franchisees had not raised a genuine dispute of material fact. Critically, there was no agreement or direct relationship between Jan-Pro and the unit franchisees. "[O]ur plaintiff unit franchisees' agreements with their respective regional master franchisee did *not* set out any rights for Jan-Pro or otherwise indicate that Jan-Pro would be a third-party beneficiary under those agreements." Indeed, beyond stating that Jan-Pro owned the trademarks, the plaintiffs' franchise agreements did not even mention Jan-Pro. While unit franchisees were "subject to several measures of control" by the regional master franchisees, their franchise agreement conferred no rights upon Jan-Pro. There was no evidence that Jan-Pro controlled—or had the right to control—plaintiffs' wages or day-to-day activities. Thus, plaintiffs could not show an employment relationship under the first or third *Martinez* prongs. Nor was there evidence that Jan-Pro "suffers or permits" franchisees to work. Once again, plaintiffs' unit franchise agreements did not extend Jan-Pro's authority over the regional masters to the unit franchisees.

In granting summary judgment to Jan-Pro, the court also rejected plaintiffs' theory that Jan-Pro should be deemed their employer because the regional masters were ostensible agents of Jan-Pro. "Plaintiff unit franchises admit they had no knowledge that the local companies they contracted with answered to a higher power. They also had no knowledge of Jan-Pro Franchising International, Inc. (our defendant) until this lawsuit. It is of no moment that they believed the companies they contracted with were called 'Jan-Pro.' There is simply no evidence that they formed a belief, reasonable or otherwise, that their respective regional master franchisees acted as agent of any other principal."

II. Joint Employment: Franchisor as Joint Employer of its Franchisees' Employees.

A. *Parrott v. Marriott International, Inc.*, Case No. 17-10359, 2017 WL 3891805 (E.D. Mich. Sept. 6, 2017).

Parrott v. Marriott International is a FLSA collective action case. Plaintiffs Stephane Parrott and Kevin Williams were previously employed as Food and Beverage Managers at two different franchised "Courtyard by Marriott" hotels in Michigan and Virginia. They alleged they and other Food and Beverage Managers were misclassified as "exempt" managers under FLSA, and thereby improperly deprived of overtime pay.

Instead of suing the franchisees they worked for, the plaintiffs sued the franchisor, Marriott International ("Marriott"), claiming Marriott is liable as a "joint employer" for the misclassification and resulting FLSA underpayment violation. Although acknowledging that they were employed by franchisees—not Marriott—the plaintiffs claimed that Marriott's control over its franchise system is so vast that Marriott effectively determines labor conditions.

Marriott moved to dismiss the complaint, arguing that the plaintiffs had not plead facts that established Marriott's control over their terms and conditions of employment, including that Marriott (i) had the power to hire and fire the employees, (ii) supervised and controlled employee work schedules or conditions of employment, (iii) determined the rate and method of payment, and (iv) maintained employment records. Unable to show control over the conditions of employment, the plaintiffs, Marriott argued, attacked the franchise model itself by focusing on Marriott's efforts to protect brand standards—efforts that are unrelated to the terms and conditions of employees' employment. Marriott emphasized that the Franchise Agreements explicitly state that franchisees—not Marriott—have exclusive control over the hiring of employees and the terms and conditions of employment at the hotels.

The court disagreed, denying Marriott's motion to dismiss. Presuming the truth of the plaintiffs' allegations, the court found the plaintiffs sufficiently alleged that Marriott: (1) treats Food Managers like Marriott employees by giving all Food Managers discount room rates at Marriott hotels worldwide (thus affecting their compensation or benefits); (2) exercises a substantial degree of supervision over the work of Food Managers through corporate managers and auditors; (3) controls operations through corporate managers and auditors who review and compel compliance with corporate directives; (4) supervises and controls work schedules for Food Managers by auditing financial records and meeting with hotel personnel about controlling labor costs; (5) controls working conditions by requiring franchisees to comply with workplace rules; (6) maintains employment records; and (7) imposes standardized procedures for hiring food managers. The court also noted the plaintiffs claimed they received direct training, instruction, and workplace directives from Marriott employees and were "faulted" by Marriott corporate auditors for failure to follow those directives. Finally, the plaintiffs allege they were told they work "first and foremost" for Marriott. The court found these allegations were sufficient to survive the motion to dismiss.

In denying Marriott's motion to dismiss, the court largely ignored Marriott's primary argument that the plaintiffs' allegations relate to Marriott's right to control brand standards across the franchise system, not control over the conditions of employment. Several of the examples of Marriott's "control" identified by the plaintiffs in *Parrott* have nothing to do with the conditions of employment but rather involve system-wide brand standards, including hotel appearance, and uniform methods of operations:

- Marriott's determinations regarding uniform décor and trade dress;
- Marriott's determination of the location of Marriott hotels;
- Marriott's selection of vendors;
- Marriott's development of menus; and
- Marriott's frequent inspections for compliance with Marriott standards.

Similarly, another example cited by the plaintiffs—Marriott's imposition of mandatory corporate training for Food Managers—is necessary to ensure that supervisory employees (like Food Managers) are fully aware of and knowledgeable regarding system-wide brand standards.

The court made no distinction at the motion to dismiss stage between a franchisor's control incident to system-wide brand standards—which is a touchstone of franchising—and control over a franchisee's employment and personnel decisions and matters. Further, the court appeared receptive to the plaintiff's argument that Marriott maintained the ability to end franchise agreements and thereby terminate Food Managers' employment.

B. *Rodriguez v. America's Favorite Chicken Co., Inc.*, Civil Action No. 2:15-cv-1775-KOB, 2017 WL 1684543 (N.D. Ala. May 3, 2017).

Plaintiff Stefhany Rodriguez worked at a franchisee's Church's Chicken restaurant. She sued the franchisors of Church's Chicken for alleged FLSA minimum wage and overtime violations. The court granted the franchisors' motion to dismiss, holding the plaintiff's factual allegations did not show that the franchisors were her "employer" under the FLSA.

An entity "employs" a person under the FLSA if its "suffer[s] or permit[s]" the individual to work. 29 U.S.C. § 203(g). "Economic reality" dictates whether a party is an employer under FLSA. Courts within the Eleventh Circuit focus on four factors in evaluating economic reality: whether the alleged employer (1) has the power to hire and fire employees; (2) supervises and controls work schedules or conditions of employment; (3) determines the rate and method of payment; and (4) maintains employment records.

While the plaintiff generally averred that the franchisors each "owns, controls, and has a managing/oversight role in its franchisee," the court found the plaintiff made

no allegations that the franchisors controlled the franchisee's employees. Mere management or oversight of a *franchisee* does not mean that the entities have the power to hire or fire, or make other personnel decisions, supervise work schedules, determine pay rate, or maintain records as to the franchisee's employees. Plaintiff's general assertion that the franchisors had a management role in the franchisee was not sufficient to allege an employment relationship. Further, the fact that the franchise agreement requires franchisees to send their restaurant managers to a "Manager in Training" program was not sufficient to "magically turn the Franchisors into Ms. Rodriguez's employers," especially where the plaintiff was not a manager and did not participate in the program. Absent allegations about the plaintiff's relationship with the franchisors, the complaint failed to allege "employment" under the FLSA. Accordingly, the court granted the franchisors' motion to dismiss.

C. ***Wickliff v. La Quinta Worldwide, LLC*, Case No. 6:16-cv-01818-AA, 2017 WL 4423407 (D. Or. Oct. 4, 2017).**

The plaintiff claimed she was sexually assaulted by her supervisor while working at a franchised La Quinta hotel, and, as a result of the sexual assault, she was constructively discharged from her employment in violation of Title VII of the Civil Rights Act and Oregon law. In addition to suing her supervisor and the franchisee, she claimed the franchisor entities—La Quinta Worldwide, LLC and LQ Management, LLC (collectively, "La Quinta")—were vicariously liable for the supervisor's sexual battery and the franchisee's unlawful employment practice. The franchisor defendants moved to dismiss.

The court granted in part and denied in part La Quinta's motion to dismiss. Plaintiff first claimed that La Quinta was vicariously liable for *the supervisor's* sexual battery under "single employer" or "joint employer" theories under Title VII. Sexual battery, however, is an intentional tort and the court found that state law governs vicarious liability for intentional torts. As a result, Oregon law—not Title VII—controls the vicarious liability analysis in this case. The court found that, while the plaintiff attempted to satisfy the standard for vicarious liability under Title VII, she failed to make sufficient factual allegations relevant to the vicarious liability analysis under Oregon law. Accordingly, the court dismissed the plaintiff's claims that La Quinta was vicariously liable for the alleged sexual battery by the franchisee's supervisor. Finding the plaintiff's pleading deficiencies may be curable, the court granted leave to amend.

By contrast, the court held the plaintiff sufficient alleged that La Quinta is vicariously liability for *the franchisee's* alleged misconduct on an agency or apparent agency theory. Under Oregon law, an agency relationship exists where (1) the principal has the right to control the act of its agent, and (2) both parties agree the agent will act on the principal's behalf. Based on the mere existence of a franchise relationship, the court found the plaintiff sufficiently alleged an agency relationship. Pointing to the franchise agreement, the court concluded that "[f]acts alleged in the complaint indicate that [the La Quinta] defendants had some right to control [the franchisee], which included [La Quinta's] ability to dictate requirements for [the franchisee] to adhere to certain systems, business methods, and training and hiring procedures. [The

franchisee and La Quinta] apparently agreed that [the franchisee] would act on [La Quinta's] behalf because of the franchise agreement (however attenuated it may be)."

The court also found that plaintiff sufficiently alleged an apparent agency relationship. For an apparent agency to exist, (1) the principal must engage in conduct that holds out another as its agent, and (2) the principal must rely on the care or skill of the apparent agent. In denying La Quinta's motion to dismiss, the court found "plaintiff points to the franchise agreement to establish that an apparent agency relationship existed between [franchisee] and [La Quinta]. [La Quinta] apparently held out [franchisee] as its agent as [franchisee] operated the facility under the specifications set forth by [La Quinta]. [La Quinta] apparently relied on the care or skill of [franchisee] as [franchisee] was the party that actually operated the facility." Based on such generic allegations about franchising, the court found plaintiff sufficiently pled an apparent agency relationship between La Quinta and its franchisee. Thus, the mere fact of a traditional franchise relationship, without more, was sufficient to allow a plaintiff's vicarious liability claim against the franchisor to survive dismissal.

D. *Harris v. Midas*, Civil Action No. 17-95, 2017 WL 5177668 (W.D. Pa. Nov. 8, 2017).

Plaintiff Hannah Harris worked as a technician at a franchised Midas location in Lower Burrell, Pennsylvania. She claims she was repeatedly sexually, physically, and emotionally harassed, assaulted, and tortured by a store manager during her employment. Plaintiff complained to the multi-unit franchisee (Katz)'s district manager, who was the store manager's direct supervisor.3 Instead of intervening, the district manager allegedly joined in the harassment and threats. Plaintiff eventually complained to the franchisee. The franchisee told the plaintiff she could either return to work with the harassers (who would not be moved or fired), be transferred to an inconvenient location, or be terminated. Because a transfer was not economically feasible, plaintiff accepted termination.

The plaintiff sued several defendants, including the alleged franchisors, TBC Corporation, Midas International Corporation, and Midas, Inc. (collectively, the "TBC Defendants") for claims of sexual harassment, gender discrimination, and retaliation under Title VII, as well as state law tort claims, based on the conduct of the franchisee's employees.

Plaintiff claimed the TBC Defendants and the franchisee were her joint employers, and thus all were liable for the alleged Title VII violations. A joint employer relationship may exist for the purposes of Title VII when two entities "exercise significant

3 The plaintiff's disturbing factual allegations regarding the verbal abuse, sexual demands, assaults, sexual harassment, and threats are graphically summarized in an earlier court order. *See Harris v. Midas,* No. 17-95, 2017 WL 3440693 (W.D. Pa. Aug. 10, 2017) (granting the franchisor defendants' original motion to dismiss, but granting plaintiff leave to amend).

control" over the same employee. Within the Third Circuit, courts consider three factors in determining whether a joint employment relationship exists: (1) the alleged employer's authority to hire and fire employees, promulgate work rules and assignments, and set conditions of employment, including compensation, benefits, and hours; (2) the alleged employer's day-to-day supervision of employees, including employee discipline; and (3) the alleged employer's control of employee records, including payroll, insurance, and taxes.

Although a "close call," the court found the plaintiff alleged sufficient facts to establish a plausible joint employment theory. As to the first factor, plaintiff alleged that the franchise agreement empowered Midas International to promulgate workplace policies at the franchised stores. More specifically, she alleged she was "covered by TBC/Midas' sexual harassment policy" because the TBC Defendants "provided training and guidance to its franchisees, including Katz Midas, regarding the creation of an employee handbook and . . . the inclusion of a sexual harassment policy." As to the second factor, the amended complaint alleged that the TBC Defendants had the authority to exercise day-to-day control over employees. For example, under the franchise agreement, Midas International could require any employee (including plaintiff) to attend trainings. In addition, the TBC Defendants trained the franchisee's supervisory employees, who in turned trained others, including plaintiff, in the "Midas System." And the franchisors visited and inspected the Lower Burrell Midas location to ensure compliance with system standards, including the requirement that employees like plaintiff followed the "Midas System." The court found these allegations made "at least a weak showing" under the second prong. Finally, as to the third factor, the plaintiff argued that Midas' ability under the franchise agreement to examine and audit a franchisee's "books and records" was so broad as to grant the TBC Defendants access to plaintiff's personnel file, including payroll, tax, benefits, and insurance information. "Although the Court would read [this] provision differently, as applying to financial records rather than personnel files, it agrees that, read in a light most favorable to Plaintiff, such wording is sufficiently broad to support a finding that Midas International exercised some control over employee records at the Lower Burrell store." Taken together, the court found plaintiff sufficiently alleged joint employment to survive dismissal.

Alternatively, the court found that the amended complaint alleged sufficient facts to establish vicarious liability on an agency theory for the alleged Title VII and state law violations. An agency relationship may exist if the putative employer has a right to control the employee's conduct, either directly or through the third party's control over the employer. There are "provisions of the [Franchise Agreement] . . . so nebulously and generally phrased as to suggest that [the franchisor] retained a broad discretionary power to impose upon the franchisee virtually any control, restriction, or regulation it deemed appropriate or warranted." Coupled with the fact that the TBC Defendants provided guidance regarding discrimination policies and required the franchisee's employees to submit to training, the court found the amended complaint contained sufficient allegations of the TBC Defendants' control over the franchisee's employees to state a plausible basis for vicarious liability under an agency theory.

E. *Lora v. Ledo Pizza System, Inc.*, Civil Action No. DKC 16-4002, 2017 WL 3189406 (D. Md. July 27, 2017).

Plaintiffs Lenin Lora and Jazmyn Miller worked at a franchised Ledo's Pizza restaurant in Owings Mills, Maryland. Mr. Lora was originally hired as a manager at the franchisee's store at the recommendation of the franchisor, Ledo Pizza Systems, Inc. ("Ledo"). Mr. Lora subsequently requested and received permission from both the franchisor and franchisee to hire his girlfriend, Ms. Miller, as a bartender at the Owings Mills store. Damon Richards, a corporate employee of Ledo, occasionally worked at the franchisee's Owings Mills store. Mr. Richards directed Mr. Lora regarding what items to stock and preparation of inventory lists. Through Mr. Richards, Ledo required Mr. Lora to provide daily and weekly reports about the store. Mr. Richards provided training, consultation, and operational support to Mr. Lora and other employees at the Owings Mills store. Mr. Richards set Mr. Lora's schedule and hired at least one server for the restaurant. After Mr. Lora hired a 64-year-old bartender (Jacki Gray), Mr. Richard instructed Mr. Lora to fire her because she was "too old." After Mr. Lora refused, Mr. Richards said he would "regret it." Mr. Lora also discovered that some employees were being paid less than minimum wage and reported the issue to the franchisee. Instead of correcting the issue, the franchisee reprimanded Mr. Lora for properly paying overtime. Mr. Lora also discovered that one employee was an undocumented worker who was being paid outside of normal payroll. After Mr. Lora raised this issue with the franchisee and franchisor, he was fired. According to the complaint, the franchisor then instructed the franchisee not to schedule Mr. Lora's "girlfriend"—that is, Ms. Miller—effectively terminating her.

Plaintiffs sued Ledo and the franchisee, claiming, among other things, that they were fired in retaliation for (1) Mr. Lora reporting wage violations in violation of the FLSA, and (2) Mr. Lora's refusal to comply with Mr. Richards' demand to fire Ms. Gray because of her age in violation of the Age Discrimination in Employment Act ("ADEA"), 28 U.S.C. § 621, *et seq*. Ledo moved to dismiss, arguing it was not the plaintiffs' "employer" under either FLSA or ADEA. Finding the plaintiffs sufficiently alleged joint employment, the court denied the franchisor's motion to dismiss.

Plaintiffs argued that Ledo and the franchisee were "joint employers" equally liable for the alleged FLSA violations. The court began its analysis by acknowledging that, without more, a franchisor's control over a franchisee does not create a joint employer relationship. Instead, to survive dismissal, the plaintiff "must show a relationship among the franchisor, the franchisee, and the plaintiff that demonstrates an employment relationship." The Fourth Circuit's recent decision in *Salinas v. Commercial Interiors, Inc.*, 848 F.3d 125 (4th Cir. 2017), establishes an expansive standard for evaluating "whether a purported joint employer shares or codetermines the essential terms and conditions of a worker's employment." The *Salinas* analysis considers not only the relationship between the employee and the alleged joint employer, but also the nature of the relationship between the actual employer and the alleged employer. Given the existence of the franchise relationship and the plaintiffs' extensive allegations about the involvement of the franchisor's employee (Mr. Richards)

in the franchisee's employment matters, the court easily concluded the plaintiffs' FLSA retaliation claim survived dismissal.

In denying Ledo's motion to dismiss the FLSA claim, the court found plaintiffs made several allegations about Ledo's involvement with the franchisee and the plaintiffs. The franchisee hired Mr. Lora at Ledo's recommendation. Mr. Lora requested permission from both the franchisee and franchisor to hire Ms. Miller. Ledo's corporate employee, Mr. Richards, directed Mr. Lora's work, required Mr. Lora to provide him with daily and weekly reports, told Mr. Lora which items to stock, set schedules for Mr. Lora and another employee, and directly hired one of the store's servers. Mr. Richards also instructed Mr. Lora to fire Ms. Gray, a 64-year-old bartender, saying Mr. Lora would "regret it" if he did not do so. Both Mr. Richards and the franchisee informed Mr. Lora that he was fired. Later, the franchisee told Ms. Miller that "corporate" told the franchisee not to put Ms. Miller on the schedule. Taken as true, these allegations indicate that Ledo generally (and Mr. Richards specifically) had some power to control, supervise, hire, or fire workers at the franchisee's store, and the franchisor-franchisee affiliation suggests a long-lasting relationship between the two putative employers. Finding the plaintiffs adequately pleaded a joint employment relationship, the court denied Ledo's motion to dismiss the FLSA claim.

The court also denied Ledo's motion to dismiss the ADEA retaliation claim. While the definition of "employer" under the ADEA is narrower than the FLSA's expansive definition, the court still found the plaintiffs sufficiently alleged "employment" to state an ADEA retaliation claim against the franchisor.4 Here, the complaint's allegations suggest that Ledo, acting through its representative, Mr. Richards, may have had control over hiring and firing decisions, day-to-day supervision of the franchisee's employees, and formal or informal training. Further, Mr. Richard's statement that Mr. Lora would "regret it" for disobeying his order to fire Ms. Gray could be considered a threat of retaliation. The court found these allegations sufficient to survive dismissal.

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4 Under the ADEA, an employer is any "person engaged in an industry affecting commerce who has twenty or more employees for each working day in each of twenty or more calendar weeks in the current or preceding calendar year." 29 U.S.C. § 630(b). In evaluating joint employment claims under the ADEA, courts within the Fourth Circuit focus on nine factors: (1) authority to hire and fire the individual; (2) day-to-day supervision, including employee discipline; (3) whether the putative employer furnishes the equipment used and the place of work; (4) possession of and responsibility over the individual's employment records, including payroll, insurance, and taxes; (5) length of time during which the individual has worked for the putative employer; (6) whether the putative employer provides the individual with formal or informal training; (7) whether the individual's duties are akin to a regular employee's duties; (8) whether the individual is assigned solely to the putative employer; and (9) whether the individual and the putative employer intended to enter into an employment relationship.

III. NLRB Developments.

The past few months have brought sudden, unexpected updates to the *Browning-Ferris* saga. In December 2017, the National Labor Relations Board ("NLRB" or "Board") issued *Hy-Brand*, which overturned *Browning-Ferris* and returned to the traditional joint-employment standard. Two months later, the NLRB vacated its *Hy-Brand* decision and reinstated *Browning-Ferris*. That decision is now being challenged. In addition, a settlement of the NLRB's joint employment action against McDonald's USA awaits ALJ approval.

A. *Browning-Ferris Industries of California, Inc.* 362 NLRB No. 186 (2015).

In August 2015, the NLRB upended over 30 years of precedent to "restate" the joint-employer standard under the National Labor Relations Act ("NLRA"), the federal law that encourages collective bargaining and regulates certain labor practices. Since a pair of decisions in 1984, the NLRB had focused on whether a putative joint employer actually exercised "direct and immediate control" over the essential terms and conditions of the relevant worker's employment, such as hiring, firing, discipline, supervision, and direction. Although a fact-specific inquiry, this standard was widely seen as creating a fairly predictable legal regime for most businesses, including those in the franchise industry. Absent extraordinary circumstances, a franchisor would rarely be found to be a joint employer with its franchisees under the pre-*Browning-Ferris* standard.

All that changed with *Browning-Ferris Industries of California, Inc.*, 362 NLRB No. 186, 2015 WL 5047768 (Aug. 27, 2015). In a 3-2 decision, the Board concluded that Browning-Ferris, Inc. was a joint employer of workers provided by staffing agency Leadpoint Business Services Inc. at a Browning-Ferris recycling plant, and therefore had an obligation to participate in collective bargaining over a contract for those workers. The Board overturned a regional director's 2013 finding that Leadpoint was the sole employer of the workers it supplied to Browning-Ferris. The Board "restated" the joint employer standard and concluded the two companies were joint employers. Overturning earlier decisions requiring "direct and immediate control," the Board held that indirect control through an intermediary or the reserved right to control, even if unexercised, may be sufficient to find a joint-employer relationship. According to the majority, "[r]eserved authority to control terms and conditions of employment, even if not exercised, is clearly relevant to the joint-employer inquiry." Thus, the hypothetical right to control, even if never exercised, may now be sufficient to find a joint-employer relationship. Further, following the decision, the NLRB no longer requires control be exercised directly and immediately. "If otherwise sufficient, control exercised indirectly—such as through an intermediary—may establish joint-employer status." Moreover, while the "essential terms and conditions of employment" have long been considered to be "hiring, firing, discipline, supervision, and direction," the majority declared the non-exhaustive list also includes things like "dictating the number of workers to be supplied; controlling scheduling, seniority, and overtime; and assigning work and determining the manner and method of work performance." This expansive

standard lowered the bar for imposing joint-employer liability. Suddenly, a company could be drawn into a labor dispute involving employees over whom it lacked any direct and immediate control.

An impassioned dissent chastised the majority for rewriting and expanding "the decades-old test" for determining whether two separate and independent entities are "joint employers" of certain workers. The dissent warned "[t]his change will subject countless entities to unprecedented new joint-bargaining obligations that most do not even know they have, to potential joint liability for unfair labor practices and breaches of collective-bargaining agreements, and to economic protest activity, including what have heretofore been unlawful secondary strikes, boycotts, and picketing."

Throughout 2017, *Browning-Ferris* remained on appeal to the U.S. Court of Appeals for the District of Columbia Circuit, which heard oral arguments on March 9, 2017. *Browning-Ferris Indus. of Cal. Inc. v. Nat'l Labor Relations Bd.*, Nos. 16-1027, 16-1063, 16-1064 (D.C. Cir. 2017). However, on December 14, 2017, while the appeal was pending, the Board overturned *Browning-Ferris* in a 3-2 decision in *Hy-Brand Industrial Contractors, Ltd.* (discussed below). Following the NLRB's *Hy-Brand* decision, the D.C. Circuit remanded the original *Browning-Ferris* appeal. Subsequently, the NLRB vacated *Hy-Brand* in February 2018 and reinstated *Browning-Ferris*. The NLRB then asked the D.C. Circuit to take the rare step of rescinding its remand order and re-accepting the appeal. On April 6, 2018, the D.C. Circuit agreed that "extraordinary circumstance" justified recalling its prior remand order. The D.C. Circuit is holding the case in abeyance pending further disposition of *Hy-Brand* by the NLRB.

B. *Hy-Brand Industrial Contractors, Ltd.*, 365 NLRB No. 156 (2017).

On December 14, 2017, the Board overruled *Browning-Ferris* in the case of *Hy-Brand Industrial Contractors, Ltd.*, 365 NLRB No. 156 (2017). A new 3-2 majority explicitly repudiated *Browning-Ferris'* expansion of the joint-employer standard and restored the NLRB's traditional standard for determining whether two separate and independent businesses are "joint-employers" of the same employees. Relying heavily on the *Browning-Ferris* dissent, the majority argued the standard announced in *Browning-Ferris* was an "analytical grab bag" that was too "vague and ill-defined" to provide meaningful guidance to employers and employees. The Board then announced its return to the prior test, which "provided certainty and predictability." Following *Hy-Brand*, imposing joint-employer liability would require proof that the alleged joint employer actually "exercised joint control over essential employment terms (rather than merely having 'reserved' the right to exercise control)." Further, "the control must be 'direct and immediate' (rather than indirect), and joint-employer status will not result from control that is 'limited and routine.'" Applying the traditional test, the Board held that Hy-Brand Industrial Contractors Ltd. and Brandt Construction Co., which are construction companies owned by the same individuals, were joint employers and both liable for illegally firing seven employees who had gone on strike to protest their wages and working conditions.

Although neither *Browning-Ferris* nor *Hy-Brand* were franchise cases, the *Hy-Brand* majority analyzed the effect of the *Browning-Ferris* standard on the franchising industry. Observing that *Browning-Ferris* was "almost certainly momentous and hugely disruptive" to franchise relationships, the *Hy-Brand* majority found that expansion of the joint-employer standard necessarily placed franchisors in a dilemma: franchisors could either police their trademarks and brand standards (as they are legally required to do) and risk joint-employer liability for such "indirect" or "reserved" control, or they could avoid such enforcement and risk losing their trademark rights altogether. As the *Hy-Brand* majority recognized, such an unworkable conflict was at odds with Congressional intent and Supreme Court precedent.

The return to the traditional standard was short lived. On February 26, 2018, the Board vacated *Hy-Brand* after an inspector general report concluded that board member Bill Emanuel should have recused himself from the case due to a potential conflict of interest. Noting that Emanuel's former firm (Littler Mendelson P.C.) had represented one of the parties in *Browning-Ferris* before the Board and that *Hy-Brand* was essentially a continuation of deliberations that took place in *Browning-Ferris*, NLRB Inspector General David Berry stated in a February 9, 2018 report that Emanuel should not have participated in *Hy-Brand*. The inspector general recommended the Board consult with an agency ethics official to determine the appropriate action. After the Board's Designated Agency Ethics Official concluded that Emanuel should have been disqualified from participating in *Hy-Brand*, the remaining board members unanimously vacated and set aside the original *Hy-Brand* decision. As a result, "the overruling of the Browning-Ferris decision is of no force or effect."

In a motion to reconsider, Hy-Brand has argued that the February 26, 2018 order itself was unlawful and should be undone. Hy-Brand's motion for reconsideration is pending as of April 24, 2018.

C. ***McDonald's USA, LLC,*** **NLRB Case No. 02-CA-093893.**

In late 2014 and early 2015, the NLRB's then-General Counsel, Richard Griffin, initiated several actions against McDonald's USA, LLC—franchisor of the McDonald's system—and its franchisees, seeking to hold McDonald's USA liable as a "joint employer" for alleged labor violations by its franchisees. The charges allege that workers' rights were violated when they were disciplined for participating in minimum wage protests. The decision to authorize the complaints against McDonald's USA was a dramatic change in how the NLRB viewed franchising. The NLRB's complaints provided little detail about the basis for asserting joint employer liability against McDonald's USA, simply noting that McDonald's USA had a franchise agreement with each franchisee and declaring, without elaboration, that McDonald's possessed or exercised control over each franchisee's labor policies. Elsewhere, the NLRB's general counsel hinted that it was McDonald's USA's use of technology that allowed it to make real-time staffing recommendations to individual franchisees based on real-time restaurant revenue that captured the NLRB's attention. Essentially, the NLRB contends that McDonald's controls the conditions of employment of the franchisee's employees through the imposition of its franchise model.

The General Counsel's actions against McDonald's USA and its franchisees were consolidated into a single case before an administrative law judge in the NLRB's New York region. Testimony was heard throughout 2017.

On March 19, 2018, McDonald's USA announced a settlement with the NLRB's new General Counsel, Peter Robb. Under the proposed settlement, McDonald's franchisees will give full back pay to certain workers and potential monetary payments in lieu of reinstatement for individuals who were discharged. McDonald's USA will establish a settlement fund with $250,000 provided by the franchisees. Any unused funds will be distributed back to franchisees at the end of a specified period. McDonald's franchisees also will post notices that collectively address all allegations in the charges. McDonald's USA admits no wrongdoing. The settlement documents contain language that McDonald's USA and its franchisees are not joint employers.

The charging parties (including the Fight For $15 campaign and Service Employees International Union) objected to the settlement, claiming it lets McDonald's USA off the hook. The NLRB's General Counsel has the authority to settle cases, even over the objection of the charging party as long as the settlement provides full relief or substantially full relief for aggrieved workers.

On April 5, 2018, the ALJ held a hearing to determine whether to approve the proposed settlement. A decision is pending at the time this paper is going to print.

IV. Federal and State Legislation.

In response to *Browning-Ferris* and other court rulings and agency actions, federal and state legislators have responded by proposing new laws intended to clarify the joint-employer relationship.

A. The Save Local Business Act.

Introduced in the House of Representatives on July 27, 2017, H.R. 3441—the Save Local Business Act—seeks to clarify who may be deemed a joint employer under the National Labor Relations Act and the Fair Labor Standards Act. Under the proposed legislation, to be a joint employer, a business must "directly, actually, and immediately, and not in a limited and routine manner, exercise[] significant control over the essential terms and conditions of employment, such as hiring employees, discharging employees, determining individual employee rates of pay and benefits, day-to-day supervision of employees, assigning individual work schedules, positions, and tasks, or administering employee discipline."[5] According to a Congressional report, the proposed bill "restores the long-held standard for determining joint employer status under the NLRA that was overturned by a decision of the National Labor Relations Board" and "provides a uniform joint employer standard under the FLSA." H.R. REP.

5 Save Local Business Act, H.R. 3441, 115th Congress (2017). The text of the bill is *available at* https://www.congress.gov/bill/115th-congress/house-bill/3441/text.

NO. 115-379 at 2 (2017), *available at* https://www.congress.gov/115/crpt/hrpt379/CRPT-115hrpt379.pdf. The Congressional report also states:

> The *Save Local Business Act* reaffirms that two or more employers must have "direct, actual and immediate" control over employees to be considered joint employers. H.R. 3441 provides needed clarity to the job creators, entrepreneurs, and workers who are being adversely impacted by expanding joint employer standards.
>
> In particular, the bill rolls back vague and convoluted joint employer schemes as created by the NLRB in *Browning-Ferris,* by the U.S. Court of Appeals for the Fourth Circuit with respect to the FLSA in *Salinas v. Commercial Interiors, Inc.* (Salinas), and by regulators and other courts. H.R. 3441 restores a commonsense definition of employer and protects workers and local employers from future overreach by unelected bureaucrats and activist judges.

The House of Representatives passed the Save Local Business Act on November 7, 2017. The bill's prospects in the Senate are unclear at this time. As of April 24, 2018, the Senate has not yet taken any action on the bill.

B. State Legislation.

Separate from the pending federal Save Local Business Act, 18 states have enacted legislation in the wake of *Browning-Ferris* aimed at clarifying and limiting joint-employer liability over the past few years. As summarized below, some states have revised their employment laws to clarify when joint employment exists under state law, while others more directly provide that a franchisor is not the employer of its franchisees or its franchisees' employees. Below is a summary of such state statutes, many of which went into effect in 2017:

- **Alabama**. Enacted in 2017, Alabama's Franchise Business Protection Act provides that a franchisee, an employee of a franchisee, or an independent contractor working for a franchisee "may not be deemed or construed to be employees of a franchisor." Ala. Code § 25-6-5.

- **Arizona**. As of 2017, Arizona has amended its employment relationship statutes to provide that "[a] franchisor is not an employer or co-employer of either a franchisee or an employee of the franchisee, unless the franchisor agrees, in writing, to assume the role of employer or co-employer of the franchisee or the employee of the franchisee." Ariz. Rev. Stat. Ann. § 23-1604.

- **Arkansas**. On April 4, 2017, the Arkansas governor signed a bill clarifying that, "[n]otwithstanding a voluntary agreement entered into between the United States Department of Labor and a franchisee, neither a franchisee nor a franchisee's employee shall be deemed to be an employee of the franchisor or subfranchisor." Ark. Code Ann. § 11-2-125.

- **Georgia**. Georgia enacted SB 277 in 2016. That law provides as follows: "Notwithstanding any order issued by the federal government or any agreement entered into with the federal government by a franchisor or a franchisee, neither a franchisee nor a franchisee's employee shall be deemed to be an employee of the franchisor for any purpose." Ga. Code Ann. § 34-1-9.

- **Indiana**. Under an addition to Indiana law that went into effect in 2016, a franchisor is not an employer or co-employer of a franchisee or a franchisee's employee "unless the franchisor agrees, in writing, to assume the role of an employer or co-employer of the franchisee or the employee of a franchisee." Ind. Code Ann. § 23-2-2.5-0.5.

- **Kentucky**. Kentucky has passed legislation that amends various employment provisions related to joint employment. For example, Kentucky's wages and hours chapter provides that "[n]otwithstanding any voluntary agreement entered into between the United States Department of Labor and a franchisee, neither a franchisee nor a franchisee's employee shall be deemed to be an employee of the franchisor for any purpose under this chapter." Ky. Rev. Stat. Ann. § 337.010.

- **Louisiana**. The Louisiana legislature passed Louisiana H.B. 464 in 2015. Subject to a narrow exception, the law clarifies that "neither a franchisee . . . nor an employee of the franchisee shall be deemed to be an employee of the franchisor for any purpose." La. Rev. Stat. 23:921(F)(2). For purposes of Louisiana's workers' compensation and unemployment compensation laws, a franchisee's employee may be deemed an employee of the franchisor only if the franchisor and franchisee "share or co-determine those matters governing the essential terms and conditions of employment and directly and immediately control matters relating to the employment relationship such as hiring, firing, discipline, supervision, and direction." La. Rev. Stat. 23:921(F)(3).

- **Michigan**. Like Kentucky, Michigan has enacted a range of legislation that clarifies the relationship between a franchisor and the employees of its franchisees. For example, in 2016, Michigan amended its Employment Security Act to state: "Except as specifically provided in the franchise agreement, as between a franchisee and franchisor, the franchisee is considered the sole employer of workers for whom the franchisee provides a benefit plan or pays wages." Mich. Comp. Laws Ann. § 421.41.

- **New Hampshire**. As of July 2017, New Hampshire's labor relations law provides in pertinent part that "[a] franchisor is only an employer if the franchisor agrees in writing to assume the role of employer or co-employer of the franchisee or the employee of the franchisee." N.H. Rev. Stat. Ann. § 275:4.

- **North Carolina**. North Carolina's Wage and Hour Act, effective in May of 2017, provides in pertinent part that "[n]either a franchisee nor a franchisee's employee

shall be deemed to be an employee of the franchisor for any purposes." N.C. Gen. Stat. Ann. § 95-25.24A.

- **North Dakota**. Effective August 2017, North Dakota's law broadly provides as follows: "Notwithstanding any other provision of law or any voluntary agreement between the United States department of labor and a franchisee, a franchisee or an employee of a franchisee is not considered an employee of the franchisor." N.D. Cent. Code Ann. § 51-19-18.

- **Oklahoma**. Passed in 2016, Oklahoma's broad statute provides in pertinent part that "[a] franchisor shall not be considered the employer of a franchisee or a franchisee's employees." Okla. Stat. Ann. tit. 59, § 6005.

- **South Dakota**. As of 2017, South Dakota law provides: "Notwithstanding any other provisions of law or any voluntary agreement between the United States Department of Labor and a franchisor, a franchisee or an employee of a franchisee is not considered an employee of the franchisor." S.D. Codified Laws § 60-1-6.

- **Tennessee**. In 2015, Tennessee legislators passed Tennessee S.B. 475, which clarifies that "[n]otwithstanding any voluntary agreement entered into between the United States department of labor and a franchisee, neither a franchisee nor a franchisee's employee shall be deemed to be an employee of the franchisor for any purpose." Tenn. Code Ann. § 50-1-208(a).

- **Texas**. In 2015, Texas passed S.B. 652, which amends several provisions of the Texas Labor Code to specify that a franchisor is not considered an employer of a franchisee or a franchisee's employee for purposes of claims relating to employment discrimination, payment of wages, the Texas Minimum Wage Act, or the Texas Workers' Compensation Act, unless the franchisor "has been found by a court of competent jurisdiction in this state to have exercised a type or degree of control over the franchisee or the franchisee's employees not customarily exercised by a franchisor for the purpose of protecting the franchisor's trademarks and brand." Tex. Labor Code Ann. § 401.014. Subject to the same exception, the act further specifies that a franchisor is not deemed to be in a co-employment relationship with a franchisee or a franchisee's employees for purposes of Texas law governing professional employer organizations, and that the general definition of "employer" in the Texas Unemployment Compensation Act does not apply to a franchisor with respect to a franchisee or a franchisee's employees.

- **Utah**. Effective May 2016, Utah's employment relations and collective bargaining law was amended to clarify that "a franchisor is not considered to be an employer of a franchisee or a franchisee's employee," unless the franchisor "exercises a type or degree of control over the franchisee or the franchisee's employee not customarily exercised by a franchisor for the purpose of protecting the franchisor's trademarks and brand." Utah Code Ann. § 34-20-14(2).

- **Wisconsin**. In 2016, Wisconsin amended various statutory provisions to clarify that a franchisor is not the employer of a franchisee or a franchisee's employees, unless the franchisor has agreed in writing to assume that role or it is administratively determined that the franchisor "exercised a type or degree of control over the franchisee or the franchisee's employees that is not customarily exercised by a franchisor for the purpose of protecting the franchisor's trademarks and brand." Wis. Stat. Ann. § 111.3205.

- **Wyoming**. Wyoming's labor and employment statutes were amended in 2017 to provide in pertinent part that "[n]either a franchisee nor a franchisee's employee shall be deemed to be an employee of the franchisor for any purpose under this title, unless otherwise agreed to in writing by the franchisor and the franchisee." Wyo. Stat. Ann. § 27-1-116.

Similar bills are pending in South Carolina, Nebraska, and Washington.

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2018 Judicial Update

Class Action Obstacles Beyond Certification

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Class action jurisprudence reflects that class certification is a challenging feat given the statutory requirements that must be met to proceed. Recent class actions and mass actions brought in the franchise context raise even more obstacles that parties must tackle to gain traction in litigation. With the steadily increasing number of federal lawsuits filed, courts show little sympathy to sophisticated parties or attorneys that fail to exercise due diligence to ensure prosecution of only meritorious claims. Even in the post-certification and settlement stage, courts are refusing to adopt awards when there is no finding of a real injury or injustice suffered by the plaintiff class. Of recent note, courts have become highly critical when analyzing what benefits the class is receiving in comparison to the fees that its attorneys are seeking.

A. Pre-Certification

1. *Estler v. Dunkin' Brands. Inc.*, 691 F. App'x 3 (2d Cir. 2017)

Consumers filed a putative class action against the franchisor of the Dunkin' Donuts chain and several Dunkin' Donuts franchisees in the Manhattan area. The plaintiffs were consumers who had purchased pre-packaged bags of coffee from defendants' stores. In connection with the purchases, the plaintiffs alleged that they were unlawfully charged sales tax in violation of New York state law.

On defendants' motion to dismiss, the U.S. District Court dismissed the plaintiffs' claims because they failed to comply with a mandatory state-law administrative remedy. Under New York law, consumers seeking a return of sales taxes that were erroneously paid must apply for a refund to the state tax commission. N.Y. Tax Law § 1139(a). The plaintiffs appealed those findings and argued that: (1) the state's exclusive administrative procedures were not mandated in this case and (2) they may independently pursue a claim under N.Y. Gen. Bus. Law § 349 if defendants' collection of sales tax rose to the level of an unfair and deceptive practice. The Court rejected each argument in turn.

First, the Court looked to the plaintiffs' damages claims to determine whether they were indeed seeking a refund of sales tax falling within the ambit of N.Y. Tax Law § 1139(a) and thus, subject to the state's exclusive administrative remedy. The plaintiffs did not dispute that they failed to exercise this remedy but argued they were seeking the return of an unlawful surcharge rather than a sales tax refund. The Court reviewed the plaintiffs' Amended Complaint, which reflected that the complained-of fee was described as a sales tax assessed at the 8.875% combined state and municipal sales tax rate in New York City. Absent from the complaint was any allegation that the charged fees were over and above the normal sales tax rate and so the Court concluded that the plaintiffs could not avoid the administrative remedy mandated under New York state law.

Alternatively, the plaintiffs argued that because these administrative procedures were only required for the refund of taxes imposed by the state tax code, and compliance was unnecessary where the taxes were assessed in violation of law, such as here where a merchant erroneously collects sales tax on exempt food products. The

Court relied on statutory interpretation and Second Circuit precedent in concluding that these forms of administrative review not only extended to clerical miscalculations of sales tax, but also in the determination of which products were statutorily exempt.

The Plaintiffs also asserted claims contesting the constitutionality of the state taxes charged to them. The Court of Appeals rejected this argument for two reasons. First, the argument was never raised in the District Court and therefore, the plaintiffs were foreclosed from raising the argument on appeal. Second, even considering the plaintiffs' constitutional claim, the comity doctrine prohibited federal courts from awarding damages for such types of claims, so long as the plaintiffs have access to state remedies that are plain, adequate, complete, and reviewable by the Supreme Court.

The plaintiffs argued that they sought a return of an unlawful surcharge, rather than a sales tax refund. However, the Court of Appeals was not persuaded because the complaint conceded that the complained-of fee was described as a sales tax and assessed at the 8.875% sales tax rate in New York City.

Second, the Court considered the plaintiffs' potential claim for unfair and deceptive practices. The Court rejected the viability of this claim for two reasons. First, the plaintiffs failed to justify why the claim would abrogate the need to resort to a mandatory administrative remedy, particularly when N.Y. Tax Law §§ 1139 and 1140 foreclosed all other legal remedies. Second, the operative Complaint failed to allege any actions beyond defendants' continued practice of charging sales tax on pre-packaged coffee that would rise to the level of supporting a claim for unfair and deceptive practices under N.Y. Gen. Bus. Law § 349.

Accordingly, the judgment of the district court was affirmed, dismissing plaintiffs' claims without prejudice.

2. ***Abrantes v. Fitness 19 LLC*, No. 16-cv-00903, 2017 WL 4075576 (E.D. Cal. Sept. 14, 2017)**

In a preliminary statement to the parties and counsel, and in what could be interpreted as an ominous (albeit candid) message to the plaintiffs who filed this action, Judge O'Neil of the U.S. District Court for the Eastern District of California stated the following:

> "Judges in the Eastern District of California carry the heaviest caseloads in the nation, and this Court is unable to devote inordinate time and resources to individual cases and matters. Given the shortage of district judges and staff, this Court addresses only the arguments, evidence, and matters necessary to reach the decision in this order."

This putative class action was brought on behalf of former members of Fitness 19 gyms against Fitness 19 and its parent company, various individual gym locations and associated individuals, and the Fitness Evolution franchisor ("Franchising LLC"). The plaintiffs alleged that the defendants failed to comply with the Electronic Funds

Transfer Act ("EFTA") governing pre-authorized electronic fund transfers when they automatically debited monthly membership fees. Socalevolution LLC (owner of the successor Fitness 19 gym in which a plaintiff was a member) and Franchising LLC's motion to dismiss argued that the Second Amended Complaint failed to allege that Franchising LLC had any direct relationship with the plaintiffs and the allegations failed to raise a reasonable inference that it deducted funds from the plaintiff's accounts. The plaintiffs urged the Court to embrace an expansive reading of EFTA liability, which imposes liability on the defendant regardless of whether it actually initiated the transfers. The plaintiffs argued that in its capacity as a franchisor, Franchising LLC provides integrated billing and marketing and are thus, liable for Socalevolution LLC's actions in its capacity as a franchisee. The Court found that indirect involvement of this nature is not enough to state a claim for a violation of EFTA's provisions governing preauthorized electronic funds transfers. The Court dismissed all claims against Franchising LLC and found "no liability for aiding and abetting EFTA violations." The Court also found the claims against Socalevolution LLC to be barred by the statute of limitations. The Court granted the plaintiffs one last opportunity to amend, but with the following caveat: "This Court's resources are limited. The amended pleadings, if filed timely, will be considered to be the best the parties can present."

3. ***Haywood v. Massage Envy Franchising, LLC*, No. 16-cv-01087, 2017 WL 2546568 (S.D. Ill. June 12, 2017), *aff'd* 2018 WL 1725229 (7th Cir. Apr. 10, 2018)**

Plaintiffs filed a class action against the Massage Envy franchisor, Massage Envy Franchising, LLC ("MEF") alleging MEF committed unfair and deceptive practices after receiving a 50-minute massage, despite paying for a one-hour massage. Plaintiffs alleged that MEF failed to adequately disclose that the consultation and time to undress and re-dress were part of the advertised hour-long session. Specifically, the lead class plaintiff alleged that she was not informed of the 50-minute massage time by any employee or posted sign during her two visits. She did find a stack of cards on the front desk, which indicated the actual massage time and was notified in an e-mail, but in fine print at the very bottom of the e-mail.

The complained-of Massage Envy locations were franchisees that were independently owned and operated. MEF requested that the Court judicially notice MEF's franchise disclosure document and training documents. The Court denied MEF's request due to its failure establish the documents' authenticity and whether the documents were publicly available, as required under Fed. R. Evid. 201.

MEF then argued that plaintiffs lacked standing because no injury could be traced back to MEF's conduct, but rather, only of the conduct of its independently owned and operated franchisees. However, the Court determined that plaintiffs' allegations that MEF's national website and policies deceptively and fraudulently misled them were sufficient to satisfy Art. III standing because they were under MEF's direct control. Nevertheless, in reviewing MEF's training manuals, the Court noted that MEF did not establish sufficient control to confer franchisee liability onto the franchisor and,

thus, MEF would not be liable for the actions of the independent franchisees' employees.

Aside from the complaint's pleading insufficiencies, the Court found plaintiffs' claims to be fatally flawed for several reasons. First, the plaintiffs failed to establish that they received a value worth less than what they paid. The Court analyzed what other massage companies were charging for a similar service and found the value to be roughly $50, which is equivalent to what plaintiffs paid at the various MEF locations. Second, since the value of MEF's service was comparable to its competitors, plaintiffs could not establish that MEF's misrepresentation caused them to receive a lesser value. Nor could plaintiffs establish that MEF's misrepresentation induced them to choose a MEF franchise over its competitors.

Notably, MEF made several attempts to avoid liability by claiming that the individual franchisees were the ones at fault, a contention which was overcome by the determination of MEF's direct control of its national advertising efforts.

4. ***Borenkoff v. Buffalo Wild Wings, Inc.*, No. 16-cv-8532, 2018 WL 502680 (S.D.N.Y. Jan. 19, 2018)**

Plaintiff represented a proposed class of members bringing claims for unjust enrichment and deceptive and/or unfair misleading trade practices (in violation of NY General Business Law § 349) against Buffalo Wild Wings, Inc. and Blazin Wings, Inc. (collectively, "Defendants") arising from Defendants' failure to disclose the use of beef tallow to fry non-meat products. The plaintiff was a vegetarian who visited Defendants' stores and alleged that the industry standard was to use non-beef cooking oil to fry items and a reasonable consumer would expect the Defendants to do follow the industry standard. Plaintiff alleged that Defendants' failure to disclose the use of beef tallow constituted a material misrepresentation or omission and had it been disclosed, she would not have ordered, consumed, or paid a premium for the respective food items.

Upon Defendants' motion to dismiss, the Court first addressed whether the plaintiff had standing to sue. Although the Court expressed serious reservations, it found plaintiff's complaint satisfied the low threshold of injury in fact for Art. III standing. However, the Court's previously expressed concerns foreshadowed the ultimate dismissal of her claims for lack of an actual injury.

As to the GBL § 349 claim, the plaintiff failed to allege any injury she suffered as a result of the misleading act or practice. Specifically, she failed to allege how the use of beef tallow affected the value of the food items she received. Therefore, the only injury alleged was the direct pecuniary loss from the purchase of Defendants' product. However, the Court held that under GBL § 349, the loss of a purchase price alone does not constitute an actual injury.

B. Certification

1. ***Gorss Motels, Inc. and E&G, Inc. v. Safemark Sys, LP*, No. 16-cv-01638, 2018 WL 1635645 *(M.D. Fla. Apr. 5, 2018)***

Plaintiffs were respectively former and current franchisees of Wyndham Hotel Group ("Wyndham"). Plaintiffs brought a putative class action against Defendant Safemark Systems, LP ("Safemark") in connection with faxes sent by Safemark, in violation of the Telephone Consumer Protection Act ("TCPA"). As part of plaintiffs' execution of various franchise agreements, plaintiffs agreed to purchase certain proprietary items from approved suppliers. Plaintiffs also agreed that the franchisor could offer assistance with purchasing items for their individual hotels. Wyndham and its affiliate were to approve third-party suppliers and identify the approved suppliers to the franchisees in a directory.

Safemark, which sold and leased safes to hotels and motels, was identified by Wyndham as an approved supplier since 2002. Wyndham e-mailed Safemark a database of its franchisees' contact information. Safemark then used the contact information to send a one-page fax in 2013 and a multi-page fax in 2015 promoting its products and services.

Plaintiffs sought class certification of two proposed classes of franchisees that were solicited by Safemark in violation of the TCPA, split between those that received the 2013 fax and the 2015 fax. The Court denied plaintiffs' motion for class certification, finding a lack of common issues and significant individual inquiries. Due to the plaintiffs' execution of varying franchise agreements with Wyndham, the Court found that no generalized proof could be used to resolve the issue of consent.

The Court's refusal to certify plaintiffs' proposed classes implicates how individual franchise relationships make it exceedingly difficult to bring mass action due to the factual differences.

C. Post-Certification Considerations

1. ***In re Subway Footlong Sandwich Mktg. & Sales Practices Litig.*, 869 F. 3d 551 (7th Cir. 2017)**

This action arose from a consumer class action that was brought on behalf of consumers that alleged Subway's owner engaged in deceptive marketing and sales practices by advertising sandwiches as "footlongs" when some sandwiches were slightly shorter than twelve inches.

Initially, the proposed plaintiff class failed to identify a compensable injury, which prevented the class from being certified. As a result, the class shifted its strategy from a class seeking damages under Rule 23(b)(3) to a class seeking injunctive relief under Rule 23(b)(2). The proposed class was ultimately certified and subsequently approved as a class.

Thereafter, the parties reached a settlement where Subway agreed to implement a number of practices designed to ensure (to the extent practicable) that its sandwich rolls were at least twelve inches long and committed to following those practices for a period of four years. Specifically, Subway agreed that:

(1) franchisees would "use a tool" for measuring sandwich rolls;

(2) corporate quality-control inspectors would measure a sampling of baked bread during each regularly scheduled compliance inspection;

(3) the inspectors would check bread ovens during each compliance inspection "to ensure that they are in proper working order and within operating specifications"; and

(4) Subway's website and each franchised restaurant would post a notice explaining that the natural variability in the bread-baking process will sometimes result in sandwich rolls that are shorter than the advertised length.

The settlement also explicitly acknowledged that "because of the inherent variability in food production and the bread baking process," Subway could not guarantee that each sandwich roll would "always be exactly 12 inches or greater in length after baking." After agreeing to the substance of the settlement terms, the parties spent the following year negotiating the fees for class counsel and the awards for the class representatives. Both sides eventually agreed to cap attorney's fees to $525,000 and incentive awards at $1,000 for each named plaintiff. The district judge preliminarily approved the settlement and scheduled a fairness hearing.

The settlement was objected to by a class member, who was identified as a professional objector, Theodore Frank ("Frank"). Frank objected on the basis that that the settlement enriched only the lawyers and provided no meaningful benefits to the class. The district court judge was not persuaded and certified the class and approved the settlement.

The Seventh Circuit reversed the lower court's decision and focused its analysis on the criticisms of the class counsel and the award of $525,000 in attorneys' fees. The Seventh Circuit was critical of class counsel and terms of the settlement deal, which would essentially provide zero benefit to the plaintiff class.

First, the Court took issue with the lawyers' failure to consider whether the plaintiffs' claims had any merit given that early discovery established that Subway's unbaked bread sticks were uniform, the baked rolls rarely fall short of twelve inches, and any minor variations were wholly attributable to the natural variability in the baking process that could not be prevented. The Court noted that early discovery conducted by the parties, although limited, was sufficient to extinguish any hope of certifying a damages class under Rule 23(b)(3). However, rather than dismissing the suit, class

counsel instead switched the theme and strategy of plaintiff's claims in order to obtain certification through an injunction class under Rule 23(b)(2).

Second, the Court analyzed the merits of the claims and whether the settlement would indeed address the plaintiffs' alleged suffered harm. The Court noted that the limited informal discovery also revealed that even though some rolls fell short of twelve inches, they contained no less bread nor less food than any 12" sandwich since the amount of meat and cheese was standardized. Therefore, the Court concluded that pre-settlement, there was only a small chance that Subway would sell a class member a sandwich that was slightly shorter than advertised.

The Court then considered the terms of the settlement to see the likelihood of plaintiffs suffering the same harm post-settlement. The Court concluded that there was still the same small chance that a sandwich would be slightly shorter than advertised due to the inherent invariability in food production and the bread baking process. Thus, the Court found that the settlement only awarded fees for class counsel while providing "zero benefits for the class." As a result, the Court reversed the lower court's approval of the settlement and certification of the class.

2. ***Cunningham v. Suds Pizza, Inc.*, No. 15-cv-6462, 2017 WL 6000616 (W.D.N.Y. Dec. 1, 2017)**

Plaintiffs brought this action against their former employers alleging violations of the Fair Labor and Standards Act ("FLSA") and New York Labor Law. Defendants consisted of the pizza franchisor itself ("Mark's"), the individual owner and founder of Mark's, and multiple franchisees of Mark's. A significant issue in the case was whether the franchisees and Mark's were considered joint employers for the purposes of FLSA liability. However, the Court did not have to address the issue as a result of the parties' mediated settlement agreement, which required the Court's approval. The original proposed settlement agreement ("Original Agreement") was rejected by the Court, primarily due to plaintiffs' counsel's request of $566,667 in attorneys' fees, or one-third of the $1.7 million settlement amount, despite settling the case in less than a year after a one-day mediation session.

Based upon the actual number of claims filed by class members, the Court calculated the true value of the settlement to be approximately $339,000, rather than the $1.7 million. Under the Original Agreement's reversion clause, any unclaimed settlement funds would be returned to the defendants and in return, the defendants would not oppose the Plaintiffs' attorney fee application. The Court expressed major concern with the benefits to the class in comparison to its counsel and their potential conflict of interest due to the reversion clause.

The Court directed the parties to revise the formula used in calculating attorneys' fees. In the Modified Settlement Agreement, plaintiffs' counsel then sought $318,000 in fees, and added the difference from the initial request to the plaintiffs' true settlement value. Thus, the plaintiff class would now receive $587,000, rather than $339,000.

Although the Court still considered the $318,000 fees request to be high in comparison to the $587,000 actual settlement value, the Court approved the settlement.

The Court recognized the risk that plaintiffs' counsel took by agreeing to take the case on a contingency fee basis. There was additional litigation risk given that several defendants were franchisees. The Court was spared from having to determine the issue of joint employer liability but was mindful of the possibility that the franchisor could escape liability, which would significantly diminish the plaintiffs' opportunity to settle the case. For those unique reasons, the Court approved the Modified Settlement Agreement.

D. Mass Actions

1. *Association of Independent BR Franchise Owners v. Baskin-Robbins Franchising, LLC*, No. 15-10963-WGY, 2017 WL 4314607 (D. Mass Sept. 27, 2017)

Plaintiffs consisting of stand-alone franchisees that collectively owned eighty-four Baskin Robbins stores ("Association") filed this action for declaratory relief against the franchisor Baskin Robins Franchising, LLC ("Baskin"), alleging that Baskin impermissibly charged its franchisees a "Commercial Factor Fee" that was not disclosed in the various franchise agreements.

The Court's Findings of Fact took note of the overall changes to the franchise agreements provided to Baskin franchisees over the past two decades and noted the following:

- Prior to 1998, Baskin franchisees either paid no royalty fees or a small percentage of "Continuing Franchise Fees" and purchased the vast majority of their ice cream products from Baskin or an affiliate. Consequently, Baskin derived its primary revenue from the sale of ice cream products.

- In 1998, Baskin offered its franchisees a "Royalty Conversion Program" that: (1) either raised or imposed for the first time a Continuing Franchisee Fee of 4.9%; (2) raised the advertising fee to be paid by franchisees to 5%; (3) lowered the costs for ice cream products and other goods; and (4) charged a "Commercial Factor" on ice cream and other products. The majority of the then-existing franchisees accepted the terms of those agreements.

- In 2000, new and renewing franchisees entered into a franchise agreement that did not contain the terms "Commercial Factor" or "Commercial Factor Fee." Baskin also ceased production of ice cream and outsourced the manufacture and wholesale distribution of its proprietary products to Dean Foods. The Current Franchise Agreements provided that franchisees must purchase all of their ice cream and related products from Dean Foods. Dean Foods in turn pays Baskin based upon its volume of sales attributed to Baskin franchisees. This arrangement had been in effect for approximately sixteen years.

The issue brought before the court was the interpretation of the Current Franchise Agreement. Dean Foods charged the franchisees a "Commercial Factor" on products, which in 2016 was approximately $1.26 per tub of ice cream and $6.52 per case of non-dairy whip topping. The Association argued that these fees were prohibited because the agreements were fully integrated and did not include a Commercial Factor Fee as part of the fee provisions. The Court first analyzed exactly what charges made up the Commercial Factor and then looked to the contract language to determine if the charge was permissible.

As to the Commercial Factor, the Court determined that it was a franchise fee imposed by Baskin upon Dean Foods for the right to sell Dean Foods products under the Baskin Robbins name. The Court characterized the fee as a pass-through cost from which Dean Foods did not make any profit and passed onto the franchisee purchasers. The Court looked to see if this was a permissible arrangement under the Franchise Agreement.

Despite no mention of a Commercial Factor, the agreement included a price provision, which stated that franchisees were obligated to pay the price of ice cream charged by Dean Foods. The Court found that Dean Foods pass-through costs were permissibly charged to the Association under the price provisions in various Franchise Agreements. The Court reasoned that this is a standard industry practice and, subject to certain limitations, the Association was also free to pass this charge along to its customers. The Court explicitly found that "a plain reading of the contract supports the interpretation that Baskin was entitled to derive revenue from franchisees by charging a franchise fee to Dean Foods, which Dean Foods then passes on to its purchasers."

Although the Court found no ambiguities in the contract, it analyzed the parties' course of dealing. When looking at the parties' course of performance, the Court noted that the Commercial Factor was consistently paid without objection despite the franchisee's clear knowledge that Baskin was entitled to revenue from the sale of its proprietary products. Baskin also disclosed to its franchisees that it reserved the right to receive fees or other consideration from suppliers in connection with its licensing of supply rights. Ultimately, the Court found that Baskin's disclosures, coupled with the franchisees' actions, favored Baskin's interpretation of the contract.

This decision provides just one significant example of the hidden costs and fees of entering into a franchise agreement. Although the Court reasons that franchisees are free to pass these costs along to their consumers, this is not a realistic or plausible solution. Franchisees are required to purchase from certain vendors and as a result, required to pay additional fees such as the Commercial Factor discussed here. Consumers, on the other hand, have free reign to shop and buy products from whomever they choose and if the same product is available from multiple sources, consumers will likely choose the most affordable option.

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2018 Judicial Update

Selected Arbitration and Forum Selection Clause Cases

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The recent year was no different from prior years at least insofar as the federal district courts were regularly presented with motions arising out of arbitration and forum selection clauses. Although there were no blockbuster decisions or words of wisdom from the Supreme Court, the decisions generally reinforce the basic principles: *first*, arbitration is favored and, therefore, a balanced and mutual arbitration provision will typically be enforced; *second*, although disfavored, a party may waive its right to compel arbitration; *third*, petitions to vacate an arbitration award are rarely granted; and *fourth*, motions to enforce forum selection clauses meet with mixed results, but the Supreme Court's decision in *Atlantic Marine Construction Co. v. the U.S. District for the Western District of Texas* is compelling support for such motions.

1. **Petitions to Compel Arbitration**

- ***Stockade Companies, LLC v. Kelly Restaurant Group, LLC*** **2017 WL 1968328 (W.D. Tex. May 11, 2017)**

This case has a somewhat unusual procedural posture — the franchisee was the party seeking to compel arbitration. The court's decision serves as a reminder that courts will carefully scrutinize the specific language of the parties' agreement in determining whether arbitration is appropriate.

Stockade Companies, LLC (Stockade) and Kelly Restaurant Group, LLC (Kelly) entered into fifteen franchise agreements granting Kelly a license to use Stockade's trademarks in the operation of Sirloin Stockade, Coyote Canyon, and Montana Mike's restaurants. Kelly failed to de-identify its restaurants after the franchise agreements were terminated, and Stockade filed suit in the U.S. District Court for the Western District of Texas to enjoin Kelly from infringing on its trademarks and to enforce the covenant not to compete in the franchise agreements. Kelly responded by filing a motion to compel arbitration and stay the lawsuit pending arbitration.

Each of the franchise agreements includes a broad arbitration clause requiring that "any and all controversies, claims and disputes between them arising out of or related to the [a]greement" be submitted to the American Arbitration Association (AAA) for binding arbitration. However, the franchise agreements also provide that Stockade "may, at its sole option, institute an action or actions for temporary or preliminary injunctive relief or seeking any other temporary or permanent equitable relief against [Kelly] that may be necessary to protect its Proprietary Marks or other rights or property . . ." (the Carve-Out Clause). The issues before the court were (i) whether Stockade's claims fit within the Carve-Out Clause, and (ii) whether the court or an arbitrator should make this determination.

The court first addressed the gateway issue of whether it or an arbitrator should decide if Stockade's claims were subject to arbitration. Citing longstanding Supreme Court precedent, the court noted that the question of arbitrability is "an issue for judicial determination [u]nless the parties clearly and unmistakably provide otherwise," and that the party claiming the question has been reserved to the arbitrator bears a heavy burden of proof. The franchise agreements did not include an express delegation

clause. Instead, Kelly argued that because the parties had agreed AAA's Commercial Rules of Arbitration applied, Rule 7 [Jurisdiction] of those Rules — which provides that the arbitrator has the power to rule on the scope of his or her own jurisdiction — also applied. The court rejected this argument, finding the general rule in the Fifth Circuit that adopting AAA's rules is "clear and unmistakable evidence that the parties agreed to arbitrate arbitrability" did not apply when the parties' agreement includes an express exclusion to the arbitration requirement. In making this finding, the court was persuaded by a recent decision from the Eastern District of Texas holding that "it would be senseless to have AAA rules apply to proceedings that are not subject to arbitration" because of an express carve-out provision. *See Archer and White Sales, Inc. v. Henry Schein, Inc.*, 2016 WL 7157421, at *7 (E.D. Tex. Dec. 7, 2016).

The court then turned to the question of whether Stockade's trademark infringement, false designation of origin, and covenant not to compete claims were arbitrable. Kelly argued (i) they were subject to arbitration because the claims were not "actions" within the meaning of the agreements and, therefore, did not fall within the Carve-Out Clause, (ii) they were not "necessary" to protect Stockade's property, and (iii) the Carve-Out Clause was vague. The court found these arguments to be "meritless" and contrary to the plain language of the arbitration provision.

The court characterized Kelly's first argument — that Stockade's claims were not "actions" within the meaning of the Carve-Out Clause because the clause "does not specify the forum and does not define 'action' to sufficiently distinguish it from a controversy, claim or dispute that is subject to arbitration" — as "illogical." The court found that the Carve-Out Clause was clear and that Stockade's claim for injunctive relief to protect its trademarks and to enforce the noncompete clause was "plainly" an action for injunctive relief relating to its propriety marks.

Kelly's second argument — that Stockade's request to enforce the noncompete provision fell outside the Carve-Out Clause — fared no better. The court agreed with Stockade that the language in the Carve-Out Clause permitting Stockade to seek injunctive relief to protect its "other rights" included a contractual right to enforce the covenant to compete.

Finally, the court addressed Kelly's argument that the Carve-Out Clause was vague and, therefore, all issues, including actions for injunctive relief, must be arbitrated. Kelly's theory was that the second sentence in the Carve-Out Clause, which states that "in [Stockade's] sole discretion, the final right of determination of the ultimate controversy, claim or dispute shall be decided by arbitration as aforesaid and recourse to the courts shall thereafter be limited to seeking an order to enforce the arbitral award," was somehow at odds with other portions of the Carve-Out Clause. The court held otherwise, reading the relevant portions of the Carve-Out Clause as giving Stockade the right to seek injunctive relief to protect its trademarks or enforce its "other rights or property," and giving Stockade the right to submit the ultimate issues (*e.g.*, liability) to arbitration if it was so inclined. The court found that Stockade's discretionary right to arbitrate the ultimate issues did not in any manner limit Stockade's right to seek the injunctive relief it was requesting from the court.

Accordingly, the court found that Stockade's claims for injunctive relief fell within the Carve-Out Clause and, therefore, denied Kelly's motion to compel arbitration.

- ***Mitnick v. Yogurtland Franchising,* Inc.**
  2017 WL 3503324 (D.N.J. Aug. 16, 2017)

This case is noteworthy mostly for the reason that it exemplifies the extent to which some parties will go to avoid arbitration. Plaintiff, as the assignee of Central Jersey Enterprises, LLC (CJE), filed a lawsuit against Yogurtland Franchising, Inc. and others (collectively, Yogurtland) in the U.S. District Court for the District of New Jersey asserting claims arising out of a number of franchise agreements. Yogurtland filed a motion to compel arbitration and stay the litigation, which the court granted.

CJE and Yogurtland entered into seven separate franchise agreements pursuant to which CJE operated Yogurtland franchises in New Jersey and Pennsylvania. CJE ultimately became insolvent and conveyed its assets to Plaintiff in an assignment for the benefit of creditors (ABC).

Each of the franchise agreements includes provisions requiring arbitration of any disputes "arising out of or relating to" the franchise agreements. However, there were some differences in the provisions. The arbitration provisions in two of the franchise agreements (the 2010 and 2011 Franchise Agreements) require that the arbitration be administered by AAA in accordance with its rules. The arbitration provisions in the five remaining agreements require that the arbitration be administered by a "reputable arbitration service[], including CPR, JAMS, and other services of equally good quality." The 2010 and 2011 Franchise Agreements also include an exception to the arbitration requirement for "any matter within the jurisdiction of a probate . . . or bankruptcy court" (the Exception Clause).

Although there were some differences in the exact language of the provisions, each of the franchise agreements include a provision requiring that the parties participate in a mediation before resorting to arbitration. The Exception Clause in the 2010 and 2011 Franchise Agreements also exempts matters within the jurisdiction of a probate or bankruptcy court from mediation.

Plaintiff did not contest the validity of the arbitration and mediation provisions or that CJE's claims arose of out of the franchise agreements. Rather, he argued that: (i) the Exception Clause in the 2010 and 2011 Franchise Agreements were triggered because the claims were subject to the jurisdiction of either the probate or bankruptcy courts; (ii) the court could not order arbitration because the arbitration provisions did not require a uniform method of arbitration; and (iii) in the event the court were to compel arbitration, it should order the parties to first participate in a mediation as required by the franchise agreements.

The court first addressed Plaintiff's argument that the Exception Clause applied. The court noted that although probate courts in New Jersey have the power to issue ABCs, they do not have the power to actually adjudicate any substantive claims asserted by an assignee following an ABC. The court also noted that the Exception

Clause only applied to matters "*within* the jurisdiction of a probate . . . court." Accordingly, because Plaintiff's claims arose out of the franchise agreements and did not in any manner implicate the jurisdiction of the probate court, the court held that the probate court exception was inapplicable.

Plaintiff's argument that the lawsuit was within the bankruptcy court's jurisdiction was similarly unsuccessful. Plaintiff theorized that because the claims were brought as an assignee of an insolvent company (CJE), the case was "similar in effect" to a Chapter 7 bankruptcy proceeding. The court rejected this argument, finding that although CJE may have been insolvent, it had not filed a petition for relief with a bankruptcy court. Therefore, Plaintiff's claims were not within the jurisdiction of the bankruptcy court.

The court then turned to Plaintiff's argument that arbitration should not be ordered because there were differences in the arbitration provisions in the franchise agreements. The court found that the differences in the rules governing the arbitrations were "trivial" and did not preclude it from compelling arbitration. Further, the court concluded that the arbitration provisions were not actually incompatible because the five agreements requiring that the arbitration be administered by a "reputable arbitration service[], including CPR, JAMS, and other services of equally good quality" would permit the arbitration to be administered by AAA.

Finally, the court addressed Plaintiff's argument that the parties should be required to mediate. Yogurtland argued that Plaintiff had waived the right to require pre-arbitration mediation by filing the lawsuit. The court concluded that the issue was "procedural" in nature and, therefore, should be submitted to the arbitrator for determination.

Therefore, despite Plaintiff's multipronged attack on the arbitration provisions in the franchise agreements, the judicial preference for enforcing such provisions — even in the absence of identical terms — was reinforced.

2. **Waiver**

- ***Money Mailer, LLC v. Brewer***
  2017 WL 3017539 (W.D. Wash. July 7, 2017)

The question of whether a party has waived its right to compel arbitration is inherently fact-specific and courts are generally reluctant to find a waiver. In this case, however, the U.S. District Court for the Western District of Washington found that counter-defendant Money Mailer Franchise Corporation (MMF) had waived its right to compel one of its former franchisees (Brewer) to pursue his claims through arbitration based on the litigation conduct of an entity affiliated with MMF.

Prior to becoming a franchisee, Brewer received a Franchise Disclosure Document (FDD) from MMF disclosing that (i) its franchisees are required to contract directly with Money Mailer, LLC (MMLLC) for the purchase of mailing production

services and materials, and (ii) the franchise agreement contains a mandatory arbitration clause. MMLLC's standard purchase terms and contract, a form of which was attached to the FDD, does not mention arbitration. The parties' franchise agreement includes a provision requiring arbitration of any dispute "arising out of or relating to" the agreement, as well as a provision requiring Brewer enter into a separate agreement with MMLLC and stating that that such agreement was *not* subject to the arbitration provision in the franchise agreement. Brewer claims that he never signed a separate agreement with MMLLC.

For several years, Brewer was regularly billed by MMLLC for amounts owed to both it and MMF. However, beginning in 2012, Brewer began challenging the bills. In 2015, Brewer received a single notice of default on letterhead for both MMLLC and MMF asserting that in excess of $1.6 million was owed to both entities.

Brewer failed to pay the amounts demanded and MMLLC filed suit. In turn, Brewer filed a number of counterclaims against both MMLLC and MMF, to which MMF responded by filing a motion for summary judgment on the ground Brewer was required to pursue all claims against MMF in arbitration. MMF also contended that the arbitration requirement did not extend to MMLLC's claims because such claims were the subject of a separate agreement that did not include an arbitration clause. The court denied MMF's motion for summary judgment, finding that that issue of waiver was a gateway issue appropriately decided by the court rather than by an arbitrator and there was a genuine issue of material fact whether MMF had waived its right to compel arbitration by seeking to recover amounts owed to it through MMLLC.

MMF filed a motion for reconsideration, which the court granted in part and denied in part. MMF filed a second motion for summary judgment on the same ground as before, but also included additional evidence that MMLLC had only filed suit to recover amounts owed to it. In opposition, Brewer argued that MMF had waived its right to arbitrate as a result of its conduct in the litigation.

As a threshold matter, the court noted that because waiver of a right to arbitrate is disfavored, the party claiming waiver "bears a heavy burden of persuasion." Thus, in order to prevail, the court held that Brewer would need to establish MMF knew that it had the right to compel arbitration, MMF acted in a manner that was inconsistent with that right, and Brewer was prejudiced as a result of MMF's inconsistent acts.

The court framed the central issue as whether the lawsuit filed by MMLLC against Brewer "constituted acts" by MMF that were inconsistent with its contractual right to arbitrate Brewer's counterclaims. The gist of MMF's argument was that it was not involved in the litigation until it was named as a counter-defendant and that MMLLC's actions in the ligation could not be attributed to MMF for purposes of finding a waiver. In response, Brewer argued that MMF and MMLLC were alter egos and, therefore, the lawsuit filed by MMLLC waived MMF's right to arbitration.

The new evidence from MMF included a declaration from its CFO in which he stated that the amounts owed to MMF and MMLLC were separately accounted for by

MMLLC even though MMLLC billed Brewer for amounts owed to MMF. Spreadsheets purportedly reflecting that the amount sought in the lawsuit was all owed to MMLLC (and not to both MMF and MMLLC) were also included with the declaration. Not surprisingly, Brewer disputed the declaration and argued, among other things, that MMF had shifted amounts owed to it to "MMLLC's side of the ledger."

As an initial matter, Brewer argued, and the court agreed, that MMLLC's claim arose from the franchise agreement. Although MMLLC alleged that its claim arose from a separate agreement — *i.e.*, MMLLC's standard purchase terms and conditions attached to the FDD — it was unable to produce a signed copy of the agreement. In the absence of a written agreement, the court concluded there was no contractual basis for MMLLC's claims and, therefore, the exemplar contract attached to the FDD formed the basis for MMLLC's claim through incorporation into the franchise agreement.

Ultimately, however, it was irrelevant whether the arbitration clause in the franchise agreement applied to MMLLC's claims because the court found that MMLLC was seeking to recover sums owed to *both* it and MMF as evidenced by the declaration submitted by MMLLC's CFO and the accompanying spreadsheets. The court held that such documents showed an "intermingling" of the amounts owed, including credits from MMF being applied to reduce the amount owed to both entities and payments from Brewer being applied to Brewer's collective debt rather than separately to his debts to MMF and MMLLC. The court was further persuaded that because Brewer did not make separate payments for amounts owed to MMF and MMLLC, but rather made single payments, it was "impossible" to determine the amount owed to one entity versus the other and the fact that a spreadsheet had to be created for purposes of MMF's motion for summary judgment suggested it was MMLLC's "routine business practice to account for both sets of debts as one." Accordingly, the court found that MMLLC's lawsuit to recover amounts owed to MMF was inconsistent with MMF's right to arbitrate.

Having reached this conclusion, the court then addressed the third element required to establish waiver — prejudice. The court found that Brewer was prejudiced by having to defend the claims to recover amounts owed to MMF in the litigation while being forced to arbitrate other disputes with MMF.

Accordingly, the court found that Brewer met his burden of proving that MMF had waived its right to arbitration and, therefore, denied MMF's motion for summary judgment and alternative motion to compel arbitration.

3. **Motions to Vacate**

Petitions to vacate an arbitration award are rarely granted and these cases are no exception.

- ***Stevens v. Jiffy Lube Int'l, Inc.***
  231 F. Supp. 3d 434 (N.D. Cal. 2017)

The U.S. District Court for the Northern District of California denied a former franchisee's motion to vacate an arbitration award in favor of Jiffy Lube International, Inc. (Jiffy Lube) stemming from a dispute regarding the termination of the franchise agreement.

After Plaintiffs lost the right to possess the location at which they operated their franchised business, Jiffy Lube issued a non-curable notice of default. The franchise agreement was terminated in June 2013, and Plaintiffs filed an action in California state court in February 2015. Jiffy Lube subsequently removed the case to federal court and filed a petition to compel arbitration. The parties ultimately stipulated to arbitration and the lawsuit was dismissed on September 3, 2015. The parties' stipulation provides, among other things, that Jiffy Lube would waive the two-year contractual statute of limitations with respect to the claims asserted in the complaint — but not as to "any other rights regarding limitations" — so long as Plaintiffs initiated the arbitration within one month of the dismissal of the federal court.

Plaintiffs filed a demand for arbitration on September 30, 2015 and a Statement of Claim on October 26, 2015. Plaintiffs amended their Statement of Claim on two occasions, the latter of which added a claim that Jiffy Lube violated the California Franchise Relations Act (CFRA). After an evidentiary hearing, the arbitrator generally ruled in Jiffy Lube's favor, finding, among other things, that the CFRA claim was barred by the two-year contractual statute of limitations provision in the franchise agreement because the claim was asserted for the first time in the Amended Statement of Claim filed in May 2016. Plaintiffs filed a motion to vacate the arbitrator's determination that the CFRA was barred by the applicable statute of limitations.

The court started its analysis by noting that although Section 10 of the Federal Arbitration Act (FAA) sets forth limited grounds to vacate an arbitration award, the Ninth Circuit has adopted several modest clarifications of the grounds upon which an arbitration award may be vacated, including if the arbitrator "manifestly disregarded the law," or the arbitration award is "completely irrational." With respect to the manifest disregard of the law exception, it is a "narrow" exception and a mere error in the law or failure to understand, or properly apply, the law will not suffice. Rather, there must be compelling evidence that the arbitrator was aware of the law and intentionally ignored it.

The court first considered, without deciding, Jiffy Lube's argument that Plaintiffs' motion to vacate was untimely because it was not filed "within three months after the award [was] filed or delivered" as required by Section 12 of the FAA. Jiffy Lube took the position that because the arbitrator's award was emailed to the parties on September 14, 2016, the motion to vacate needed to be filed by no later than December 14, 2016, and that it was untimely because it was filed one day later. In response, Plaintiffs pointed to the fact that the FAA does not specify the method for computing time. Therefore, Plaintiffs' argued that Federal Rule of Civil Procedure 6(a) applied, which provides that the day of the event that triggers the period is excluded for purposes of calculating the time. The court declined to decide the matter, noting there was conflicting authority regarding this issue and instead elected to consider the rest of Plaintiffs' arguments.

The court then turned to the substance of Plaintiffs' motion. Plaintiffs argued that (i) the arbitrator manifestly disregarded the law, or (ii) his decision was "completely irrational" because the doctrines of equitable tolling and relationship back applied and, therefore, the CFRA claim was not time-barred. The court disagreed.

The court held that even if the CFRA claim was saved by the equitable tolling and relationship back doctrines saved the CFRA claim, something more than a "mere error in the law or failure on the part of the arbitrator[] to understand and apply the law" was required to overturn the arbitrator's ruling. Rather, the arbitrator must have must been both aware of the law and chosen to "intentionally disregard it." The court found there was no evidence that the arbitrator was aware of the law regarding equitable tolling or the relation back doctrine. The court also rejected Plaintiffs' assertion that the arbitrator had prevented them from addressing these issues at the arbitration. The court found that the arbitrator had expressly withheld making any ruling on the issue of whether the CFRA claim was barred by the statute of limitations when he permitted Plaintiffs to add the claim. The court further found that Plaintiffs had addressed the statute of limitations issue in their arbitration briefing, but had not argued either that the statute of limitations was equitably tolled or that the CFRA claim related back to the initial pleading.

- ***System4, LLC v. Ribeiro***
  275 F. Supp. 3d 297 (D. Mass. 2017)

The U.S. District Court for the District of Massachusetts denied a franchisor's petition to vacate an arbitration award finding that its franchisee was an employee under the Massachusetts Wage Act (the Wage Act).

Defendant System4, LLC (System4) is a franchisor of commercial cleaning and facility services management businesses. A group of System4's unit franchisees filed a putative class action against it and one of its master franchisees in Massachusetts state court, claiming they were improperly classified as independent contractors in violation of the Wage Act. System4 filed a motion to compel Plaintiffs to pursue their claims in arbitration on an individual basis. The Massachusetts Supreme Judicial Court granted the motion and Plaintiff Luis Ribeiro (Ribeiro) filed a demand with the American Arbitration Association (AAA).

At the outset of the arbitration, Ribeiro requested that the arbitrator make an initial determination that AAA's Employment Rules applied and that System4 bear the costs of the arbitration proceeding. After the parties briefed the issue, the arbitrator determined that she would apply the AAA Employment Rules because Ribeiro was likely to prevail in his claims under the Wage Act and ordered System4 to advance the costs of the arbitration. However, the arbitrator indicated this was a preliminary ruling and that System4 could revisit the issue of whether Ribeiro was properly classified as an independent contractor.

The parties ultimately filed cross-motions for summary judgment. In ruling on these motions, the arbitrator found that: (i) Ribeiro's claims were not barred by the statute of limitations because Ribeiro was a member of the putative class and, therefore, his claims were subject to the class action tolling doctrine; and (ii) Ribeiro should have been classified as an employee, and not as an independent contractor, under the Wage Act. System4 filed a motion for reconsideration of the arbitrator's ruling regarding Ribeiro's status, which the arbitrator denied on the ground it failed to meet the standard for reconsideration. System4 subsequently filed three motions against Ribeiro's counsel for allegedly violating the confidentiality clause in the franchise agreement and to recover attorneys' fees and costs related to the state court litigation. The arbitrator denied these motions as well. Thereafter, the arbitrator issued her decision (the Award).

System4 filed a petition to vacate the Award and the rulings set forth above on the grounds there was "evident partiality by the arbitrator" and she exceeded her powers. Before addressing System4's arguments, the court set forth the relevant principles and standards applicable in the First Circuit, including that the court's review is "extremely narrow and exceedingly deferential," arbitral awards are "nearly impervious to judicial oversight," and the moving party has the burden of establishing something "substantially more than an erroneous conclusion of law or fact." With this daunting backdrop, the court turned to System4's arguments.

A finding of evident partiality requires more than an appearance of potential bias; rather, the evidence must be such that a "reasonable person" would conclude the arbitrator was "partial to one party." Although System4 had not raised the partiality issue during the arbitration proceedings, the court nonetheless addressed the merits of System4's claims. System4 asserted that there was evident partiality because: (i) the arbitrator undertook an independent investigation into the procedural history of the state court case and included a summary of that history in her decision on the parties' cross-motions for summary judgment; (ii) the arbitrator ruled in Ribeiro's favor on the statute of limitations issue even though he had not filed an opposition; and (iii) the arbitrator did not undertake an independent investigation into one of System4's arguments in support of its motion for attorneys' fees and costs.

The court rejected System4's arguments, finding there was no evidence the arbitrator reviewed the state court procedural history because she believed it would be to Ribeiro's benefit and System4 had failed to identify any fact regarding the state court procedural history that was either in the interest of or more favorable to Ribeiro. The court found that contrary to System4's argument, Ribeiro had opposed System4's argument regarding the statute of limitations issue. Moreover, System4's general arguments were that the arbitrator had ruled against System4, which does not alone evidence bias. Accordingly, the court found that System4 had failed to meet its "high burden of demonstrating 'objective facts inconsistent with impartiality.'"

The court then addressed System4's arguments that the arbitrator had exceeded her powers by failing to "adhere to the clear and unambiguous terms of the franchise

agreement," and manifestly disregarding the law "in each and every one of her major decisions in the case."

System4 contended that the arbitrator had not adhered to the requirements of the franchise agreement because she refused to (i) apply the AAA Commercial Arbitration Rules as required by the agreement, (ii) enforce the confidentially provision, and (iii) enforce the attorneys' fees and costs provision. The court found that although the arbitrator applied the AAA Employment Rules in holding that System4 should advance the costs of the arbitration, the Award was not based on the application of those Rules. Rather, the Award was "based on her determination that Ribeiro was an employee" and, therefore, System4 had violated the Wage Act by classifying him as an independent contractor. And under Massachusetts law, the Wage Act "override[s]" a contractual agreement to split the costs of arbitration if the plaintiff prevails on the Wage Act claims. The court rejected System4's other arguments that the arbitrator had not adhered to the additional terms of the franchise agreement, finding that the arbitrator had not refused to enforce such provisions, but rather had considered the motions and ruled against System4.

System4 further claimed that the arbitrator manifestly disregarded the law in her decisions on the misclassification issue and the statute of limitations defense. As the court noted, a party claiming manifest disregard has the burden of proving that the arbitrator knowingly ignored the applicable law. The court concluded that the record revealed the arbitrator "carefully considered — and rejected — System4's arguments." Specifically, the arbitrator analyzed the relevant law, both favorable and unfavorable to the parties, and made a decision.

4. **Forum Selection Clauses**

- ***ServiceMaster of Fairfax, Inc. v. ServiceMaster Residential/Commercial Servs., L.P.***
  2017 WL 3023342 (D. Md. July 17, 2017)

This case illustrates the continuing impact of the Supreme Court's decision in *Atlantic Marine Construction Co. v. U.S. District Court for the Western District of Texas*, 134 S. Ct. 568 (2013) (*Atlantic Marine*) on the enforceability of forum selection clauses.

ServiceMaster of Fairfax, Inc. (Plaintiff) entered into four franchise agreements with ServiceMaster Residential/Commercial Services, L.P. (ServiceMaster) to operate ServiceMaster businesses in the District of Columbia, Virginia, and Maryland. Each franchise agreement includes a forum selection clause requiring all litigation be venued exclusively in Memphis, Tennessee, which is ServiceMaster's principal place of business. One of the franchise agreements includes an addendum, which provides that "[t]he Maryland Franchise Registration and Disclosure Law [Maryland Franchise Law] allows a franchisee to bring a lawsuit in Maryland for claims arising under this law."

Plaintiff filed a lawsuit in Maryland state court naming ServiceMaster and others as defendants (Defendants) asserting a number of claims, including alleged violations of

the Maryland Franchise Law. Defendants removed the case to the U.S. District Court for the District of Maryland and filed a motion to transfer the matter to the U.S. District Court for the Western District of Tennessee pursuant to 28 U.S. § 1404(a) based on the forum selection clauses in the franchise agreements.

As a preliminary matter, the court addressed the impact of the Supreme Court's decision in *Atlantic Marine* on a § 1404(a) motion to transfer. As the Court said, "the calculus changes when the parties' contract contains a valid forum-selection clause . . . [which should be] given controlling weight in all but the most exceptional cases." Thus, in the event of a valid forum selection clause, (i) the plaintiff's choice of forum is given no weight and plaintiff bears the burden of demonstrating that a transfer to the designated forum is "unwarranted"; (ii) the parties' interests (*i.e.*, convenience of the parties/witnesses and the other "private interest factors") are irrelevant and the court may only consider the public interest factors; and (iii) the choice of law rules of the venue in which the lawsuit was filed do not apply.

The court also noted that *Atlantic Marine* involved a mandatory selection clause and the Fourth Circuit has yet to address whether *Atlantic Marine* applies to a permissive forum selection clause. The court concluded, however, that the "majority" of post-*Atlantic Marine* cases that have considered the issue have not applied its rulings to a permissive forum selection clause.

Thus, the court started its analysis by determining whether the forum selection clauses in the franchise agreements were mandatory or permissive. The court concluded that the clauses were on their faces mandatory because each provided that "all litigation . . . must and will be venued exclusively in Memphis, Tennessee." The court noted, however, that its analysis did not stop there because there were other relevant provisions in the franchise agreements. First, the above quoted language in the forum selection clause was preceded by a qualification — "[u]nless the law applied in accordance with Paragraph 25.1 of this Agreement provides otherwise . . . ." Second, Paragraph 25.1 provides that the laws of Tennessee apply *unless* the state in which the franchisee was doing business requires that the law of that state applies. And third, the addendum to one of the franchise agreements states that "[t]he [Maryland Franchise Law] allows a franchisee to bring a lawsuit in Maryland for claims arising under this law."

The court found that the language in the addendum was a permissive exception in that a subcategory of claims (*i.e.*, those alleging violations of the Maryland Franchise Law) *may* be brought in Maryland. The court concluded that this did not "alter the mandatory nature" of the forum selection clauses and that other courts had reached the same conclusion. The court also noted that "unless the law applied in accordance with Paragraph 25.1 of the agreement provides otherwise" language would be rendered meaningless if the forum selection clauses were not mandatory. As the court explained, the effect of Paragraph 25.1 was to identify the sole exception to the mandatory nature of the forum selection clauses — *i.e.*, when the law of the state (in this case Maryland) requires that a lawsuit be brought elsewhere. Here, the addendum does not mandate that the lawsuit be filed in Maryland. Rather, it simply "allows" for that alternative.

Having concluded the forum selection clauses were mandatory and, therefore, *Atlantic Marine* applied, the court then considered the public interest factors, which include "the administrative difficulties flowing from court congestion; the local interest in having localized controversies decided at home; [and] the interest in having the trial of a diversity case in a forum that is at home with the law." Plaintiff made two arguments, neither of which the court found persuasive.

First, Plaintiff argued that Maryland maintains an interest in deciding the case because "the vast majority of the alleged conduct occurred in the state." The court rejected this argument because Plaintiff failed to provide any factual support for this assertion and the Complaint simply alleged that Plaintiff's territory includes parts of Maryland. Second, Plaintiff asserted that Maryland law governs and, therefore, the case should be handled by a court familiar with Maryland law. The court noted that this factor is "given significantly less weight when the case involves basic or sufficiently well-established . . . issues of state law or when there is no reason to believe that the applicable law of forum differs markedly from the law of the proposed transferee state." Here, the Complaint alleged claims based on Virginia and Maryland law arising from franchise agreements executed in Tennessee for franchises in the District of Columba, Maryland, and Virginia. Therefore, because the law of several jurisdictions were involved, the law of no single jurisdiction (including Maryland) would govern the entire case. Accordingly, the court found familiarity with Maryland laws was "not outcome determinative."

Thus, the court enforced the forum selection clauses and granted ServiceMaster's motion to transfer.

- ***Zounds Hearing Franchising, LLC v. Bower***
  2017 WL 4399487 (D. Ariz. Sept. 15, 2017)

To say that this case did not go well for the franchisor is an understatement. The court thoroughly rejected the franchisor's arguments regarding the enforceability of the venue and choice of law provisions in the parties' franchise agreements, seemingly questioned the franchisor's motivations, and capped off its decision by awarding attorneys' fees to the franchisees.

Zounds Hearing Franchising, LLC (Zounds) is the franchisor of Zounds' hearing aid centers (together with its parent company, Zounds). Four Ohio companies and their owners (Franchisees) entered into franchise agreements with Zounds to operate Zounds hearing aid centers in Ohio. The franchises "fared poorly" and the Franchisees filed a lawsuit in Ohio state court asserting that Zounds violated the Ohio Business Opportunity Purchasers Protection Act (the Act) by, among other things, not including a five-day right to cancel provision in the franchise agreements and making false/misleading representations regarding the franchise opportunity. Zounds removed the case to the U.S. District Court for the Northern District of Ohio and filed a motion to dismiss or transfer the case to Arizona based, at least in part, on the forum selection and choice of law provisions in the franchise agreements. The Ohio federal court did not address these arguments, but nonetheless transferred the case to Arizona based on

the convenience of the parties and witnesses pursuant to 28 U.S.C. § 1404(a). While the motion to dismiss or transfer was pending, Zounds filed four separate complaints for declaratory relief in the U.S. District Court for the District of Arizona, which were consolidated.

Before the court was Zounds' renewed motion to dismiss the Franchisees' complaint or to stay the proceedings pending mediation. The central issue was whether the Act's prohibition on out-of-state venue and choice-of-law provisions trumped the Arizona venue selection and choice-of-law clauses in the franchise agreements. In answering this question with a resounding yes, the court applied what it characterized as the "highly abstract methodology" of the Restatement (Second) of Conflict of Laws §§ 187 and 188 ("Restatement").

The court distilled the relevant guiding principles from the Restatement as follows: (i) "the law of the state with the most significant relationship to the transaction and parties governs"; (ii) however, the parties may elect to apply the law of another state; (iii) provided such law would not be contrary to the fundamental policy of the state with the most significant relationship to the parties and their affairs and that state has a "materially greater interest than the chosen state in the determination of the particular issue."

The court then turned to the first question — which state has the most significant relationship to the transaction and parties. The court noted that "[w]here people are not allowed to do things in a state, the chosen exercise of the police power of the state would be defeated by allowing parties to grant themselves extraterritoriality by contact. On such issues, the location of the conduct will usually trump all other considerations." With this backdrop, the court found that the prohibition on financial representations not included in the FDD and other requirements/provisions of the Act "go to the core of minimum business fairness and honesty" that is statutorily required in the sale of franchises in Ohio. Thus, the court concluded that the "Ohio domicile, situs, and statutory purpose of investor protection outweigh any factors favoring application of any other state's laws . . . [and] far outweigh any theoretical interest of Arizona in enabling its residents, by virtue of their Arizona domicile and superior bargaining power, to project Arizona *laissez faire* investment policy into states that protect buyers, wherever domiciled, of investments in their state through disclosures and prohibition of contract terms." Accordingly, the court found that the "state where the franchise is located and the franchisee is domiciled will always have the most significant relationship to the transaction and the parties if that state's investor protection laws are stronger and there is a conflict between that law and the law of the chosen state."

The court next addressed whether Arizona law is contrary to Ohio's fundamental policy. The court found that the "heightened protections" in the Ohio statute, which it characterized as "mandatory, complete, and true written disclosures," were at the core of the lawsuit. Accordingly, the court held that "[t]he Ohio franchise regulation statutes and those in similar states always reflect fundamental policy of the state, and a contractual choice of the law of a less protective state cannot defeat the state's protection for an in-state franchise and franchisee." The court further noted that the

2012 amendments to the statute expressly stated that it "represents a fundamental public policy of this state," and for good measure stated that Ohio is the "franchisee protection state on steroids."

Finally, the court concluded the Arizona choice-of-law and forum selection provisions in the franchise agreements provisions were invalid under the Act, which provides that "any provision in an agreement restricting jurisdiction or venue to a forum outside this state, or requiring the application of laws of another state, is void . . . ." Therefore, the court transferred the action back to Ohio.

The court then considered Zounds' motion that the Franchisees be compelled to participate in individual mediations in Arizona as required by the terms of the franchise agreements. The court found that the mediation requirement was a prerequisite to filing suit and, therefore, was prohibited by the Act because it voids any contractual provision requiring that any litigation occur outside of Ohio. The court also rejected Zounds' argument that it would be prejudiced by having to participate in a consolidated mediation, commenting that the Franchisees would be prejudiced by having to incur the fees and costs of four separate mediations involving the same issues. However, the court left the question of whether to have individual or consolidated mediations to an Ohio Magistrate Judge to decide.

Based on its rulings, the court then entered declaratory judgment against Zounds in the consolidated Arizona actions on the grounds that the forum selection, choice-of-law, and mediation clauses in the franchise agreements were invalid and unenforceable under the Act. As the coup de grace, the court awarded attorneys' fees to the Franchisees based on Arizona statute. The court characterized the one-way attorneys' fees provision in the franchise agreement as "odious" and commented that it "should be an abuse of discretion not to award attorney fees against an unsuccessful party who used its superior bargaining power to impose such a term."

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2018 Judicial Update

State Statutory Law Summary

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A major component of franchise regulation involves the enforcement of state registration and relationship statutes along with consumer protection laws. Just as in past years, courts in 2017-2018 confronted these state regulatory schemes and their interplay with federal and state common law in fascinating and, at times, creative ways. From trucking distributorships, to breweries and wine distributors, to a fitness franchise in Kentucky, the decisions below demonstrate that courts continue to show an affinity for requiring parties to look at the intent of these statutes in their efforts to dispose of claims brought under them.

1. ***859 Boutique Fitness, LLC v. CycleBar Franchising, LLC*** **699 F. App'x 457 (6th Cir. 2017)**

Putative franchisee brought an action in state court against franchisor of indoor-cycle fitness studios asserting negligent and fraudulent misrepresentation claims and claim under the Kentucky Consumer Protection Act ("KCPA"). Franchisor removed and filed a motion to dismiss. The district court granted franchisor's motion to dismiss holding that franchisee failed to state a claim for violation of the KCPA because the Act only provides a private cause of action to a purchaser for personal, family, or household purposes. The district court dismissed the common law claims and found that franchisee failed to **allege** a causal relationship between the alleged misrepresentations and any injury with the particularity required by Fed. R. Civ. P. 9(b). The court dismissed the action without prejudice and permitted the franchisee to amend. Franchisee amended the pleading and the franchisor filed another motion to dismiss for failure to state a claim. The district court again granted franchisor's motion holding that franchisee still failed to show a connection between the alleged misrepresentation and any damages suffered. Franchisee appealed.

Before the Sixth Circuit, the franchisee argued that franchisor violated the KCPA by engaging in "unfair, false, misleading or deceptive acts or practices in the conduct of their trade and/or commerce." In dismissing this claim, the district court had found that "the KCPA only provides a private cause of action for an individual who 'purchases or leases goods or services primarily for personal, family, or household purposes.'" (quoting Ky. Rev. Stat. § 367.220(1)). On appeal, franchisee argued that Ky. Rev. Stat. § 446.070 establishes a private right of action to those injured by a violation of a statute which is penal in nature or which does not prescribe the remedy for its enforcement or violation. The court disagreed and affirmed the district court ruling, concluding that the franchisee failed to allege that it was a purchaser or lessee for personal, family, or household purposes as required by the statute and, as such, failed to state a claim under the KCPA.

As to franchisee's negligent and fraudulent misrepresentation claims, the franchisee claimed on appeal that the district court applied the relevant pleading standards too strictly. Under the oft-stated rule, a party alleging fraud must state with particularity the circumstances constituting fraud or mistake. This generally requires a plaintiff to specify: (1) what the fraudulent statements were, (2) who made them, (3) when and where the statements were made, and (4) why the statements were

fraudulent. Under Kentucky law, negligent misrepresentation claims are subject to these same heightened pleading requirements. In addition, to establish fraudulent misrepresentation under Kentucky law, a plaintiff must prove by **clear and convincing evidence**: (1) that the declarant made a material representation to the plaintiff, (2) that this representation was false, (3) that the declarant knew the representation was false, (4) that the declarant induced the plaintiff to act upon the misrepresentation, (5) that the plaintiff relied upon the misrepresentation, and (6) that the misrepresentation caused injury to the plaintiff. In its decision affirming the district court decision, the Sixth Circuit emphasized that the plaintiff's reliance on any misrepresentation must be "justifiable."

The district court dismissed franchisee's negligent and fraudulent misrepresentation claim because franchisee failed to show a causal nexus between the alleged misrepresentation – that franchisor had executed the Franchise Agreement – and any specific injury. On appeal, the Sixth Circuit noted that had franchisee alleged a claim of negligent and fraudulent misrepresentation that spanned the entirety of its dealings with franchisor, franchisee likely would have met the pleading requirements. However, franchisee pled its misrepresentation claim as beginning on the day the alleged misrepresentation was made and ending two days later on the day the franchisor notified franchisee that it had not and would not execute the contract. The franchisor refunded the franchisee's initial fees, and in the eyes of the Court of Appeals the franchisee failed to plead with particularity any injury resulting from the limited misrepresentation claim.

2. *S. Glazer's Distributors of Ohio, LLC v. Great Lakes Brewing Co.* 860 F.3d 844 (6th Cir. 2017)

Great Lakes, a craft beer manufacturer, entered into a distribution agreement with Ohio Glazer's, a distributor in the Columbus, Ohio beer market. Ohio Glazer's was a subsidiary of a larger company. Glazer's and another large distributer merged. Great Lakes subsequently sought to end its relationship with Glazer's because Glazer's executed the merger without seeking Great Lakes' consent, which the contract required. Distributor moved to preliminarily enjoin the termination arguing that the contract's consent requirement was invalid under Ohio law. The district court agreed, and the brewing company appealed.

The parties' agreement set out the conditions under which a party could terminate the distribution agreement. Specifically, the agreement provided that the manufacturer may terminate the agreement for cause immediately upon written notice of the occurrence of certain events not subject to cure, including distributor undertaking an ownership change without written consent as required by the agreement. Following the merger, the manufacturer gave notice to distributor of termination and set the effective termination date for sixty days from the date of the notice – even though the agreement authorized manufacturer to terminate without a notice period.

The four traditional factors guided the district court's decision to grant a preliminary injunction: (1) whether the movant had a strong likelihood of success on the

merits; (2) whether the movant would suffer irreparable injury absent the injunction; (3) whether the injunction would cause substantial harm to others; and (4) whether the public interest would be served by the issuance of an injunction. In analyzing these elements, the district court noted that the distributor's case requires a court to conclude that the consent provision is invalid under the Ohio Alcoholic Beverages Franchise Act (the "Ohio Franchise Act").

The Ohio Franchise Act imposes two requirements on all written franchise agreements that were critical to plaintiff's case. First, it legislates a "just cause" requirement into every franchise agreement: "[N]o manufacturer or distributor shall cancel or fail to renew a franchise . . . without the prior consent of the other party for other than just cause and without at least sixty days' written notice...." (quoting Ohio Rev. Code § 1333.85). Second, while the Act encourages manufacturers and distributors to enter into written franchise agreements, it renders "void and unenforceable" "[a]ny provision of a franchise agreement that waives any of the prohibitions of, or fails to comply with, [the Act]. (quoting Ohio Rev. Code § 1333.85). Distilled to its essence, the first clause prohibits manufacturers from failing to act in good faith in accordance with reasonable standards for fair dealing with respect to a distributor's right to sell its business. Contrary to distributor's claims, the Sixth Circuit found that the parties' agreement did not waive that prohibition. The relevant provision of the parties' agreement specifically states that manufacturer cannot unreasonably withhold its consent and must exercise reasonable business judgment in deciding whether to consent to a change of ownership. The court held that there was no meaningful inconsistency between this provision and the Ohio Franchise Act. For this reason, at least as to the first argument asserted, the Sixth Circuit held that distributor likely would not succeed on the merits such that the injunction should not stand.

As to the second assertion, the Sixth Circuit found that plaintiff had established that it would likely suffer irreparable harm in the absence of a preliminary injunction due to the manufacturer's unique position in the beer market. The court acknowledged that when a distributor loses a unique product such as this, it threatens the distributor's relationship with the retailers that have come to rely on the distributor for in-demand product. Such loss of customer goodwill was, in the eyes of the Sixth Circuit, a prime example of an intangible, irreparable harm.

With respect to the third factor, the Sixth Circuit held that there was no indication that enjoining the beer manufacturer from terminating its franchise would harm third parties such that the Court determined it would favor granting the injunction. However, on the fourth injunctive factor, the Court found that the public has a strong interest in holding private parties to their agreements and in enforcing the Ohio Franchise Act, which weighed against granting the injunction. Ultimately, the Court held that the district court committed error and necessarily abused its discretion in granting the preliminary injunction. Accordingly, the Sixth Circuit reversed and remanded.

3. ***Andy Mohr Truck Ctr., Inc. v. Volvo Trucks N. Am.*** **869 F.3d 598 (7th Cir. 2017)**

Manufacturer sought declaratory judgment that it was entitled to terminate dealer's dealership agreement because dealer had allegedly misrepresented a material fact in connection with its dealer application – that it would build a new long-term facility for the dealership if manufacturer awarded the contract to dealer. Dealer then alleged that manufacturer had violated the Indiana Franchise Disclosure Act ("IFDA") and the Indiana Deceptive Franchise Practices Act ("IDFPA") after manufacturer allegedly promised to award a Mack Truck dealership franchise to dealer. Dealer claimed that the Mack Truck line would have justified dealer's investment in a new facility, and dealer claims that this promise induced it to enter into the dealer agreement with manufacturer and commit to building updated facility. Manufacturer instead awarded the Mack franchise to another company. Dealer further accused manufacturer of providing more favorable concessions on truck pricing to other franchise dealerships through its Retail Sales Assistance ("RSA") program than it gave to dealer – and dealer contended that this violated the provision of the IDFPA that prohibits a franchisor from "discriminating unfairly among its franchisees."

The district court granted summary judgment **for dealer** on manufacturer's declaratory judgment claim, holding that the integration clause in the dealer agreement barred manufacturer's new-facility claim. In a case of what's "good for the goose is good for the gander," the district court granted summary judgment **for manufacturer** on dealer's Mack claim because it, too, was barred by the contract's integration clause. Nevertheless, the district court allowed the dealer's claim for unfair discrimination under the IDFPA to proceed to trial, where the jury concluded that manufacturer had discriminated unfairly against dealer in violation of Indiana law.

On appeal to the Seventh Circuit, the Court of Appeals agreed with manufacturer that the evidence submitted by dealer at trial (dealer compared 13 concessions manufacturer awarded to other franchisee-dealers with the concession it received from manufacturer) did not support an inference of unfair discrimination. The Seventh Circuit concluded that although dealer could show that it received an inexplicably inferior concession on similar transactions, dealer failed to show why the lack of an explanation must be equated with unfairness. In its view, the Seventh Circuit concluded that discrimination under the IDFPA must be in relation to the franchise agreement, and the agreement in question allowed for the manufacturer's discretion by its terms. The 13 transactions on which dealer relied showed no more than the fact that sometimes dealer received the better concession and sometimes a competitor did.

The Seventh Circuit also considered manufacturer's claim that dealer breached the dealership agreement by failing to build a new facility in accordance with a promise allegedly made by dealer and that this misrepresentation entitled manufacturer to terminate the dealer. In reviewing the district court enforcement of the integration clause, the Seventh Circuit noted that the mere existence of such a clause does not control whether a writing was intended to be completely integrated. Thus, the weight to

be accorded an integration clause varies on the facts and circumstances of each case. One of the factors that can affect the significance of an integration is the sophistication of the parties. Thus, where the parties occupy unequal bargaining position, the integration clause may not accurately express their meeting of the minds, but where two sophisticated parties have engaged in extensive preliminary negotiations, the integration clause may be afforded more weight as a reflection of the final terms of their agreement.

The Seventh Circuit determined that both manufacturer and dealer were sophisticated parties—both had experience with franchise and dealer agreements. If the move to a new facility had been material to the decision to enter into the agreement, then that term should have placed in the agreement. And, even if the integration clause did not bar the claims, the Seventh Circuit reasoned that the plans to build a new facility could have been foiled by any number of things. Because manufacturer did not argue that dealer **never intended** to construct a new facility, it would be a stretch to consider the inclusion of the plan to be a misrepresentation of a material fact rather than the expression of a hope for the future relationship. Therefore, the Court of Appeals agreed with the district court's grant of summary judgment in dealer's favor on this claim.

Finally, the Seventh Circuit addressed dealer's challenge to the district court's rejection of its claim under the IFDA that the manufacturer intentionally misrepresented that it would provide dealer with a Mack Truck franchise in exchange for operating manufacturer's dealership. The district court found that dealer could not have reasonably relied on any such representation in light of the existence of the integration clause in the franchise agreement and the Court of Appeals agreed. Had dealer been an unsophisticated party, or if there had been a greater imbalance in bargaining power, the integration clause might not have been used to bar evidence of an extrinsic promise and render reliance on it unreasonable – but that was not the case here.

4. *Cooper v. Primary Care Sols., Inc.* 2017 WL 1086186 (M.D. La. Mar. 21, 2017)

Plaintiffs brought action against defendants alleging violations of the Federal Trade Commission Act ("FTCA"), the Fair Labor Standards Act ("FLSA"), and Louisiana state law for unfair and deceptive trade practices, violations of Louisiana's securities law, breach of contract, interference with contracts, conversion and unjust enrichment. Plaintiffs alleged that the Individual defendants were alter egos of Defendant Primary Care Sols ("PCS") and that the defendants collectively induced plaintiffs to enter into a franchise investment scheme. Plaintiffs alleged that they were misled by defendants into investing in what plaintiffs believed to be franchises of PCS without providing plaintiffs with adequate disclosures and that PCS ultimately sold the offices established by certain plaintiffs to a third party without paying the plaintiffs a percentage of the profits derived from the sale.

The district court first held that plaintiffs' claims against the individual defendants should be dismissed for lack of personal jurisdiction. The court found that they were not

the alter ego of the corporation, PCS, and there was no evidence that the individual defendants committed an intentional tort or acted outside of their corporate authority such that the Fiduciary Shield Doctrine should not apply. Under Louisiana law, the doctrine holds that an individual's transaction of business within the state solely as a corporate officer does not create personal jurisdiction over that individual though the state has in personam jurisdiction over the corporation.

The district court further held that because plaintiffs had not laid out any specifics regarding the time, place, contents, and speaker of the allegedly false representations and because plaintiffs' allegations are more akin to a breach of contract claim, plaintiffs' Louisiana Unfair Trade Practices Act ("LUPTA") should be dismissed. Plaintiffs' claims under Louisiana securities law were also dismissed because the franchise agreements did not constitute investment contracts and therefore did not fall under Louisiana securities law. The district court also dismissed plaintiffs' FLSA claims due to plaintiffs' failure to allege or establish that PCS was their employer and because the record demonstrated that the plaintiffs operated fairly independently on a day to day basis.

5. *Safe Step Walk in Tub Co. v. CKH Indus., Inc.*
242 F. Supp. 3d 245 (S.D.N.Y. 2017)

Trademark holder brought action against licensee alleging non-payment of fees associated with agreement. Licensee counter-claimed for breach of contract, breach of implied covenant of good faith and fair dealing, promissory estoppel, unjust enrichment, violation of state laws prohibiting unfair or deceptive business practices, and fraud. Trademark holder moved to dismiss the counterclaims.

Plaintiff brought this diversity action in New York and asserted that New York law applied. Defendant argued that Tennessee law governs contract disputes based on the parties' agreements. The agreements between the parties contain mandatory arbitration clauses which provide that arbitration is to be governed by the substantive law of the State of Tennessee. The court held that Tennessee law applies noting that it was apparent to the court that the parties, particularly the plaintiff (a Tennessee corporation) intended for Tennessee law to apply. Additionally, New York choice of law principles require the court to enforce choice of law provisions given that Tennessee bears a close relationship and has a material connection to both the plaintiff and to the parties' agreements.

The district court grouped defendant's counterclaims into three categories: (1) contract related claims; (2) fraud claims; and (3) statutory franchise and unfair or deceptive practices claims. The court first addressed the franchise-based claims.

It found the trademark holder to be a manufacturer of walk-in bathtubs that purportedly held trademarks for the marketing of such tubs. Licensee was permitted to use those trademarks when marketing, selling, and installing holder's tubs in particular geographic areas. A number of "regional" agreements were entered into between the parties based on sale regions with addendums specifying the components of the

business relationship. The trademark holder asserted that a licensor-licensee or supplier-dealer relationship exists whereas licensee argued that the regional agreements constituted franchise agreements under both federal law and corollary state law provisions.

Under the Federal Trade Commission Act ("FTCA"), a franchise is defined as "any continuing commercial relationship or arrangement, whatever it may be called, in which the terms of the offer or contract specify: (1) the franchisee will obtain the right to operate a business that is identified or associated with the franchisor's trademark, or to offer, sell, or distribute goods, services, or commodities that are identified or associated with the franchisor's trademark; (2) the franchisor will exert or has authority to exert a significant degree of control over the franchisee's method of operation, or provide significant assistance in the franchisee's method of operation; and (3) as a condition of obtaining or commencing operation of the franchise, the franchisee makes a required payment or commits to make a required payment to the franchisor or its affiliate."

In the eyes of the district court, it had long been recognized that what the parties call their relationship is irrelevant to the question of whether it constitutes a franchise. Instead, the court looked to the New York-New Jersey regional agreement as an example of how the parties dealt with each other. It specifically noted that the agreement: (1) allowed defendant to use plaintiff's trademarks, marks, slogans, and names within the contracted territory; (2) enabled plaintiff to set minimum sales requirements, to assist defendant in a marketing plan, to direct defendant to make changes to its business model, to terminate the agreement for failure to "complete training" on plaintiff's products or for failure to provide potentially monthly sales reports, income statements, and balance sheets, and prohibits defendant from marketing or selling any products that are competitive with plaintiff's tubs; and (3) required defendant to pay at a minimum a $5,000 fee to enter into the agreement. Accordingly, the district court held that at least the first prong of the FTC rule had been met.

The district court then held that the second prong had also been met because the alleged involvement by plaintiff in defendant's business operations amounted to the "authority to exert a significant degree of control" or "provide significant assistance in [defendant's] method of operation." The district court also held that the third prong had been met based on defendant's alleged payment of a non-nominal fee as a condition of obtaining or commencing operations related to plaintiff. In the view of the district court, the parties' relationship may plausibly constitute a franchisor-franchisee relationship under the FTC rule.

Because there is no private cause of action under the rule, defendant turned to state franchise law and "little FTC" statutes to assert its claims. Defendant asserted that the regional agreements constituted franchises under the Connecticut Franchise Act, the New Jersey Franchise Practices Act, the New York Franchise Act, and the Rhode Island Franchise Investment Act. The district court determined, that, unless it is clear that the public policy **of Tennessee** is to honor the foreign state's statutory schemes, these claims would be non-cognizable. Because Tennessee also has a statutory

scheme designed to protect franchises similar to the statutes in Connecticut, New Jersey, New York, and Rhode Island, the court ultimately held that Tennessee would honor the protections available under the franchise acts of states where defendant had franchises.

Because defendant plausibly alleged a substantial association with plaintiff's marks, a marketing plan prescribed in substantial part by the putative franchisor, a community of interest between the parties in marketing the products, and the existence of operations in each state, the district court held that defendant qualified as a franchisee under each applicable state's law. Notwithstanding this fact, the district court dismissed defendant's "Little FTC" claims under the New York and Rhode Island statutes because both statutes protect consumers from deceptive conduct, and the conduct defendant complained of – violation of FTCA and state franchise law disclosure obligations – arose out of the parties' contractual relationship and were not directed at consumers.

The district court then turned to defendant's contract-related claims. Under Tennessee law, to allege a breach of contract claim one must prove: (1) the existence of an enforceable contract; (2) nonperformance amounting to breach of the contract; and (3) damages caused by the breach of contract. Finding that the defendant had sufficiently alleged damages resulting from the breach, the court turned to the first two elements of the test. In so doing, the district court held that the existence of the regional agreements (some oral, some written, and some orally modified) along with part performance plausibly supported defendant's claim that the agreements existed and are enforceable, thus satisfying the first element of the test. The district court then broke the alleged breaches into three categories: (1) breaches that occurred during the "original terms" of the agreements; (2) breaches that occurred after the Marketing Addendum was effective; and (3) post-modification and extension breaches. The court held that the first category of breaches was actionable based on the inferences drawn from defendant's allegations. This category of alleged breaches arguably occurred during the "original terms" of the agreements (prior to any potential expiration and before they were modified by the Marketing Addendum), and each of the actions or inactions that defendant alleges as breaches would violate the provisions of the original regional agreements. The court held that the second category of breaches largely fail as a matter of law. This is due to the fact the Marketing Addendum introduced a monthly billing scheme for unique leads generated by plaintiff's national and regional marketing campaigns such that the actions or inactions alleged by defendant do not constitute breaches of the agreements as modified by the Marketing Addendum. The court held that the third category of breaches was actionable to the extent they were not in conflict with the Marketing Addendum.

Reasoning that the disputes between the parties arose out of plaintiff's alleged breach of its obligations under the parties' agreements and did not involve plaintiff confusing the public as to whether the services offered were its own or the defendants, the district court held that defendant failed to state a cognizable claim for unfair competition. The district court went on to hold that defendant's fraud claim based on the allegation that plaintiff failed to disclose pertinent information about the franchise

despite plaintiff's contractual obligation to do so could proceed because the counterclaim put plaintiff on notice as to the actions and timeframes implicated.

6. *JDS Grp. Ltd. v. Metal Supermarkets Franchising Am., Inc.* No. 17-CV-6293 (MAT), 2017 WL 2643667 (W.D.N.Y. June 20, 2017)

Franchisee brought this action against franchisor alleging that franchisor violated the Washington State Franchise Investment Protection Act ("FIPA") and breached the implied covenant of good faith and fair dealing by forcing franchisee to install new operating software. Franchisee filed a motion for temporary restraining order and preliminary injunction seeking to prevent franchisor from installing new software on its store computers.

Franchisee operated two retail locations for approximately 10 years and was using a computer software platform known as "Metal Magic," provided to it by the franchisor. The franchisor determined that Metal Magic was outdated and inefficient. As a result, franchisor undertook the development of new software, known as MetalTech, which took three years and cost more than $1,000,000. Franchisee alleges that MetalTech is unreliable and does not perform as required. In response, franchisor produced evidence that 78 out of 86 stores were currently using MetalTech and had seen a 7.4% increase in sales, on average, in the months following the conversion and had not faced any business concerns. The district court noted that it was clear that franchisee was on notice of the claimed issues with MetalTech at least as of August 2016, yet in January 2017 franchisee executed new franchise agreements which expressly provided that franchisor had the right to develop or designate computer software programs and accounting system software and require that franchisees use them.

The district court analyzed two preliminary injunction factors: (1) whether the franchisee was subject to irreparable harm; and (2) whether the party seeking preliminary injunctive relief either will likely succeed on the merits or that there are sufficiently serious questions going to the merits of the case to make them fair ground for litigation and that a balancing of the hardships tips decidedly in favor of the moving party. Franchisee alleged that franchisor's actions violated FIPA, specifically the provision requiring parties to deal with each other in good faith and the provision related to unfair or deceptive trade practices or unfair methods of competition.

With respect to good faith, the district court concluded that Washington courts have generally held that lack of good faith is the equivalent of bad faith, and bad faith embraces more than bad judgment or negligence and imports dishonest purpose and moral obliquity. The court held that the franchisee had identified no evidence that franchisor's development or implementation of MetalTech were undertaken in bad faith or that franchisor had any improper purpose or motivation. The evidence actually demonstrated that franchisor dedicated significant time and resources to MetalTech, and for this reason the district court held that franchisee had **not** demonstrated a likelihood to succeed on the merits of this claim.

As to franchisee's claims related to the FIPA provision addressing whether a requirement to purchase or lease goods or services constitutes an unfair or deceptive act or practice or an unfair method of competition, the district court found that plaintiff had not identified any authority in support of the proposition that a franchisor requiring the use of specific computer software violates the antitrust laws. It found dispositive that numerous federal courts have repeatedly held that it is permissible for a franchisor to require that its franchisees use proprietary computer systems designed by the franchisor for use in the system. Just as it did on the implied covenant claim, the district court determined that the franchisee had not demonstrated a likelihood to succeed on the merits and denied the injunction.

7. *Winebow, Inc. v. Capitol-Husting Co.*
867 F.3d 862 (7th Cir. 2017)

Upstream wine supplier filed a declaratory judgment action seeking a determination that it could terminate a contract granting distributors the exclusive right to sell and distribute supplier's wine in certain areas of Wisconsin. Supplier became dissatisfied with two distributors and abruptly terminated both distributorships. There were no express agreements standing in the way of the termination, but the distributors allege that the Wisconsin Fair Dealership Law ("WFDL") barred supplier from terminating the distributorships without statutory compliance.

Addressing these claims required the Seventh Circuit to undertake an in-depth analysis of the WFDL's legislative history. It provides that grantors may unilaterally stop doing business with their existing distributors only if they have good cause to do so. The WFDL seeks to prevent suppliers from behaving opportunistically once franchisees have sunk substantial resources into tailoring their business around, and promoting, a brand. However, as has been the case since the inception of the WFDL, it **does not regulate all** grantor-distributor relationships.

The statute initially addressed only business relationships (referred to as "dealerships" in the statute) in which there was a "community of interest" between the grantor and the distributor. Both the Wisconsin Supreme Court and Seventh Circuit have added "judicial gloss" to what constitutes a dealership under the statute and typical defense assertions center around the inapplicability of the statute.

In 1999, the Wisconsin Legislature sought to broaden the WFDL to ensure that all "intoxicating liquor" dealerships were protected (including wine dealers). To that end, it sought to eliminate the requirement for "intoxicating liquor" dealerships to prove "community of interest" under the statute and instead opted for a blanket protection. As such, the legislature amended the definition of a "dealership" to include large-volume distributors of "intoxicating liquor." In a classic example of the interplay between politics, lobbyists, and legitimate public policy questions, the revised definition of "dealership" under the WFDL expressly incorporated the definition of "intoxicating liquor" from the chapter regulating alcohol sales in Wisconsin, which included wine.

The new section expressly incorporated the definition of "intoxicating liquor" from the pre-existing statute. However, the Governor (Tommy Thompson) objected to the idea of treating wine dealerships the same as other alcohol dealerships and he partially vetoed and struck a significant portion of the legislature's changes to the WFDL. Specifically. Governor Thompson used his veto pen to eliminate the reference to the existing definition of "intoxicating liquor" in the newly created section of the WFLD by handwriting the phrase "minus wine." The Governor's changes to the bill became law, yet confusion ensued.

In the case, the sole question presented to the Seventh Circuit was whether an "intoxicating liquor" dealership, as defined by the WFDL, includes a dealership that sells and distributes wine. If not, then wine dealership would have to establish a "community of interest" like all other non-alcoholic dealerships in Wisconsin; if so, then they would immediately qualify as dealers and be in a position to obtain the protections of the WFDL.

The Seventh Circuit punted on whether wine dealership was per se protected by the WFDL. Based on the incorporated definition of "intoxicating liquors," wine would seem to be protected. But the former Governor's pesky veto said it was excluded. Despite looking at the legislative history, scope, context, and subject matter of the law, the Seventh Circuit was unable (or unwilling) to reach a conclusion. It certified the question to the Wisconsin Supreme Court to answer the following question: Does the definition of a dealership contained in Wis. Stat. § 135.02(3)(b) include wine grantor-dealer relationships? Oral argument occurred on February 19, 2018. Stay tuned.

International Franchise Association
51st Annual Legal Symposium
May 6-8, 2018
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2018 Judicial Update

Other Cases of Importance

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I. NON-COMPETE AND TRADEMARK INFRINGEMENT

A. *Cajun Global LLC v. Swati Enterprises, Inc.,* 283 F. Supp. 3d 1325, (N.D. Ga. 2017), Bus. Franchise Guide (CCH) ¶16, 118.

The franchisor of Church's Chicken sought a preliminary injunction against the signatory of a franchise agreement and the subsequent buyer and operator of the franchise restaurant for breaching the non-compete covenant and for trademark infringement. Two months after Swati Enterprises signed a ten-year franchise agreement with Cajun Global, it sold the franchise restaurant to Rahman. Rahman operated the franchise restaurant through the term of the franchise agreement. Rahman claimed that he was unaware of the existence of the franchise agreement, but he worked in concert with Swati Enterprises to remit royalties and marketing fees to Cajun Global. He also used the Church's Chicken trademarks and received operational training and support from Cajun Global.

After the franchise agreement expired, Rahman rebranded the franchised restaurant as "Orange Fried Chicken" and used logo, marks, and other decor that were similar to Church's Chicken. Swati Enterprises, the signatory of the franchise agreement, did not oppose Cajun Global's request for injunctive relief. Rahman opposed injunctive relief and asserted that he did not sign the franchise agreement and was not bound by its terms.

The court granted a preliminary injunction and concluded that Rahman was bound by the obligations in the franchise agreement. The most persuasive facts were Swati Enterprises' failure to disclose the sale and Rahman's performance under the franchise agreement for nearly ten years. As a result, Rahman was bound by the obligation not to compete for two years in the sale of chicken within a 25-mile radius of the franchised restaurant or any other Church's Chicken location. The court also found that the logo and marks used by Orange Fried Chicken were confusingly similar.

B. *H&R Block Tax Servs. LLC v. Frias*, No. 4:18-00053-CV-RK, 2018 WL 576858, (W.D. Mo. Jan. 26, 2018), vacated in part, 2018 WL 934901 (W.D. Mo. Feb. 16, 2018, Bus, Franchise Guide (CCH) ¶16,127.

In this case a former franchisee opened a compete tax preparation business after the expiration of his franchise license/agreement with H&R Block. The post-termination obligations in the agreement included a two-year noncompetition and nonsolicitation covenant. The restricted geographic area for the noncompetition covenant was limited to a 25-mile radius from the former franchisee's service territory.

H&R Block moved for a temporary restraining order and a preliminary injunction to enforce the noncompetition and nonsolicitation covenants. Looking at the terms of the covenants, the court found that the covenants were enforceable under Missouri law. The covenants sought to protect legitimate interests, including H&R Block's established brand, goodwill and confidential business information, as well as its interest in preventing the former franchisee from unfairly competing by using his knowledge about

H&R Block. The court also found the two-year period and 25-mile radius appropriately narrow. Lastly, the court noted that Missouri courts are more liberal in enforcing covenants that are part of a business transaction, compared to being ancillary to an employment contract.

After concluding the covenants were enforceable, the court granted the temporary restraining order and subsequently granted the preliminary injunction. In both orders, the court found a substantial likelihood of success on the merits because the former franchisee was operating a new tax preparation business within the 25-mile radius and within the two-year restricted period.

Update: In the court's subsequent order granting a preliminary injunction, it partially vacated the Temporary Restraining Order. The court vacated the portion of the TRO where it found that the former franchisee was in further breach of the covenants because his spouse also operated a tax preparation business within the restricted 25-mile radius. The court vacated the part of its order enjoining the spouse's business because she was not a party to the franchise license agreement.

C. ***Red Roof Franchising, LLC v. Riverside Macon Grp.,*** **LLC, No. 2:18-CV-16, 2018 WL 558954, (S.D. Ohio Jan. 25, 2018), Bus. Franchise Guide (CCH) ¶16,126.**

The former franchisee of a Red Roof Inn failed to cease using the franchise mark and operating as a Red Roof Inn after the termination of its franchise agreement. Red Roof terminated the franchise agreement after the former franchisee failed to make franchise payments and failed to improve the property as required. Upon termination, the former franchisee was required to cease operating as a Red Roof Inn and to not directly or indirectly hold itself out to the public as a Red Roof Inn.

The court granted Red Roofs motion for a preliminary injunction. The court found there was a likelihood of success on the merits because there was a high probability of customer confusion and concrete evidence of actual customer confusion. The marks displayed on the former franchisee's building were not merely similar to Red Roof, they were identical. Red Roof also presented evidence of a disgruntled customer who contacted Red Roof to complain of subpar service and poor conditions at the former franchisee's hotel. The customer was confused because the hotel was labeled as a Red Roof Inn and she was billed on Red Roof stationary.

As for irreparable harm, the court noted that for the purposes of the Lanham Act, irreparable harm is presumed once there is a finding of a likelihood of confusion. The court observed that Red Roof would continue to suffer financial harm from not having exclusive use of the Red Roof Inn mark. The court also found that there was a strong public interest in avoiding confusion in the marketplace.

D. *Osborne v. Brown & Saenger, Inc.,* 2017 ND 288, 904 N.W.2d 34 (2017), Bus. Franchise Guide (CCH) ¶16, 102.

In this non-franchise agreement case, the North Dakota Supreme Court considered whether a choice-of-law provision in an employment contract was enforceable. Most non-compete agreements are unenforceable and against public policy in North Dakota. The choice of law provision required the application of the laws of South Dakota, which are more favorable to non-compete agreements in terms of non-enforceability.

The enforceability of the non-compete agreement hinged on the governing law. Section 9-08-06 of the North Dakota Century Code provides that all contracts restraining the exercise of lawful business are void with the exception of (1) contracts for the sale of the goodwill of a business that will continue operating, and (2) the dissolution of a partnership. Pursuant to this code section, courts in North Dakota have consistently held covenants not to compete to be unenforceable. In contrast, a court in South Dakota had recently enforced an identical non-compete agreement between the defendant employer and another employee.

The court held that parties may not contract for the application of the laws or forum of another state for the purpose of circumventing North Dakota's longstanding and strong public policy against non-compete agreements. In reaching its decision, the court looked to cases in Georgia and Wisconsin that declined to enforce choice of law and forum selection provisions on similar grounds.

E. *D.P. Dough Franchising, LLC v. Southworth,* No. 2:15-CV-2635, 2017 WL 4315013, at *13 (S.D. Ohio Sept. 26, 2017), appeal dismissed, No. 17-4120, 2017 WL 7048511 (6th Cir. Dec. 8, 2017), Bus. Franchise Guide (CCH) ¶16,049.

This case involves a calzone restaurant franchise that offers late night calzones on college campuses. The franchisor moved for a preliminary injunction alleging breach of the franchise agreement's non-diversion and non-competition clauses and trademark infringement, among other claims.

After managing a franchise restaurant in Courtland, New York, the former franchisee purchased the franchise restaurant and subsequently signed a franchise agreement. While under the franchise agreement, the former franchisee inquired about opening a second franchise in Columbia, South Carolina because the franchisor had not yet expanded there. He ultimately decided to open a restaurant of his own to avoid paying the $25,000 franchise fee and royalties. Prior to opening his own restaurant, he transferred the franchised restaurant in Courtland to his mother, terminating the franchise relationship.

The new Columbia restaurant shared some resemblances to the franchise system. It was located in a college town, it served late-night calzones, provided delivery

services, and its original menu was substantially similar. After the franchisor filed suit alleging trademark infringement, the former franchisee redesigned his menu.

Following his first restaurant in Columbia, the former franchisee sought to open a second location in Athens, Georgia. During this same period, the franchisor had another prospective franchisee, Bulldawg Dough, LLC, who also wanted to open a location in Athens. The two competing restaurants enlisted the same real estate agent and applied to lease the same location. After the former franchisee won the lease and he opened his restaurant in Athens. The other interested party was forced to open in a less desirable location.

Despite the franchisor's claims that the former franchisee knew of its intent to expand in the Athens market, the court found that the non-diversion and non-compete clauses were not applicable. The court noted that the clauses did not explicitly restrict competition in areas of anticipated development or expansion. Thus, the former franchisee was only restricted in areas where a current franchise existed before the ex-franchisee opened his restaurant. As a result, the court held he was not in breach of the franchise agreement.

The court further held that the ex-franchisee was not in violation of the Lantham Act for trademark infringement because it was not likely that customers would confuse the marks. The court summarily dismissed the franchisor's contention that its general business model was part of its trademark. Operating a late-night calzone delivery restaurant near college campuses was too broad to constitute a trademark and the franchisor provided no evidence that the model was registered as a trademark. Finally, the former franchisee had removed all potentially infringing content from his menus and website, eliminating any potential confusion.

F. ***Homewatch Int'l, Inc. v. Navin*, No. 16-CV-02143-KLM, 2017 WL 4163358, (D. Colo. Sept. 20, 2017), Bus. Franchise Guide (CCH) ¶16,051.**

This case was before the court on a motion to dismiss the franchisor's complaint against the owner of a former franchise, for, *inter alia,* breach of the post—termination covenant not to compete. Following the termination of the franchise agreement on June 30, 2017, the owner started a competing business on July 1, 2016. The owner claimed that the franchise agreement was not binding in her individual capacity. She also claimed that the non-compete covenant was void under Colorado law.

The court denied the owner's motion to dismiss. It found that sufficient facts were alleged to bind the owner to the franchise agreement in her individual capacity. Most significant was the fact that the owner signed a guaranty where she agreed to be bound personally for each and every provision in the franchise agreement, including the covenant not to compete.

Next, the court considered the enforceability of the non-compete covenant. It noted that Colorado has a strong public policy against non-compete clauses and that Colorado Statute §8-2-113(2) renders covenants not to compete void except under a

few narrow exceptions. These exceptions include contracts for the purchase and sale of a business or assets of a business. The court concluded that franchise agreements are under the “sale of a business” exception. By entering franchise agreement, the franchisee is allowed to use the established goodwill and brand franchise agreement, the franchisee is allowed to use the established goodwill and brand -) recognition of the franchisor. Accordingly, the court held that the non-compete covenant was not

G. *Dickey’s Barbecue Pit, Inc. v. Celebrated Affairs Catering, Inc.,* No. 4:17-CV-00127, 2017 WL 1079431, (E.D. Tex. Mar. 22, 2017), Bus. Franchise Guide (CCH) ¶15,975.

The franchisor of a barbeque restaurant moved for a preliminary injunction to enjoin a former franchisee from using its registered trademarks. The former franchisee owned two franchise restaurants in Tuscan, Arizona. On February 2, 2017, the franchise agreements for the two restaurants terminated. The franchise agreement had provided that upon termination, the former franchisee would be prohibited from reopening the franchise restaurants, opening a barbeque restaurant within a 5-mile radius of any franchise restaurant, and using any confidential information or trade secrets.

Shortly after the agreements terminated, a representative of the franchisor visited the two restaurants and documented the continued use of the franchisor’s trademarks. The former franchisee continued to operate the restaurants until the court granted the preliminary injunction.

The court found that the franchisor was likely to succeed on the trademark infringement claim. Following the termination of the franchise agreement, all use of the trademarks was unauthorized. Moreover, consumer confusion was likely because the former franchisee used marks that were identical to the registered trademarks of the franchisor.

H. *Better Homes Realty, Inc. v. Watmore*, No. 3:16-CV-01607-BEN-MDD, 2017 WL 1400065, (S.D. Cal. Apr. 18, 2017), Bus. Franchise Guide (CCH) ¶15,957.

Better Homes Realty is a real estate brokerage franchising business that has franchise locations throughout California and the United States. Better Homes has registered the marks “Better Homes” and “Better Homes Realty.” The defendant is a real estate and investment firm named San Diego Better Homes Realty. Better Homes brought a lawsuit against defendant for trademark infringement.

Before the court was the former franchisee’s motion to dismiss. The court denied the motion to dismiss and found that there was a likelihood of trademark confusion based on three considerations. First, Better Homes alleged sufficient strength of the mark because it has been registered since 1985. Second, defendant and Better Homes both offered services in residential real estate. Third, the marks “Better Homes Realty” and “San Diego Better Homes” were sufficiently similar such that they would likely cause consumer confusion.

Other cases of interest: *E.T. Products, LLC v. D.E. Miller Holdings, Inc.,* 7th Cir., ¶ 16,044 (noncompete agreement after the sale of a business); *Stone Surgical, LLC v. Stryker Corp.,* 6th Cir., ¶ 15,980 (noncompete agreement ancillary to employment contract); *Frye v. Wild Bird Centers of America, Inc.*, 4th Cir., ¶ 16,080 (arbitrator's decision that franchisee violated noncompetition agreement would not be set aside).

II. FRAUD ISSUES

A. *QFA Royalties, LLC v. ZT Investments, LLC*, 2017 WL 5517408 (D. Colo. Nov. 17, 2017), Bus. Franchise Guide (CCH) ¶16,087.

Quiznos franchisor brought claims against franchisees, accusing them of continuing to operate a restaurant that was an unauthorized Quiznos franchise. When one Defendant did not appear, the Clerk entered default against it. Plaintiffs moved for default judgment and the court granted the motion in part and denied it in part.

The court awarded Plaintiffs both past-due amounts and also future lost profits based on Defendants' violation of 15 U.S.C. § 1114(1) (trademark infringement), 15 U.S.C. § 1125(a)(1) and breach of contract. In addition, Plaintiffs requested injunctive relief. First, Plaintiffs asked for a permanent injunction enjoining (1) using any of the Quiznos Marks and trade dress or any trade mark that is confusingly similar to the Quiznos marks; (2) infringing the Quiznos marks or trade dress using any similar designation or any other similar design or decor alone or in combination with other components; or (3) passing off any products or services as those of authorized Quiznos' franchisees or as genuine Quiznos' products or services. The court held that because it already awarded this relief as part of its preliminary injunction, it was appropriate to include the same provisions as part of a permanent injunction.

Plaintiffs also asked for an injunction against Defendant (1) causing a likelihood of confusion or misunderstanding as to the source or sponsorship of their business, products, or services; (2) causing a likelihood of confusion or misunderstanding as to their affiliation, connection, or association with Quiznos or with any of its product/services; and (3) unfairly competing with Quiznos in any manner. However, the court found that this was an impermissible "obey the law" injunction and did not include the language in a permanent injunction.

Plaintiff further requested a specific performance injunction that Defendant cease to operate a competitive business within 5 miles of Defendants' franchise restaurant or within 5 miles of any other Quiznos restaurant for a period of 2 years based on a section in the Franchise Agreement. The court held that Plaintiffs did not attempt to demonstrate that this covenant not to compete was reasonable under the circumstances and also did not show irreparable harm in light of the damages to which it is entitled. The court did not grant this injunctive relief.

However, the court granted the Plaintiffs' specific performance injunction as to returning all proprietary and confidential information and material and ceasing to use or

disclose Plaintiffs' proprietary and confidential information. Plaintiffs further requested a specific performance injunction to notify the telephone company and all telephone directory publishers of the termination of Defendant's right to use any telephone number and telephone directory listing associated with Quiznos. The court held that in light of Quiznos' allegation that Defendant's employees have continued to represent the new restaurant a Quiznos, it would order Defendant not to hold itself out in any manner as a Quiznos (including via telephone) and to inform all telephone directories that the restaurant is not a Quiznos.

B. *Broward Motorsports of Palm Beach, LLC v. Polaris Sales, Inc.,* 2018 WL 1072211 (S.D. Fla. Feb. 27, 2018), Bus. Franchise Guide (CCH) ¶16,142.

Broward Motorsports, a motor vehicles dealer, and Polaris, a manufacturer of motor vehicles, entered into an Agreement ("Agreement") authorizing Plaintiff to act as a dealer of Victory Motorcycles ("Victory") from July 2016 to June 2017. Plaintiff alleges that Defendant knew that it would be terminating the Victory line shortly thereafter. A couple months later, Defendant sent Plaintiff a letter indicating that it would be terminating the Victory line and would not renew the Agreement for that particular line in July 2018. Broward filed suit against Polaris alleging fraudulent concealment, fraudulent inducement, violation of Florida's Deceptive and Unfair Trade Practices Act ("FDUTPA"), and breach of the implied covenant of good faith and fair dealing. Polaris filed a Motion to Dismiss Plaintiff's First Amended Complaint and the district court granted the motion.

With respect to the fraudulent concealment claim, the court found there was no detrimental reliance or duty to disclose, and therefore, the plaintiff was unable to state a claim for fraudulent concealment as a matter of law. Although Plaintiff alleged that it relied on the protection of Florida Statute § 320.641 for the notion that Florida franchise agreements are continuing in nature, § 320.641(2) allows a franchise agreement to be discontinued if the licensee notifies the DMV of the failure to renew the agreement at least 90 days before the effective date. Also, the language of the Agreement stated that Defendant could "discontinue or . . . add or delete Products at any time." In addition, the court held that Defendant did not owe a statutory duty to disclose its intention to discontinue its Victory line to Plaintiff because § 320.641 only imposes a duty on Defendant to disclose its intention not to renew a dealer agreement 90 days in advance which Defendant did. Plaintiff also did not have a common law duty to disclose because Florida law is settled in that parties negotiating an arms'-length transaction, such as the one involving a potential franchise, do not form a special relationship that would impose a duty of disclosure.

The court also held that Plaintiff's fraudulent inducement claim failed as a matter of law because there was no false statement made or justifiable reliance. The court held that merely stating "We look forward to a long and profitable relationship" was not actionable because there were no allegations that Defendant did not intend to maintain a long and profitable relationship with Plaintiff and in fact, the dealer relationship remained ongoing as to five other product lines. Also, no justifiable reliance existed

because at the time Plaintiff and Defendant entered into the Agreement, no alleged misrepresentation had been made—Defendant's statement about a "long and profitable relationship" occurred one day after the Agreement was executed.

Plaintiff's claim for violation of FDUTPA failed as a matter of law because § 320.641 on which Plaintiff based its claim that the Agreement should have been continuing in nature, also provided for a non-renewal procedure. In addition, a consumer acting reasonably under the circumstances would not have been misled by failing to disclose the fact that it would be discontinuing the Victory line because 320.641 does not create a perpetual dealer agreement between a manufacturer and dealer.

C. *Lomeli v. Jackson Hewitt, Inc.,* 2018 WL 1010268 (C.D. Cal. Feb. 20, 2018), Bus. Franchise Guide (CCH) ¶16,147.

Plaintiff Lomeli claims Defendant Jackson Hewitt is (1) directly liable for fraudulent statements it made to consumers like Plaintiff regarding the accuracy of its tax preparation services; and (2) vicariously liable for fraud and other derivative claims for its franchisee's actions in preparing fraudulent tax returns. Defendant filed a Motion to Dismiss claiming each of Plaintiff's causes of action is grounded in fraud but Plaintiff does not meet the requirements of Federal Rule of Civil Procedure 9(b) and also Plaintiff fails to allege facts sufficient to state a claim for relief under Rule 8.

The court found that Plaintiff's allegations in its Second Amended Complaint taken as true were sufficient to allege a theory of direct fraud against Defendant. Plaintiff claimed Defendant was directly liable for fraud because (1) Defendant reviewed and approved tax returns; and (2) Defendant wrote a letter to Plaintiff telling him that the return he authorized for filing was sent to the IRS processing center, when, in fact Defendant sent a different return to the IRS. Although Defendant argued that Plaintiff merely lumped all the Defendants together instead of parsing out the allegations as to each Defendant, Plaintiff alleged that Defendant knew of the fraudulent scheme. In addition, Plaintiff explained how the circumstances surrounding the submission of his fraudulently-prepared tax returns would lead a reasonable person to suspect fraud was afoot. Therefore, the circumstances surrounding the submission of his returns are pleaded with particularity, and lead the Court to reasonably infer a fraudulent intent.

Defendant also contended that Plaintiff's claim should fail because he never alleged that he relied on the fraudulent statements and did not allege that Defendant knew the statements were false when made. However, Plaintiff pleaded that the representations were material because they induced Plaintiff and class members to entrust preparation and submission of their tax returns to Defendants and they acted in justifiable reliance on these misrepresentations and omissions by permitting Defendants to prepare and file their tax returns. The court found these allegations were sufficient.

In addition, the court denied Defendant's Motion to Dismiss Plaintiff's vicarious liability claims because he alleged additional control over the processing and

submission of tax returns which directly related to the fraudulent conduct of which Plaintiff complained. Plaintiff alleged that Defendant controlled the instrumentality that caused his harm—the hiring and training of tax preparers. He also alleged that Defendant reviewed, approved, and submitted the tax returns to the IRS through its proprietary, and mandatory, computer systems.

The court did not dismiss Plaintiff's equitable claims because he pleaded in the alternative. The court also found that Plaintiff sufficiently alleged standing for injunctive relief because even though he did not allege that he would patronize Defendant in the future, he requested injunctive relief such as resubmission of tax returns and an explanation to the government of how the returns were filed. In addition, the court did not dismiss Plaintiff's Fraud, California Consumer Legal Remedies Act (CLRA), and California's Unfair Competition Law (UCL) claims as well as Plaintiff's claim for wrongful tax disclosure and negligence. The court also denied Defendant's Motion to Strike Plaintiff's class allegations.

D. ***In re Volkswagen*** **"Clean Diesel" Marketing, Bus. Franchise Guide (CCH) ¶26,998.**

Plaintiff alleged that Defendants conspired with Volkswagen to develop the defeat device that was intentionally installed in Volkswagen diesel-engine vehicles to evade U.S. emissions regulations, thereby violating the Racketeer Influenced and Corrupt Organizations Act (RICO).

The court stated that when a plaintiff brings a RICO claim against multiple defendants, it must plead facts that support that each defendant took some part in directing the RICO enterprise's affairs. Additionally, where the predicate acts of a RICO enterprise were acts of mail and wire fraud, plaintiffs must identify the role of each defendant in the allegedly fraudulent scheme. In this case, Plaintiff did not do so. Its complaint blurred the lines between the conduct of each of the Defendants. Additionally, it lumped all the defendants together into the term "Bosch" which was inappropriate.

Plaintiffs also did not allege that one defendant was the alter ego of another so as to avoid the need to plead specific facts as to each Defendant.

Therefore, the court granted Plaintiffs leave to amend their complaint instead of dismissing the case.

E. ***Fres-co Systems USA, Inc. v. Hawkins,*** **690 Fed. Appx. 72 (3d Cir. 2017), Bus. Franchise Guide (CCH) ¶15,985.**

Defendant's former employer sue employee and his new employer for misappropriation of trade secrets and sought to enforce non-competition agreement employee signed when he began his employment with Plaintiff. The district court granted Plaintiff a preliminary injunction barring employee from disclosing Plaintiff's confidential information and from soliciting twelve clients whom he had serviced while in

employment for Plaintiff. Defendants appealed. The Court of Appeals remanded for the trial court to reconsider the preliminary injunction factors.

The court quoted the four factor preliminary injunction test stating that a preliminary injunction may issue if (1) the plaintiff shows that it is likely to succeed on the merits; (2) the plaintiff establishes that it is likely to suffer irreparable harm absent issuance of the injunction; (3) the balance of equities does not disfavor granting an injunction; and (4) public interest concerns do not outweigh the interests advanced by issuance of the injunction.

The court correctly considered and found a likelihood of irreparable harm because of the substantial overlap between the employee's work for his new employer and Plaintiff in that he had the same role, same industry, and same geographic region.

However, the appellate court found that the trial court did not analyze the arguments regarding likelihood of success on the merits. The court quoted the U.S. Supreme Court in stating that "likelihood" of success means that it is not enough that the chance of success of the merits be better than negligible and more than a mere possibility of relief is required. The court held that the trial court should analyze the elements of the movant's claims to determine whether the movant could likely meet each element. In this case, the district court neither mentioned Plaintiff's causes of action nor analyzed the elements of any or all of them to determine whether it was likely to succeed on the merits. In addition, the court did not address Defendants' arguments that Plaintiff could not prevail on the merits of its breach of contract claim because an earlier opinion concluded a nearly identical non-competition agreement by Plaintiff was so oppressively overboard as to render it unenforceable. The court did not analyze these arguments to determine whether Defendants' issue preclusion argument was sufficiently persuasive to prevent Plaintiff from meeting its burden to show a likelihood of success on the merits.

The appellate court also held that the district court did not consider the final two preliminary injunction factors. First, the district court did not address the competing interests of balance of harms and the public interest nor did it explain how it weighed the potential harm to Plaintiff against the potential harm to Defendants.

The district court failed to state the reasons why it issued the injunction with respect to three of the four preliminary injunction factors. In addition, the limited cord consisted of only two affidavits that provided conflicting information regarding the nature of the information to which Defendant had access while in the employment of Plaintiff. The appellate court left it to the district court's consideration whether there needed to be an evidentiary hearing in this matter prior to ruling on the preliminary injunction. The appellate court remanded for further analysis of the preliminary injunction factors consistent with the opinion.

III. RENEWAL

A. *Howell v. Advantage Payroll Servs., Inc.,* No. 2:16-CV-438-NT, 2017 WL 6327832, (D. Me. Dec. 11, 2017), Bus. Franchise Guide (CCH) ¶16,100.

Franchisee plaintiffs filed a declaratory judgment action as to their contractual rights to renew their franchise agreements. Between 1986 and 1997, the franchisee plaintiffs entered into ten-year franchise agreements with the franchisor. The franchise agreements contained an option to renew the agreements for one additional ten-year term. Each of the plaintiffs exercised its renewal rights upon the expiration of the first ten-year term. The plaintiffs executed renewal addenda that excluded any promises or representations outside of the addenda and stated that the addenda were controlling with respect to any inconsistent terms in the franchise agreements.

When the expiration of the second ten-year terms neared, the plaintiffs attempted to renew their franchise agreements for an additional ten-year term. The franchisor denied their requests and stated that they do not have a contractual right to renew.

The franchisor moved for summary judgment on the plaintiffs' claims. The issue before the court was the interpretation of the renewal provision in the franchise agreements and the terms of the renewal addenda. The court concluded that the agreements were unambiguous and did not grant an additional option to renew. The franchise agreements created one option to renew for one ten-year term. The renewal addenda did not include any language expressly creating an additional renewal. Without express terms in the agreements addressing the issue of renewal, the court declined to insert additional terms.'

B. *Dalwadi v. Holiday Hosp. Franchising, Inc.,* No. CV H-16-2588, 2017 WL 4479962, (S.D. Tex. July 5, 2017), Bus. Franchise Guide (CCH) ¶16,017.

This case involved a franchisor's refusal to renew a franchise agreement for the operation of a Holiday Inn in Houston, Texas. When the former franchisee entered into a ten-year license agreement, the franchisor assured its operator that almost all franchise agreements automatically get renewed. The former franchisee spent millions of dollars developing and building the hotel with the intention of renewing the agreement for another ten years.

Before the license expired in April 2016, the former franchisee informed the franchisor that it intended to stay in the system and paid the $15,000 relicensing fee and the $2,500 fee for the improvement plan. It further requested the right of first refusal to build a new hotel in its service market. The franchisor denied the renewal request and advised that a new hotel will replace the existing hotel.

The former franchisee filed a lawsuit against the franchisor for breach of contract and the implied covenant of good faith and fair dealing, promissory estoppel, and fraud.

Applying Georgia law, the court granted the franchiser's motion for summary judgment on all claims. The court denied the claim for breach of contract and the implied covenant of good faith and fair dealing because the agreement did not contain any terms entitling the former franchisee to renewal or the issuance of a new license. To the contrary, the agreement expressly stated that the license was not renewable. The express nonrenewal term precluded of any inconsistent implied terms.

The court granted summary judgment on the promissory estoppel claim because there was a valid contract that governed. Lastly, the court granted summary judgment on the fraud claim because the complaint did not contain sufficiently detailed allegations.

IV. CONTRACT ISSUES

A. *Lokhandwala et al. v. KFC Corp.,* 2018 WL 509959 (N.D. Ill. Jan. 23, 2018), Bus. Franchise Guide (CCH) ¶16,130.

Plaintiff Lokhandwala, a franchisee, sued Defendant KFC, alleging that Defendant breached their agreement by unreasonably attempting to block him from telling customers that his KFC franchises offered Halal chicken. Defendant sought to dismiss Plaintiff's claims of declaratory and injunctive relief, breach of contract, and promissory estoppel, claiming that the valid franchise agreement entitled him to control how Plaintiff marketed products at his KFC franchise.

The court agreed with Defendant in holding that the franchise agreement gave Defendant "the absolute right" to approve or prohibit any advertising or promotional claims regarding KFC products. Because there was no ambiguity in the agreement, the court construed it strictly according to the ordinary meaning of the terms. First, the contract stated the franchisee would strictly comply with the requirements and instructions of KFC regarding the use of its trademarks. Another section stated Franchisee would take such action and precautions necessary to assure that only advertising and-promotional material "which met KFC's standards and specifications" were used. This section gave Defendant control over Plaintiff s advertising and promotional material.

Another section made it clear that Defendant could enforce the franchise agreement at any time regardless of any past failures to do so. It stated, "No failure, forbearance, neglect or delay of any kind or extent" on the part of KFC in connection with enforcing and exercising rights under the agreement "shall affect or diminish KFC's right to strictly enforce and take full benefit of each provision of this Agreement at any time." Additionally it stated, "No waiver by KFC of any performance of any provision of this agreement shall constitute or be implied as a waiver of KFC's right to enforce such provisions at any future time." Lastly, there was a section stating that the franchise agreement constituted the parties' complete agreement and superseded any other agreements between the parties. Looking at all of these sections together, the court

found that under the agreement, Defendant could bar Plaintiff from advertising his products as Halal, even if Defendant allowed that advertising in the past.

Plaintiff argued that because the contract was silent or ambiguous as to whether he may make "truthful disclosures" about Halal products, the court should consider extrinsic evidence. However, Plaintiff himself stated that he was "marketing" and "advertising" the Halal products, which the franchise agreement unambiguously entitles Defendant to control. In addition, Plaintiff's truthful statements regarding the meat could still be advertising. The court upheld the merger/integration clause and refused to consider extrinsic evidence.

Lastly, Plaintiff claimed that Defendant breached the contract by making "unreasonable" demands that he stop marketing his products as Halal. However, the section pertaining to advertising in the agreement did not contain any language regarding "reasonableness," and the court found that the franchise agreement did not impose any specialized, overarching reasonableness requirement to Defendant's decisions about advertising.

B. *Sumanth v. Essential Brands, Inc.,* 2018 WL 558612 (D. Md. Jan. 25, 2018), Bus. Franchise Guide (CCH) ¶16,129.

Plaintiffs, a married couple, sought to purchase a daycare franchise from Essential Brands. During the negotiations, purchase, and construction of the daycare franchise facility, Plaintiffs stated that they acted upon "false information" provided by Defendants and never received access to Defendants' proprietary information or historic data regarding the franchisees' profitability even though they were promised it. Plaintiffs brought claims of intentional and negligent misrepresentation, fraud in the inducement, and defamation by Defendants. Defendants subsequently moved to dismiss all claims. Defendants argued that they should be awarded attorneys' fees under the contract. Applying Maryland law, the court applied an "objective interpretation" of the contract and looked to "the entire language of the agreement, not merely a portion thereof." The court found that the contract provision itself contained ambiguity regarding whether Plaintiff had an obligation to indemnify Defendants or fees incurred in the lawsuit. The section stated Plaintiffs were required to reimburse Defendant if violated a term or condition contained within the Agreement and the Defendants had to "pursu[e] the enforcement of this Agreement." The provision also covered costs and fees incurred by Defendant relating to "defenses, counterclaims and/or crossclaims" asserted by Plaintiff. However, the agreement did not clearly cover attorneys' fees in the event that Plaintiffs sued Defendants for misrepresentation or fraud.

Because the applicable provision contained ambiguity, the court considered other provisions of the contract and noted that the parties negotiated the payment of attorneys' fees in a variety of situations, including in an indemnification action brought by a third party, but not in a situation where the franchisee first brings a lawsuit alleging claims related to the validity of the Agreement or other tort claims. The court declined to

read such an obligation into the contract. Therefore, the contract did not provide for attorneys' fees in this situation.

The court also did not find any basis for imposing sanctions on the Plaintiffs or their counsel in the case. They did not multiply the proceedings in an unreasonable and vexations way but instead were looking at considering other avenues of relief to save the parties' and the court's resources.

C. *Jos A. Bank Clothiers v. J.A.B.-Columbia*, 2017 WL 6406805 (D. Md. 2017), Bus. Franchise Guide (CCH) ¶16,106.

Franchisor, Jos A. Bank, sued Franchisees that owned three of Jos. A. Bank's franchise stores. Franchisor files a complaint seeking a declaratory judgment asking the court to declare (1) that the franchise agreements in issue provided for only a single franchise renewal and not unlimited or perpetual franchise renewals; (2) that the Franchisees' failure to execute the form of successor franchise agreement offered to them by Franchisor, without further renewals, constituted an election by them not to buy a successor franchise; and (3) that the Franchisees' election not to buy a successor franchise allowed franchisor to terminate the franchises of the Franchisees at any time. The Franchisees in turn pled a counterclaim for declaratory judgment that they were entitled to a renewed franchise agreement on the same terms as their original agreement and also a counterclaim for breach of contract because Franchisor tendered the improper successor franchise agreement to the Franchises. Both parties filed motion for summary judgment and the court denied both motions.

Franchisor argued that the plain language of the contract stating the Franchisees had the right to buy "a successor franchise" limited them to only "a" single renewal. However, the court found that although the Agreement did not explicitly provide for multiple renewals, it also did not clearly limit the Franchisees to a single renewal. Franchisees asserted that they were entitled to unlimited rolling renewals. However, the court held nothing in the plain language of the agreement suggested they were entitled to rolling renewals. In addition, it was irrelevant that Franchisor had consistently granted every other franchise a rolling renewal. The contract contained an integration clause and explicitly stated that the Franchisor "shall not be deemed to have waived any right reserved by this Agreement by virtue of any custom or practice of the parties at variance with it." Therefore, the Agreement did not allow the Franchisees to point to any prior practice of granting rolling renewals as an indication that Franchisor was obligated to offer them in this instance. Moreover, rolling renewals were not a universal practice. Lastly, citing to documents that did not reveal an ambiguity in the Agreement were not relevant.

Most of the argument between the parties surrounded which "form" of franchise agreement should have been in place when the Franchisees sought renewal. The court held that the Agreement did not unambiguously indicate the proper form and therefore none of the phrases in the contract referring to which "form" should be used resolved which terms should apply with respect to the Franchisees' successor franchises. The

language was ambiguous. In addition, because reasonable people could disagree on the meaning of the clause "may contain provisions, including royalty fees, materially different from those contained herein," the court could not conclude as a matter of law that Franchisor had the right to alter materially the terms of a new franchise agreement. As a result, the court could not conclude that the Agreement unambiguously supported Franchisor's actions in offering the Franchisees a successor franchise agreement without a renewal option.

Next, because the language of the contract was ambiguous with respect to the question of which form would be the "then current form," the court looked to extrinsic evidence as to the parties' intent at the time of the Agreement's execution. Because of thin evidence from each party, the ambiguity could not be resolved by reference to extrinsic evidence. Therefore, the court denied both motions for summary judgment.

D. *Charter Practices Intl, LLC*, 2017 WL 4366717 (D. Conn. Sept. 30, 2017), Bus. Franchise Guide (CCH) ¶16,052.

Plaintiff, Franchisor of a pet hospital, sought to terminate the franchise of Defendant, a veterinarian found by a state board o have violated state law by administering partial dosages of rabies vaccine to animals. Plaintiff, Charter Practices Intl, filed a motion for summary judgment on a breach of contract and Connecticut Unfair Trade Practices Act (CUTPA) claims and Defendant's counterclaims under the CUTPA. The court granted Plaintiff's Motion for Summary Judgment.

The court found issue preclusion prevented Defendant from relitigating issues already decided by the Board of Veterinary Medicine of the Connecticut Department of Health (the "Board"). The Board determined that under-vaccinating animals for rabies could endanger e lives of animals and those around then, and rejected Defendant's assertion that his authority vet allowed him to overrule animal vaccination laws and regulations.

In addition, the court held that Defendant's practice of administering half-doses rabies vaccine, as found by the Board, violated the CUTPA. He had engaged in this practice for two years and each time he did so, he violated the CUTPA.

Defendant alleged a counterclaim for breach of contract under the Connecticut Franchise Act (the "CPA") which provides that a franchise cannot be terminated without good cause and 60 days' notice. However this counterclaim failed. First, Defendant's violation of Connecticut law, as found by the Board, was good cause for termination. In addition, he was given 60 days' notice. The termination notice was issued on December 7, 2012 and stated that the franchise was terminated effective February 5, 2013, exactly 60 days after the date of the notice. Even though another entity stepped in and operated the franchise until the termination date, "exercising step-in rights is not equivalent to terminating a franchise." Defendant argued that a document dated December 13 stated Defendant no longer owed the hospital. However, the CPA made it clear that the Franchisee owned the hospital until the date of termination and during the step-in

period, revenue would accrue to the Franchisee's account. Because there was no ambiguity in the CPA and extrinsic evidence such as the December 13 document did not raise a triable issue. Plaintiff's motion for summary judgment on this counterclaim was granted.

Defendant's counterclaims for breach of the covenant of good faith and fair de g and for violation of CUTPA also failed. The Board's findings compelled the conclusion that Plaintiffs were entitled to terminate the CPA and exercise their step-in rights.

Lastly, Defendant's counterclaim for negligent infliction of emotional distress also failed because his only supporting evidence was his own affidavit and the testimony in his affidavit was inadmissible with regard to some of the factual matters essential to his claim.

In conclusion, the court granted Plaintiff's motion for summary judgment on its claims and all four of Defendant's counterclaims.

E. *In re Bambu Franchising, LLC*, 2017 WL 4003428 (Tex. App.—Dallas Sept. 12, 2017), Bus. Franchise Guide (CCH) ¶16,039.

Plaintiff Franchisee and Defendant Franchisor's franchise relationship was consummated through a Business Agreement which included a forum selection clause that stated, "Any lawsuit relating to any matter arising under this agreement shall be initiated in a State or Federal Court located in San Jose, California." The Agreement also provided that the Franchisee consented to jurisdiction, venue, and to the service, of process, pleading, and notices in the state and federal courts of California. Franchisee sued Franchisor for Deceptive Trade Practice Act (DTPA) violations, and Defendant moved to dismiss based on the forum selection clause. The trial court denied the Motion to Dismiss. However, the Court of Appeals held the trial court abused its discretion in denying the Motion to Dismiss.

The court held that Plaintiff's business tort claims arose under the parties' Business Agreement, and therefore the forum selection clause governed. The court cited the Supreme Court decision in Pinto Technology Ventures which held that business tort claims were subject to the forum-selection clause in a shareholders agreement. The court held that using the term "matter" showed the forum selection clause would apply to matters other than breach of contract claims. In addition, the extra-contractual claims emanated from the Business Agreement because the rights and representations in dispute were related to the Agreement. Therefore, there was a but-for relationship between the dispute and the Business Agreement, so Plaintiff s pleading did not remove its claims from the scope of the forum selection clause.

The court also held that the forum selection provision was unambiguous. It used the mandatory word "shall," and therefore this clause was mandatory. In addition, Plaintiff did not establish an exception to the general rule of enforceability; it did not seek to establish that (1) enforcement would be unreasonable or unjust; (2) the clause was invalid for reasons of fraud or overreaching; (3) enforcement would contravene a strong

public policy of the forum where the suit was brought; or (4) the selected forum would be seriously inconvenient for trial. Therefore, the forum selection clause applied and the trial court abused its discretion by denying the Motion to Dismiss.