The GPMemorandum

TO: **OUR FRANCHISE AND DISTRIBUTION CLIENTS AND FRIENDS**

FROM: **GRAY PLANT MOOTY'S FRANCHISE AND DISTRIBUTION PRACTICE GROUP**

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CASE SUMMARIES

Below are summaries of recent case decisions of interest to franchisors.

ARBITRATION

COURT FINDS EMPLOYEE'S WAGE AND HOUR CLAIM FALLS WITHIN ARBITRATION PROVISION OF ONLINE EMPLOYMENT APPLICATION

A federal court in Illinois found that an arbitration agreement in a franchisor's online employment application is valid and enforceable, and held that the arbitrator should decide whether the arbitration agreement allows class arbitration. *Chatman v. Pizza Hut, Inc.*, 2013 U.S. Dist. LEXIS 73426 (N.D. Ill. May 23, 2013). The case was brought as a class action in state court by a delivery driver on behalf of himself and all other similarly situated employees. The plaintiff asserted claims against Pizza Hut and the franchisee under the Illinois Wage Payment and Collection Act and the Illinois Minimum Wage Law. Pizza Hut removed the case to federal court and filed a motion to compel arbitration based upon the arbitration provision in the online job application the employee had completed and submitted. Pizza Hut also sought an order requiring that the arbitration proceed on an individual basis rather than as a class action.

The employee-plaintiff argued that there was no valid agreement to arbitrate because the online application lacked consideration. Pizza Hut countered that its promise to consider the plaintiff for employment, its obligation to submit to binding arbitration, and its employment of the plaintiff constituted

sufficient consideration. The court agreed and granted Pizza Hut's motion to compel arbitration, but denied its motion to order the arbitrator to hold individual arbitrations. Instead, after reviewing the existing case law, the court determined that the issue of whether to arbitrate as a class or on an individual basis was within the arbitrator's discretion to decide.

CONTRACTS

FRANCHISEE'S BREACH OF CONTRACT AND BREACH OF GOOD FAITH AND FAIR DEALING CLAIMS DISMISSED IN TERMINATION CASE

In *Damabeh v. 7-Eleven, Inc.*, 2013 U.S. Dist. LEXIS 66565 (N.D. Cal. May 8, 2013), a federal court in California dismissed a franchisee's claims that 7-Eleven breached the express terms of the franchise agreement, breached the implied covenant of good faith and fair dealing, and tortiously interfered with the franchisee's prospective business advantage when 7-Eleven terminated the franchise agreement instead of repairing damage to the franchisee's store. The parties' claims and defenses relied on a franchise agreement provision providing that the agreement could be terminated if the store was damaged and, in 7-Eleven's determination, could not "reasonably be repaired or replaced within thirty days or less." During a fire in a neighboring store, firefighters cut a hole approximately 1.5 feet in diameter in the ceiling of the franchisee's store. 7-Eleven determined that the store could not be repaired within thirty days and terminated the franchise agreement.

The court dismissed the franchisee's claim that the termination constituted a breach of contract because the termination provision merely required 7-Eleven to make a "determination" that the store could not be repaired within thirty days, even if that determination was "wrong" or "unsupported." And evidence that a 7-Eleven representative told the franchisee, prior to the issuance of the termination letter, that the store could be repaired in one week did not change the court's holding. Nothing in the agreement precluded 7-Eleven from reassessing its determination, the court decided. Further, the franchisee's claim that 7-Eleven had breached the implied covenant of good faith and fair dealing by removing merchandise from the store after the termination, without the franchisee's knowledge, was dismissed because the agreement expressly permitted 7-Eleven to reclaim merchandise from the store upon termination and it neither explicitly nor implicitly required the franchisee's knowledge that 7-Eleven was doing so. Finally, the court dismissed the franchisee's tortious interference claims because the franchisee had not shown that 7-Eleven's conduct was wrongful, that 7-Eleven owed a duty to the franchisee, or that the franchisee's relationship with any "particular" individual had been interfered with.

CHOICE OF VENUE

COURT TRANSFERS EMPLOYMENT ACTION TO FRANCHISOR'S HOME STATE

The Minnesota federal district court recently transferred to the Northern District of Texas a putative collective action against franchisor Jani-King International and two wholly-owned subsidiaries. *Von Brugger v. Jani-King of Minn., Inc.*, 2013 U.S. Dist. LEXIS 74548 (D. Minn. May 28, 2013). The defendants are Texas corporations headquartered in Texas. Von Brugger, the plaintiff, who worked primarily as an assistant operations manager for Jani-King of Minnesota, claims that the defendants intentionally misclassified him (and other employees) as exempt from the Fair Labor Standards Act so that the defendants could avoid paying overtime.

In granting the defendants' motion to transfer, the court considered it most significant that if the case proceeded as a collective action, the Northern District of Texas would likely be the only appropriate forum because Minnesota would lack personal jurisdiction over several necessary defendants. In addition, the court discounted the typical deference to the plaintiff's choice of forum because there were more than 130 potential opt-in plaintiffs who worked for Jani-King affiliates across the United States. Finally, the court briefly considered the named plaintiff's argument that he could not afford to travel to Texas, but observed that he did not substantiate that claim.

COURT FINDS PERSONAL JURISDICTION OVER FRANCHISEE DESPITE COMPETING CLAUSES IN AGREEMENTS

When two franchise agreements contained contradictory choice-of-law and forum selection clauses, the United States District Court for the Northern District of Ohio decided that Pennsylvania law should control, but that it had personal jurisdiction over the franchisee and Ohio was the appropriate forum. *Mgmt. Recruiters Int'l, Inc. v. Corbin*, 2013 U.S. Dist. LEXIS 69736 (N.D. Ohio May 16, 2013). In this case, franchisor Management Recruiters International, Inc. brought suit against franchisees Van Corbin and Management Consulting Group, Inc. alleging they owed fees under franchise agreements made between the parties. Corbin moved to dismiss, claiming the amount in controversy did not exceed $75,000, Ohio did not have personal jurisdiction over him, and the venue was improper. The court denied Corbin's motion based on the amount in controversy but requested supplemental briefing for the remaining issues.

In its second opinion, the court denied Corbin's motion to dismiss based on lack of personal jurisdiction and improper venue. The court focused on the contradictory choice-of-law and forum selection clauses in two franchise agreements: a Contract Staffing Agreement named Ohio as the proper forum and controlling law in arbitration, while a franchise agreement more generally named Pennsylvania as providing the

proper forum and controlling law. With regard to the choice-of-law issue, the court reasoned that Pennsylvania law should apply, as the parties' franchise agreement stipulated that Pennsylvania law would govern "all matters relating to or arising out of the[ir] relationship," and nothing suggested that Pennsylvania law would be inappropriate under the circumstances. As for the forum selection and personal jurisdiction issues, the court read the agreements together and concluded that permissive language allowed the parties to bring a dispute in either Ohio or Pennsylvania. Accordingly, by signing the agreements, Corbin gave effective consent to personal jurisdiction and venue in the Ohio federal court, making it proper for that court to hear and decide the case so long as it applied Pennsylvania law.

FRAUD/MISREPRESENTATION

WISCONSIN COURT RULES THAT EXCULPATORY CLAUSES IN PARTIES' CONTRACT DO NOT BAR FRANCHISEE FROM BRINGING MISREPRESENTATION CLAIM

In *C&M Hardware v. True Value Co.*, 2013 Wisc. App. LEXIS 404 (Wisc. Ct. App. May 9, 2013), the appellate court declined to enforce two exculpatory clauses in the parties' Retail Member Agreement. C&M sued True Value for misrepresentations that were allegedly made to induce C&M to become a franchisee. The trial court granted True Value's motion for summary judgment based on the language in two different exculpatory provisions in the parties' contract. The court of appeals reversed the ruling on these misrepresentation claims after determining that the exculpatory language failed to clearly, unambiguously, and unmistakably explain to the franchisee the risks it was accepting, and the form of the exculpatory provisions did not alert the franchisee of the nature and significance of the document being signed.

One of the provisions at issue stated that True Value had made "NO REPRESENTATIONS OR WARRANTIES EITHER EXPRESS OR IMPLIED REGARDING THE PERFORMANCE OF [C&M's] BUSINESS," and the other was a standard integration clause that identified the written contract as the entire and complete agreement between the parties. Under Wisconsin law, an exculpatory clause in a contract must specifically identify the tort that is being disclaimed. The court of appeals concluded that the contract did not clearly indicate that True Value was requiring C&M to waive its right to any tort claims in general, let alone misrepresentation claims in particular. It noted that neither exculpatory provision was sufficiently conspicuous to provide C&M with adequate notice of its nature and significance, since the two disclaimers appeared on separate pages of the contract, but on neither the first nor the last page. The provisions did not have a heading or other feature that would draw attention to them, and were merely two sentences among 35 paragraphs of "often opaque legalese." Based on these deficiencies, the court concluded that the exculpatory clauses were void and unenforceable as against Wisconsin public policy, and it reversed the trial court's summary judgment with respect to C&M's misrepresentation claims.

COURT FINDS THAT CLEAR LANGUAGE IN AGREEMENTS DISPROVES FRANCHISEE'S REASONABLE RELIANCE ON FRANCHISOR'S PROMISES

In *Ayu's Global Tire, LLC v. Big O Tires, LLC,* 2013 Cal. App. Unpub. LEXIS 3721 (Cal. Ct. App. May 24, 2013), the California Court of Appeals, applying Colorado law, found that clear and specific language in a Uniform Franchise Offering Circular and franchise agreement undermined a franchisee's assertion that he reasonably relied on purported precontract misrepresentations and omissions by the franchisor. In this case, a tire store franchisee claimed that he was fraudulently induced to enter into a franchise agreement with Big O Tires. He alleged that he had been assured by Big O that it did not require prior experience in running a tire store in order to make the franchise a success because Big O would provide "many services and benefits" to support the franchisee. In addition, the franchisee alleged that Big O withheld from him the fact that many of its franchises had failed. The trial court granted Big O's motion for summary judgment on the fraud in the inducement claim, holding that the franchisee had failed to show that it reasonably relied on Big O's misrepresentations and omissions.

The appeals court affirmed. It noted that in order to succeed in a fraudulent inducement claim under Colorado law, a plaintiff must demonstrate that it reasonably relied on an alleged misrepresentation or material omission of fact. The franchisee failed to meet this standard because, among other things, both the UFOC and the franchise agreement contained disclaimers stating that the franchisee had not been promised anything prior to signing the contract and that Big O was not guaranteeing the success of the franchise. As for the fraudulent concealment claim, the court found that Big O had no duty to disclose any oral or written information regarding actual or potential earnings other than what specifically appeared in the UFOC.

DAMAGES TO FRANCHISOR – ATTORNEYS' FEES

TEXAS APPEALS COURT HOLDS FRANCHISOR NOT ENTITLED TO AWARD OF FEES IN ENFORCING NONCOMPETE AGREEMENT THAT WAS REFORMED

A franchisor that successfully enforced its franchisees' covenants against competition was recently prevented by the Texas Court of Appeals from recovering its legal costs of enforcement. *Franlink, Inc. v GJSM Unlimited, Inc.,* 2013 Tex. App. LEXIS 5118 (Tex. Ct. App. Apr. 25, 2013). Franlink, the franchisor, had sued its former franchisees for injunctive relief to prevent the breach of a noncompete provision in their franchise agreements. The trial court granted the injunction, but denied its request for attorneys' fees. The dispute on appeal centered on whether Franlink was entitled to recover fees even though the trial court had reformed Franlink's noncompete provision, by narrowing its geographic scope, before enforcing it against the former franchisees. Franlink argued that it was entitled to fees as the prevailing party under the Texas Civil

Practice and Remedies Code, and that the legislative intent of removing barriers to the enforcement of noncompete clauses, combined with the plain language of the Texas Covenant Not to Compete Act, supported its entitlement to attorneys' fees.

The court of appeals disagreed, and held that the Covenant Not to Compete Act precluded an award of attorneys' fees where a court reforms a disputed noncompete covenant. The court based its decision on a close reading of the act, reasoning that it was clear that the legislature intended to permit the recovery of attorneys' fees only in the context of a personal-services agreement, where a promisor (such as the franchisees) satisfies certain evidentiary requirements defending against enforcement of an unreasonable noncompete covenant. The court also noted that a party seeking to enforce an unreasonable noncompete covenant that must be judicially reformed is exclusively limited to injunctive relief, and may not obtain attorneys' fees.

ENCROACHMENT

A RHODE ISLAND COURT REJECTS WENDY'S FRANCHISEE'S CHALLENGE TO THE NEARBY DEVELOPMENT OF A MCDONALD'S FRANCHISE

In *CCF, LLC v. Pimental*, 2013 R.I. Super. LEXIS 98 (R.I. Super. Ct. May 24, 2013), a Wendy's franchisee in East Greenwich, Rhode Island, sued McDonald's Corporation and a town official challenging the approval of various permits and approvals issued by the local planning board and zoning board that allowed for a McDonald's drive-through restaurant across from the Wendy's franchisee's restaurant. On the parties' cross-motions for summary judgment, the court found for McDonald's. It weighed whether the Wendy's franchisee had standing to appeal the decisions of the planning board and the zoning board. Because Rhode Island's statute does not define who is an aggrieved party to appeal a planning board's decision, the court looked to other jurisdictions.

Concluding that courts in other jurisdictions have liberally interpreted an "aggrieved party" to include nearby tenants and property owners, the Rhode Island court held that the Wendy's franchisee had standing to appeal the planning board's decision. But the court dismissed the claim because the Wendy's franchisee filed its appeal too late. On the appeal of the zoning board's decision granting the drive-through, the court found for McDonald's. The statute that applied to the zoning board's decision specifically defined an aggrieved party to be a property owner. The Wendy's franchisee did not have standing, according to the court, because it was only a lessee. The court granted summary judgment to McDonald's.

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