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BLOGS

Damages

Federal Court Enforces Liquidated Damages Provision Under Washington Law

A federal court in Washington granted a franchisor's motion for summary judgment enforcing the liquidated damages provision in the parties' franchise agreement. *Red Lion Hotels Franchising, Inc. v. First Capital Real Estate Invs., LLC*, 2018 WL 4259241 (E.D. Wash. Sept. 6, 2018). Red Lion brought a breach of contract action against three former franchisees who defaulted under their agreements, seeking liquidated damages and past due fees. The franchisees conceded that the license agreements were enforceable contracts and that Red Lion lawfully terminated the agreements. The only issue in dispute was the enforceability of the liquidated damages clause.

Applying a two-part test under Washington law, the court first analyzed whether the clause was a reasonable forecast of compensation for harm at the time the contract was signed. The franchisees claimed the provision was unreasonable because hotel revenues plummeted immediately after they began operating, and then clientele declined after the shale oil market crashed. The court rejected this argument, noting that these events occurred after execution of the franchise agreements. The court also considered party sophistication in determining the reasonableness of the liquidated damages provision. Here, the franchisees specialized in turning around failing real estate projects, knew of the risks associated with the properties in question, and agreed to the liquidated damages provision. The court further noted that the franchisees demonstrated their expertise when they negotiated other terms in the franchise agreements and received concessions from Red Lion. Finally, the court found the liquidated damages provision satisfied the second factor, as the harm was "incapable or very difficult of assessment" at the time of contracting. The franchise agreements involved inherent risks for both parties, given the failing state of the hotels at the time and their location in difficult markets. Further, Washington courts have recognized that the real estate market is an area in which liquidated damages provisions are reasonable. For these reasons, the court enforced the liquidated damages provision.

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