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Franchise Sales/Transactions

Closing Addendum and Integration Clause Defeat Claim of Unlawful Financial Performance Representation

In a recent decision, a federal district court in the Eastern District of Pennsylvania granted summary judgment to a franchisor on a terminated franchisee's counterclaim. In *Vino 100, LLC v. Smoke on the Water, LLC*, 2012 U.S. Dist. LEXIS 46465 (E.D. Penn. Mar. 30, 2012), a wine/tobacco store franchisee had been terminated for failure to pay royalties and for breaching its lease agreement for the franchised business premises due to nonpayment. As a defense and counterclaim to the franchisor's action for damages, the franchisee asserted that the franchisor had made an unlawful, undisclosed financial performance representation during the sales process, in violation of the FTC's Franchise Rule. The franchisee argued that this violation rendered the franchise agreements at issue void as against the public policy of Pennsylvania.

The court noted that the Franchise Rule empowers the FTC (and not individual litigants) to enforce its provisions. Further, although Pennsylvania law states that courts will not enforce contracts that are opposed to the public interest, the franchisee's assertion that Pennsylvania law therefore incorporated the disclosure requirements of the FTC Franchise Rule was without merit. The court also held that the franchisee did not have a viable claim for fraudulent inducement of the franchise agreements. Given that the franchise agreements contained an integration clause and a separate closing addendum, both of which stated that no earnings information had been provided by the franchisor, the parol evidence rule prevented the franchisee from relying on the franchisor's alleged oral financial performance representations.