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Franchise Law

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I. INTRODUCTION

THIS Article provides an update of case law and legislative efforts that have had, or will have, an impact on franchise and dealership law in Texas and the Fifth Circuit. This update provides an overview of developments and opinions during the Survey period, but it is not an exhaustive reference for all cases regarding franchises and dealerships during the Survey period. Notably, this was not a year of significant decisions but rather a year in which courts reminded businesses and counsel that the plain meaning of the words in contracts between the parties is important in deciding franchise and distribution disputes.

II. FRANCHISE BASICS

Franchisors continued to adjust to the amended Federal Trade Commission Franchise Rule[1] during the Survey period, but there were no significant developments in basic franchise, business opportunity, or dealership laws.

III. PROCEDURE

A. JURISDICTION

The first issue a court normally considers in a case is jurisdiction—whether the court has the authority to hear the dispute. Several state and federal courts addressed this issue during the Survey period. In *Bellfort Enterprises Inc. v. PetroTex Fuels Inc.*,[2] the plaintiff challenged the district

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1. 16 C.F.R. § 436 (2010).
2. 339 F. App'x 416 (5th Cir. 2009).

court's refusal to remand the action to state court after arguing that the federal court did not have federal-question jurisdiction. Plaintiff Bellfort, who sold motor fuel and conducted automotive repairs, had a dealer marketing contract with defendant PetroTex, which supplied the motor fuel. Although the parties had a dealer marketing contract that constituted a franchise agreement pursuant to the Petroleum Marketing Practices Act (PMPA),[3] Bellfort argued that PetroTex did not provide certain incentives promised under the franchise agreement[4] and overcharged for fuel.[5] After Bellfort filed its lawsuit in Texas state court, PetroTex removed the suit to federal district court and filed counterclaims against Bellfort and its owner, Soon Yim.

Bellfort and Yim challenged the removal by arguing that the case did not contain a federal question.[6] As it is well known, lower federal courts (i.e., district courts) have limited jurisdiction, and the plaintiff must establish that the district court has the power to hear a particular action. Because subject-matter jurisdiction cannot be waived or agreed to between the parties, the plaintiff must show that jurisdiction is based on federal-question jurisdiction, diversity jurisdiction, or another basis authorized by a federal statute, the U.S. Constitution, or a U.S. treaty.

In its initial order, the district court granted Bellfort and Yim's motion for remand for lack of federal-question jurisdiction.[7] On rehearing, the district court vacated its initial order and held that "jurisdiction was proper because the PMPA preempted Bellfort's state law claims."[8] As the action continued in federal district court, PetroTex moved for summary judgment, and the district court granted the motion for summary judgment in PetroTex's favor. Bellfort and Yim appealed.[9] The only issue that the Fifth Circuit addressed was whether federal subject-matter jurisdiction existed.[10]

PetroTex had used the "well-pleaded complaint" rule to establish that federal-question jurisdiction existed.[11] Relying on particular statements from Bellfort's complaint, Bellfort alleged that PetroTex terminated the franchise agreement. PetroTex, therefore, concluded that Bellfort's claims fell under the PMPA, which was "designed to protect franchisees from arbitrary and discriminatory termination or nonrenewal of a franchise."[12]

The Fifth Circuit used two well-known concepts to resolve this jurisdictional question: (i) the "well-pleaded complaint rule," and (ii) the "artful

3. *Id.* at 417 (citing 15 U.S.C. § 2801).
4. *Id.*
5. *Id.*
6. *Id.*
7. *Id.*
8. *Id.*
9. *Id.*
10. *Id.* at 418.
11. *Id.*
12. *Id.* (quoting Kostantas v. Exxon Co., 663 F.2d 605, 606 (5th Cir. 1981)).

pleading doctrine."[13] The Fifth Circuit noted that "[t]he well-pleaded complaint rule provides that 'a federal court has original or removal jurisdiction *only if a federal question appears on the face of the plaintiff's well-pleaded complaint*' and that 'there is no federal jurisdiction if the plaintiff properly pleads only a state law cause of action.'"[14] The Fifth Circuit further noted that the artful pleading doctrine does not allow a plaintiff to hide a federal question (and defeat removal) if the plaintiff has pled in a way to "artfully avoid[ ] any suggestion of a federal issue."[15]

In its analysis, the Fifth Circuit concluded that Bellfort's complaint did not invoke the protections of the PMPA.[16] The Fifth Circuit found that, although Bellfort partly sought a declaratory judgment that its franchise agreement with PetroTex was terminated, Bellfort's only intent was to assert a breach of contract claim.[17] The court noted that Bellfort's requested relief was "inconsistent with an argument that PetroTex had already terminated the franchise agreement."[18]

In *TGI Friday's Inc. v. Great Northwest Restaurants, Inc.*,[19] several franchisees challenged whether they were amenable to personal jurisdiction in Texas. As further discussed below, Friday's filed a trademark infringement action against several franchisees when they failed to cease use of Friday's trademarks and service marks after termination of eleven franchise agreements. Pursuant to the franchise agreements, defendants operated TGI Friday's restaurants in California, Oregon, and Washington.[20]

Friday's is a New York corporation with its principal place of business in Carrollton, Texas. Defendants are located in several states. Defendant Great Northwest Restaurants, Inc., a Washington corporation with its principal place of business in California, operated four restaurants in Washington and one in Oregon. Defendant PRC Restaurants, Inc., a Washington corporation with its principal place of business in California, operated one restaurant in Washington. California corporations TGIA Restaurants, Inc. and Ten Forward Dining, Inc. were assignees of five franchise agreements for five restaurants in California.[21] Defendants first challenged personal jurisdiction.[22]

Because Friday's operates and franchises restaurants throughout the United States, "[e]ach franchise agreement contain[ed] an identical or nearly identical provision, in capital letters and bold font, addressing

13. *Id.*
14. *Id.* (quoting Gutierrez v. Flores, 543 F.3d 248, 251-52 (5th Cir. 2008)) (emphasis added).
15. *Id.*
16. *Id.*
17. *Id.*
18. *Id.*
19. 652 F. Supp. 2d 750 (N.D. Tex. 2009).
20. *Id.* at 754.
21. *Id.*
22. *Id.*

choice of law, jurisdiction, and venue" in Texas.[23] The franchise agreements also provided that "franchisee and principals each irrevocably accept[ed] and submit[ted] to the jurisdiction of the courts of the State of Texas and the federal courts located in Dallas County, Texas" for disputes relating to the agreements.[24] Despite these provisions, defendants argued that they did not have sufficient "minimum contacts" with Texas to confer personal jurisdiction. Although the district court agreed with defendants' contention that entering into the franchise agreements did not automatically establish sufficient minimum contacts,[25] the district court looked at the circumstances, such as negotiations and circumstances of the contract, to determine whether defendants had purposefully established minimum contacts. The district court held that defendants had not only established their minimum contacts through their course of dealing, but that defendants had "extensive" contacts with Texas.[26] Defendants entered into eleven, twenty-year franchise agreements with Friday's. Defendants' principals engaged in extensive negotiations via face-to-face, telephone, and email communications in Texas. Defendants' principals traveled to Texas on several occasions to discuss legal aspects, operations, and termination. Defendants' representatives attended annual training in Texas. Defendants sent their payments to Texas, and Friday's support to defendants came from Texas. Defendants did not dispute these facts.

Based on Friday's undisputed evidence, the district court concluded that defendants "purposefully availed themselves of the privilege of conducting activities in Texas, and that defendants certainly should have reasonably anticipated being haled into court in Texas."[27] The district court denied defendants' motion to dismiss for lack of personal jurisdiction.[28]

In *Qassas v. Daylight Donut Flour Co., LLC*,[29] the district court addressed personal jurisdiction related to a marketing representative agreement for a donut shop licensor. Latif Qassas (a Sugarland, Texas, resident) and Daylight (which has at least thirty-five donut stores that do business under the Daylight name) entered into an international marketing representative agreement in 2006. Pursuant to the agreement, Qassas agreed to "acquire new clients internationally, train and open new international stores, and [complete] the international contracts."[30] Qassas received a commission for food and equipment purchases plus a training fee.[31]

Through a letter to Qassas's home, Daylight terminated the representative agreement in July 2008. Qassas sued Daylight in Harris County,

23. *Id.* at 755.
24. *Id.*
25. *Id.* at 757 (citing Burger King Corp. v. Rudzewicz, 471 U.S. 462 (1985)).
26. *Id.*
27. *Id.* at 758.
28. *Id.*
29. No. 4:09-CV-0208, 2009 WL 1795004 (S.D. Tex. June 24, 2009).
30. *Id.* at *1.
31. *Id.*

Texas, and Daylight removed the action to the Southern District of Texas. Daylight moved to dismiss for lack of personal jurisdiction. Daylight claimed that it did not have any Texas "offices, warehouses, or facilities."[32] Also, Daylight claimed that it did not have Texas employees or agents. Daylight described its international and domestic donut shops, including the thirty-five in Texas, as "'customers' of Daylight with whom it ha[d] 'limited license agreements.'"[33] The limited license agreement allowed Daylight's "customers" to use the Daylight name, receive a protected territory, and purchase Daylight's raw products. The only fee that Daylight received was for purchase of the materials—no franchise fees, no percentage of sales, and no payment from the sales of its customers' products. Daylight also claimed that it did not support, manage, or interfere with its customers' operations.[34]

In evaluating general personal jurisdiction based on Daylight's presence in Texas, Daylight argued that the fact that it shipped materials to its Texas customers constituted only doing business *with* Texas, not doing business *in* Texas.[35] Therefore, it was not subject to personal jurisdiction. The district court agreed.[36] It noted that Daylight did business *with* various Texas companies, but that "those entities [were] independently owned stores in Texas."[37] Although Daylight granted licenses to Texas store owners, the district court held that "Daylight [did] not receive any royalties or percentages from the Texas stores."[38]

The district court similarly held that Daylight's website was not sufficient to confer personal jurisdiction.[39] "Whether personal jurisdiction can be constitutionally exercised over a defendant based on operation of a website depends on the 'nature and quality of commercial activity that an entity conducts over the Internet.'"[40] The court concluded that Daylight's website content was "passive," which meant that it provided only "general information about the company and information about owning a Daylight store."[41] Although the website provided a store locator feature, online pre-application form, and an online store, the district court held that the posted information was "merely a passive advertisement."[42] Moreover, Qassas presented "no evidence pertaining to Daylight's sales over the website, and thus no evidence of sales to Texas residents."[43] Even considering Daylight's "contacts" in the aggregate, the court held that these contacts were "not so substantial that [Daylight]

32. *Id.*
33. *Id.*
34. *Id.* at *2.
35. *Id.* at *3 (citing Access Telecom, Inc. v. MCI Telecomms. Corp., 197 F.3d 694, 716-18 (5th Cir. 1999)).
36. *Id.*
37. *Id.*
38. *Id.* at *3-4.
39. *Id.* at *5.
40. *Id.* (quoting Mink v. AAAA Dev. LLC, 190 F.3d 333, 336 (5th Cir. 1999)).
41. *Id.*
42. *Id.*
43. *Id.*

'should have reasonably expected to be sued in Texas on any matter.'"[44]

The district court also found that specific jurisdiction could not be established.[45] The court concluded that Daylight's contacts and related communications related to the representative agreement were insufficient.[46] "[M]inimum contacts cannot be established by 'merely contracting.'"[47] Based on the evidence before the court, Qassas failed to establish personal jurisdiction.[48]

DAVACO, Inc. v. Dunkin' Brands, Inc.[49] was a personal jurisdiction case involving the interplay between franchisor, franchisee, and a third-party contractor. Dunkin' Brands hired DAVACO to perform construction services on Dunkin' Donuts stores throughout the United States. For stores in Georgia and Maryland, DAVACO entered into contracts with the franchisees. During the construction of the improvements for the Georgia and Maryland franchisees, DAVACO alleged that it performed additional work not provided for in the contract. Although DAVACO alleged it performed the work, it asserted that the franchisees refused to pay. DAVACO filed a suit, asserting breach of contract, negligent misrepresentation, fraud, and unjust enrichment in Texas state court. The defendant franchisees removed the action to federal court and moved to dismiss for lack of personal jurisdiction.[50]

The parties engaged in considerable jurisdictional discovery. Based on a contract theory, the district court held that DAVACO did not meet its burden of proving that the franchisees availed themselves of Texas law.[51] The district court concluded that "the evidence show[ed] that at least some of the contracts were signed . . . at [the franchisees'] stores in Maryland and Georgia," where the entirety of the work was performed.[52] The court also held that telephone conversations, of which DAVACO offered no specific details, would, at most, be considered "unilateral activity of those who claim some relationship with a nonresident defendant."[53] This activity was not enough to satisfy the minimum-contacts requirement. Therefore, the district court held that DAVACO failed to establish that the Georgia and Maryland franchisees had exposed themselves to a lawsuit in Texas.[54]

Personal jurisdiction based on a tort theory also failed.[55] First, the district court held that DAVACO failed to identify any specific misrepresen-

44. *Id.* at *6 (quoting Johnston v. Multidata Sys. Int'l Corp., 532 F.3d 602, 613 (5th Cir. 2000)).
45. *Id.*
46. *Id.*
47. *Id.*
48. *Id.*
49. No. 3:08-cv-0581-M, 2008 WL 4975880 (N.D. Tex. Nov. 21, 2008).
50. *Id.* at *1.
51. *Id.* at *2.
52. *Id.*
53. *Id.* (quoting Hanson v. Penckla, 357 U.S. 235, 253 (1958)).
54. *Id.*
55. *Id.* at *3.

tation on which DAVACO relied.[56] The district court noted that this requirement was necessary for a fraud claim in federal court.[57] The district court also noted that DAVACO had failed to allege other elements of a fraud claim, such as the falsity of any statement, or that the franchisees were negligent in making any statement.[58] DAVACO's claims were dismissed for lack of personal jurisdiction.[59]

During this Survey period, the Southern District of Texas reminded practitioners of a few items relating to jurisdiction. In *Ford Motor Co. v. DeMontrond Lincoln Mercury Co.*,[60] the district court made its ruling on the plaintiff's motion for a preliminary injunction on only those claims related to the Lanham Act. The district court noted that it had "clear" subject-matter jurisdiction over the Lanham Act claims.[61] Therefore, even if an action includes claims under the Lanham Act (or any other statute providing for federal-question jurisdiction), subject-matter jurisdiction is not automatically determined as to similarly pled and related state-law claims. Furthermore, the district court may decide to bifurcate its decision on those claims where it "clearly" has subject-matter jurisdiction.

B. Forum Selection

In *TGI Friday's Inc. v. Great Northwest Restaurants, Inc.*, discussed above, defendants also contended that Texas was an improper venue for the action.[62] Because Friday's asserted claims under the Lanham Act, the district court held that "28 U.S.C. § 1391(b) control[led] where venue [was] proper."[63] Friday's had the burden to establish proper venue.

Friday's relied on § 1391(b)(2) to establish that venue was proper in the Northern District of Texas because "a substantial part of the events or omissions giving rise to the claim" occurred in that district.[64] Friday's also relied on the forum selection clause in each of the franchise agreements, which stated that the parties "agree that any claim, controversy or dispute arising out of or relating to this agreement or the performance thereof which cannot be amicably settled . . . shall be resolved by a proceeding in a court in Dallas County, Texas."[65]

To determine applicability of the forum selection clause, the court made a two-step determination: (1) whether Friday's claims fell within the scope of the forum selection clause, and (2) whether the forum selec-

56. *Id.*
57. *Id.*
58. *Id.*
59. *Id.* at *4.
60. No. H-09-3082, 2009 WL 3151306 (S.D. Tex. Sept. 28, 2009).
61. *Id.* at *1.
62. 652 F. Supp. 2d 750, 758 (N.D. Tex. Aug 20, 2009); *see supra* notes 24-28 and accompanying text.
63. *Friday's*, 652 F. Supp. 2d at 758.
64. *Id.*
65. *Id.*

tion clause was enforceable under the circumstances.[66] The district court resolved both issues in the affirmative.[67] First, the court held that the broad language of the clause—"arising out of or relating to [the franchise agreements]"—encompassed Friday's claims.[68] Second, the court determined that Friday's four state and federal claims would be treated together because they were predicated on the same facts and issues.[69] "When a party seeks dismissal of a case based on improper venue, a forum selection clause is presumed to be valid 'and should be enforced unless enforcement is shown by the resisting party to be "unreasonable" under the circumstances.'"[70] Defendants' only argument as to the enforceability of the forum selection clause was that it was void under California law.[71] Defendants provided no reason for applying California law. Moreover, defendants did not show that enforcement of the forum selection clause would contravene Texas public policy. Because California law did not apply, the district court held that it needed not consider whether California law would be contravened.[72] Defendants did not show that enforcement of the forum selection clause was unreasonable. Therefore, the district court denied defendants' motion for improper venue.[73]

In *Snaza v. Howard Johnson Franchise Systems, Inc.*,[74] the parents of Duane Snaza brought a wrongful death action against defendants StudentCity.com, Howard Johnson Franchise Systems, Inc., and Howard Johnson International, Inc., after Snaza fell from his balcony on the tenth floor of a Howard Johnson hotel in Mazatlan, Mexico. After StudentCity removed the case from state to federal court, plaintiffs amended their complaint, alleging that Howard Johnson was negligent regarding the height of the hotel railing. Howard Johnson moved to dismiss for *forum non conveniens*.[75]

The district court initially noted the standard for a motion for *forum non conveniens*. "A defendant bears the burden of persuasion as to all elements of the *forum non conveniens* analysis."[76] In deciding a motion to dismiss, the "court first determines whether an alternate forum is available and adequate," then whether "the alternate forum is more convenient for the litigants by weighing the various private and public interest factors."[77] Howard Johnson moved for the trial to be resolved in the Mexican courts.[78]

66. *Id.* at 758-59.
67. *Id.* at 759-60.
68. *Id.* at 759.
69. *Id.*
70. *Id.* at 760 (quoting Int'l Software Sys., Inc. v. Aplicon, Inc., 77 F.3d 112, 114 (5th Cir. 1996)).
71. *Id.* (citing CAL. BUS. & PROF. CODE § 20040.5 (West 2008)).
72. *Id.*
73. *Id.*
74. No. 3:07-CV-0495-0, 2008 WL 5383155 (N.D. Tex. Dec. 24, 2008).
75. *Id.* at *1.
76. *Id.* at *2.
77. *Id.* at *2-3.
78. *Id.* at *3.

The district court first analyzed whether the Mexican courts were available, i.e., whether the entire case and all the parties could come within the jurisdiction of that forum. Howard Johnson agreed to submit to the Mexican court's jurisdiction. In addition, although there was some disagreement, both parties' experts agreed that the court would accept jurisdiction if both parties agreed to submit to the Mexican courts. Plaintiffs objected to the magistrate judge's finding, because the magistrate judge purportedly gave little weight to the plaintiffs' expert witness. For several reasons, including the fact that plaintiffs' expert was a law professor, not a licensed attorney, the district court agreed with the magistrate judge.[79] The magistrate judge also found that the availability of the Mexican court "[could] be assured by conditioning dismissal on the [Mexican court's] willingness to hear the case."[80] The district court agreed that the Mexican court was an available forum.[81]

Likewise, the magistrate judge found that the Mexican court was adequate because "the parties [would] not be deprived of all remedies or treated unfairly, even though they may not enjoy the same benefits as they might receive in an American court."[82] Plaintiffs objected, asserting that Mexican courts "lack procedural safeguards available in the United States, no Mexican attorney would take plaintiffs' case on a contingency fee basis, proceedings in Mexico would not be concluded within a reasonable time frame, and the damages recoverable in Mexico would be very limited."[83] The district court overruled plaintiffs' objection.[84] Based on Fifth Circuit and Texas Supreme Court authorities that had already addressed each of these issues, the district court held that a Mexican court would be adequate.[85]

The district court then considered the magistrate judge's finding on each of the public and private factors. After giving a strong deference to plaintiffs' choice of forum, the district court considered the private factors (i.e., "the relative ease of access to sources of proof; the availability of compulsory process for attendance of unwilling, and the costs of obtaining attendance of willing, witnesses; the probability of an opportunity to view the premises, if view would be appropriate to the action; and all other practical problems that make trial of a case easy, expeditious and inexpensive")[86] and the public factors (i.e., "the administrative difficulties flowing from court congestion; the local interest in having localized controversies decided at home; the interest in having the trial of a diversity case in a forum that is at home with the law that must govern the action; the avoidance of unnecessary problems in conflict of laws, or in the appli-

79. *Id.* at *5.
80. *Id.* at *4.
81. *Id.* at *6.
82. *Id.* at *8.
83. *Id.* at *9.
84. *Id.*
85. *Id.* at *12.
86. *Id.*

cation of foreign law; and the unfairness of burdening citizens in an unrelated forum with jury duty").[87] Notably, the district court observed that while the accident took place in Mexico, some of the documents and witnesses would be located in the United States.[88] The court therefore concluded that "it would be easier to access these [documents and witnesses] by retaining jurisdiction . . . in a United States court."[89] Also, the court believed that a physical viewing of the hotel balcony would not be necessary.[90] Based on advanced technology, "the parties and experts could present photographs and video to the court and/or jury."[91]

The district court determined that the private factors weighed in favor of trying the case in the United States in Texas, and that the public factors were neutral.[92] In light of these findings, the district court held that Howard Johnson had failed to meet its burden of showing that the private and public factors weighed in favor of the Mexican forum.[93] Therefore, the district court accepted in part and rejected in part the magistrate judge's recommendation and sustained in part and overruled in part plaintiffs' objections.[94] Based on the convenience of the parties and witnesses, and in the interest of justice, the district court, sua sponte, transferred the action to the District of Massachusetts—StudentCity's principal place of business.[95] Several private-interest factors influenced the district court's decision—no documents or witnesses were located in Texas, numerous witnesses were located in Massachusetts, and StudentCity's business, employees, management and business decisions were located in, and made in, Massachusetts.[96] Other than the location of plaintiffs' attorneys, which is not a factor to be considered, the case had no connection with Texas.[97] Therefore, the district court directed the clerk to effect transfer of the case to the District of Massachusetts.[98]

C. ARBITRATION

In *Cottman Transmission Systems, L.L.C. v. FVLR Enters., L.L.C.*,[99] discussed in detail below, franchisor Cottman argued that it was entitled to have its dispute with the commercial landlord, FVLR, resolved by binding arbitration. The Dallas Court of Appeals determined whether Cottman had waived its right to arbitration.

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87. *Id.*
88. *Id.*
89. *Id.* at *13.
90. *Id.*
91. *Id.*
92. *Id.* at *14.
93. *Id.*
94. *Id.*
95. *Id.* at *15.
96. *Id.*
97. *Id.*
98. *Id.*
99. 295 S.W.3d 372 (Tex. App.—Dallas 2009, pet. denied); *see infra* notes 197-208 and accompanying text.

"A party waives arbitration if it takes an action inconsistent with its right to arbitration that is prejudicial to the other party."[100] Because Cottman took the case to trial before seeking arbitration, the court of appeals held that Cottman "invoke[ed] the judicial process to [FVLR's] detriment."[101] Therefore, the court of appeals held that Cottman waived its right to arbitration.[102]

IV. INTELLECTUAL PROPERTY: TRADEMARKS

A common fact scenario of unauthorized use of a franchisor's trademarks occurs when a former franchisee continues operations, using the franchisor's trademarks, trade name, and trade dress, following a valid termination of the franchise agreement. This Survey period was no exception. In *Petro Franchise Systems, LLC v. All American Properties, Inc.*,[103] Petro,which owned a system for the operation of full-facility truck/auto travel centers, filed an application for preliminary injunction based on an underlying action for trademark infringement. As franchisor, Petro had a right to sub-franchise its affiliate's proprietary marks. Petro granted franchises to individuals and businesses throughout the United States, including Pennsylvania. Nevertheless, Texas law governed the franchise agreements.

In 2007, Petro's predecessor was acquired by Travel Centers of America, LLC. Travel Centers operated five travel plazas under an affiliate brand within territory belonging to defendants All American Properties, Inc. and All American Plazas, Inc. Defendants claimed that "after the acquisition, [the affiliated brand] began to integrate . . . with the Petro brand," which caused the value of Petro's brand to diminish.[104] Defendants claimed that this caused a decline in their business.[105] The parties exchanged letters and ultimately entered into a "Confidential Settlement Agreement and Mutual Release."[106] The release provided that $500,000 of escrow funds would be used to "cure the monetary default" of one of the franchise agreements and "as advance payments for sums due Petro" under the other franchise agreement.[107] The agreement released claims between the parties to that date.

The escrow funds were applied to the franchise fees owed through April 2008. Although defendants did not dispute that they failed to make any payments for franchise fees after April 2008, defendants argued that Petro "placed [them] in a position [to be] unable to pay those fees."[108] After Petro sent default notices for failure to pay the franchise fees, Petro

100. *Id.* at 380 (citing *In re* Oakwood Mobile Homes, 987 S.W.2d 571, 574 (Tex. 1999)).
101. *Id.*
102. *Id.*
103. 607 F. Supp. 2d 781 (W.D. Tex. March 23, 2009).
104. *Id.* at 785.
105. *Id.* at 787.
106. *Id.* at 786.
107. *Id.*
108. *Id.*

terminated the franchise agreements in late 2008.[109] After termination, Petro sued defendants for "trademark infringement, false designation of origin, and dilution under the Lanham Act; unfair competition and unjust enrichment; trademark infringement under Texas law; breach of contract; and conversion."[110]

Defendants did not contest ownership of the marks or that they continued to use the "marks in commerce and in connection with the sale, offering for sale, distribution, or advertising of any goods."[111] Because defendants not only used identical marks, but also requested that Petro notify its consumers that defendants were still franchisees, the district court held that consumer confusion was likely to be established.[112] "The parties' only dispute [was] whether [defendants'] use of the Petro marks [was] authorized."[113]

Defendants argued that their trademark use was authorized unless Petro proved that the franchise agreements were properly terminated. The district court noted that it was unaware of any Fifth Circuit cases addressing whether a franchisor must prove proper termination before it may obtain equitable relief.[114] Nevertheless, defendants claimed that Petro breached the franchise agreements by improperly integrating its affiliates and Petro's brands. Petro argued that this claim was resolved in the release, and, notwithstanding the release, Petro properly terminated the franchise agreements. The district court concluded that the payment requirements and termination procedure under the franchise agreement were unambiguous.[115] Petro followed the termination procedures to the letter.[116] Also, the court concluded that defendants' actions in response to Petro's alleged breach were not proper.[117] "Treating a contract as continuing, after a breach, deprives the non-breaching party of any excuse for terminating their own performance."[118] When Petro allegedly breached, the court held that defendants had two options: continuing performance or ceasing performance.[119] Defendants did not exercise these options. Moreover, the court held that defendants likely released their counterclaims in the release.[120] Therefore, Petro met its burden of proving that it would likely succeed on the merits.[121] Because Petro met the remaining elements for preliminary injunction, the district court granted Petro's application.[122]

109. *Id.*
110. *Id.*
111. *Id.* at 788.
112. *Id.* at 788-89.
113. *Id.* at 789.
114. *Id.* at 790.
115. *Id.*
116. *Id.*
117. *Id.*
118. *Id.*
119. *Id.*
120. *Id.* at 791-92.
121. *Id.* at 792.
122. *Id.* at 801.

In *TGI Friday's Inc. v. Great Northwest Restaurants, Inc.*,[123] Friday's initiated a trademark infringement action against its former franchisees. Friday's sought a preliminary injunction against the franchisees for their continued use after termination of Friday's trademarks and service marks for restaurants located in California, Oregon, and Washington.

Through eleven separate franchise agreements, Friday's had a franchise relationship with defendants. Friday's and defendants entered into the franchise agreements between 1997 and 2006.[124] The franchise agreements granted standard authorization and provided for standard obligations. The franchise agreements permitted defendants "to use [Friday's] trademarks and service marks in connection with the operation of [TGI Friday's] restaurants."[125] The franchise agreements provided that defendants must cease use of the marks upon termination.[126] The franchise agreements also obligated defendants to pay monthly royalty and advertising fees, for which Friday's could terminate if defendants failed to pay.[127]

Defendants stopped paying their franchise fees in 2007. After a notice of default and no fewer than seven deadline extensions, Friday's terminated the franchise agreements through a termination notice dated December 18, 2008. The termination notice requested compliance with the franchise agreement, including defendants' compliance with the post-termination obligations. Defendants did not abide by the termination obligations of the franchise agreements. Defendants "continue[d] to use [Friday's] marks and hold their restaurants out as TGI Friday's locations."[128] Friday's action for violations of the Lanham Act and other state law trademark infringement causes of action followed.[129]

The district court noted the standard for considering a preliminary injunction. Because it is an "extraordinary remedy," the district court held that a preliminary injunction could be granted only if Friday's established "(1) a substantial likelihood that it [would] prevail on the merits, (2) a substantial threat that it [would] suffer irreparable injury if the injunction [were] not granted, (3) that the threatened injury to it outweigh[ed] the threatened harm the injunction may do to defendants, and (4) that granting the preliminary injunction [would] not disserve the public interest."[130] The district court considered only whether Friday's Lanham Act claims had a substantial likelihood of success.[131]

Defendants did not dispute several factors. They did not dispute that Friday's owned the trademarks and service marks and that the marks

123. 652 F. Supp. 2d 763 (N.D. Tex. Aug. 20, 2009); *see supra* Part III.A-B.
124. *Id.* at 766.
125. *Id.*
126. *Id.*
127. *Id.*
128. *Id.* at 766-67.
129. *Id.* at 767 (noting that defendants asserted several counterclaims, but that those counterclaims were not relevant to the district court's opinion).
130. *Id.*
131. *Id.*

were legally protected. Defendants did not dispute their use of the marks "in commerce in connection with the sale of goods."[132] Because defendants used Friday's exact marks (just as they did while franchisees) and without Friday's consent, the district court held that it was "evident that there [was] a likelihood of consumer confusion between licensed TGI Friday's restaurants and defendants' restaurants."[133] The only disputed issue was whether defendants were using the marks without Friday's authorization.

Although defendants did not dispute that they failed to pay the required royalty and advertising fees and that Friday's adhered to the proper termination procedure, defendants alleged that the "termination of the [franchise] agreements [were] 'wrongful and improper.'"[134] Defendants argued that Friday's was responsible for defendants' inability to pay the royalty and advertising fees because the food distribution system of Friday's was "discriminatory and cost-prohibitive."[135] Defendants alleged that Friday's, through its changed distribution agreement, caused defendants to pay higher freight charges since they were located a great distance from the new distributor.[136] Defendants argued that "because [Friday's] choice of distribution system led to defendants' default" (by failing to pay their royalties and advertising fees), Friday's "breached its duty of good faith and fair dealing when it entered into [the new distribution] agreement."[137] The district court rejected this argument.[138]

The district court held that defendants' argument "[did] not diminish [Friday's] likelihood of success on its trademark infringement claim."[139] Friday's agreement with the new distributor was a business decision that Friday's made in 2000. Defendants "cite[d] no case law or precedent for the proposition that a franchisee who is negatively affected by a business decision of a franchisor . . . is excused from performing its contractual obligations."[140] Defendants offered no evidence for their "alleged distribution-related issues until after they defaulted [under] the franchise agreements."[141] The district court observed that defendants "negotiated their own food distribution contracts" for approximately seven years "without pursuing any claims or issues."[142] Also, defendants' argument was challenged by a forbearance agreement, whereby defendants pur-

132. *Id.*
133. *Id.*
134. *Id.* at 768.
135. *Id.*
136. *Id.* (noting that defendants had uniform freight charges under the old distribution system).
137. *Id.* at 769 (noting that although some circuits have addressed whether a franchisor seeking injunctive relief is required to establish proper termination of the franchise agreements in order to show lack of consent, the Fifth Circuit has not).
138. *Id.*
139. *Id.*
140. *Id.*
141. *Id.*
142. *Id.*

portedly waived any distribution-related claims in 2007.[143] Most notably, the district court held that defendants' nonperformance was not excused:

> [E]ven if defendants have a claim for breach of a duty of good faith and fair dealing (and it is not clear that they do), this does not excuse their nonperformance under the franchise agreements or render [Friday's] termination of the agreements improper. Under Texas law, which applies to the franchise agreements, if a defendant believed that [Friday's] breached the contract, it had two options: continue to perform the contract and sue for partial breach, or cease performance and treat the contract as terminated. A defendant could not cease performing its obligations under the franchise agreement— e.g., paying the franchise fees—while continuing to treat the agreement as valid and enjoying the benefits granted under the agreement— e.g., using [Friday's] marks. Also, any claims defendants may have against [Friday's], including breach of contract or breach of a duty of good faith and fair dealing, have no apparent effect on [Friday's] right to terminate the agreements pursuant to their terms.[144]

The district court concluded that Friday's had a right to terminate the franchise agreements.[145] Furthermore, although Friday's "continued to inspect [the] restaurants, to send [defendants] menus and other promotional materials, and to list defendants' restaurant locations on Friday's website," the district court held that Friday's actions did not indicate any waiver of termination or consent that defendants could continue to use the marks.[146] The district court concluded that Friday's had established a substantial likelihood of success on the merits of its trademark infringement claims.[147]

The district court also found that Friday's had met its burden of establishing a substantial threat of injury if the injunction were not granted.[148] The district court held that consumer confusion was evident.[149] Defendants argued that the court could not rely on consumer confusion to establish substantial threat of injury. The district court countered by observing that the majority of circuits, including the Fifth, "ha[d] addressed [the] issue and held that a court may presume irreparable injury upon finding a likelihood of confusion in a trademark case."[150] Even without this presumption, the court found that Friday's had shown that defendants' passing off of their restaurants as TGI Friday's™ restaurants, after termination, caused Friday's to "los[e] control over its valuable trademarks and the quality of the restaurants operating under its name."[151]

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143. *Id.*
144. *Id.* at 769-70 (internal citations omitted).
145. *Id.* at 770.
146. *Id.*
147. *Id.*
148. *Id.*
149. *Id.* at 771.
150. *Id.* The majority of other circuits included the First, Second, Third, Sixth, Seventh, Eighth, Ninth, and Eleventh. *Id.*
151. *Id.*

The district court further held that Friday's "suffer[ed] a risk of injury to its reputation and the value of its marks even if the alleged infringer offer[ed] superior services."[152]

The district court concluded that Friday's harm outweighed any harm that defendants may suffer.[153] Unlike Friday's harm, defendants' harm was not irreparable. If Friday's did not prevail at trial, the court concluded that the harm caused by closing the restaurants was "calculable and compensable through money damages."[154] In evaluating the public interest factor, the district court held that it considered a broader public interest other than employees losing their jobs and local neighborhoods and economies being hurt.[155] The public interest "promotes the protection of valuable trademarks and service marks in a capital-based economy that rewards success through competition."[156] Accordingly, the district court held that Friday's "satisfied all four requirements for the issuance of a preliminary injunction" and granted Friday's application.[157]

V. THE FRANCHISE RELATIONSHIP, TERMINATION AND NON-RENEWAL

Franchisors, franchisees and their attorneys await the outcome of arbitration proceedings and litigation regarding the closure of General Motors and Chrysler dealerships and the termination of franchise agreements in the spring and summer of 2009. Nevertheless, during the Survey period there were significant developments in the law related to franchise relationships in Texas.

A. THE FRANCHISE RELATIONSHIP

In *Bellfort Enterprises, Inc.*, discussed above, a dealer successfully sought remand of a case involving state-law claims.[158] Bellfort brought a state court action against PetroTex alleging breach of contract, fraud, negligent misrepresentation and unilateral rescission. PetroTex removed the suit to federal court on the basis that the Petroleum Marketing Practices Act (PMPA) preempted the dealer's state-law claims because the "PMPA protect[s] franchisees from arbitrary and discriminatory termination . . . of a franchise" agreement.[159] PetroTex argued that Bellfort's statement in its complaint—"PetroTex's refusal to deliver motorfuel [was] arrogant and tantamount to putting Bellfort out of business; and it did"—conceded that PetroTex had terminated the agreement

152. *Id.* at 772.
153. *Id.*
154. *Id.*
155. *Id.* at 773.
156. *Id.* (quoting Ramada Franchise Sys., 2001 WL 540213, at *3).
157. *Id.*
158. 339 F. App'x 416, 417 (5th Cir. 2009); *see supra* Part III.A, *infra* Part VII.B.
159. *Bellfort*, 339 F. App'x at 418 (quoting Kostantas v. Exxon Co., 663 F.2d 605, 606 (5th Cir. 1981)).

and that Bellfort's complaint invoked the PMPA.[160] The Fifth Circuit concluded that Bellfort, as "master of its complaint," intended only to raise a state-law breach of contract claim, and that Bellfort's request for a declaratory judgment that the agreement be terminated would be inconsistent with a finding that PetroTex had already terminated the agreement.[161] Because states are permitted to "regulate aspects of the franchise relationship not affecting termination by a franchisor," the PMPA did not preempt Bellfort's state-law claims.[162]

B. The Failure to Perform

In *Archer Motor Sales Corp. v. Mazda Motor of America, Inc.*,[163] the district court granted Mazda's motion for summary judgment, because Archer's claims were barred by statutes of limitations. In 1977, Archer began to sell Mazda vehicles through a dealer sales and service agreement. In 1986, Mazda informed Archer that it would offer the next Houston area Mazda dealership to Archer. Instead, in 1990, Mazda offered and awarded a new dealership to a different dealer. Archer quit selling Mazda vehicles in 2002. In July 2004, Mazda approved a second new Houston dealership. In October 2008, Archer filed its claims. The court concluded that Mazda's failure to perform (by failing to offer Archer the next Mazda dealership in Houston) occurred, if at all, in 1990, when Mazda offered the "next" Houston-area Mazda dealership to another dealer.[164] Thus, the limitations period had run long before Archer filed its lawsuit.[165]

C. Termination and Non-Renewal

In *Blackmon-Dunda v. Mary Kay, Inc.*,[166] the Dallas Court of Appeals affirmed the grant of summary judgment to Mary Kay on all claims in a suit brought by a former sales director following termination of her Independent Sales Director agreement.[167] The agreement permitted either party to terminate upon thirty days' notice.[168] Mary Kay terminated the agreement after Ms. Blackmon-Dunda twice used promotional materials in violation of the agreement. Following termination, Ms. Blackmon-Dunda sought commissions she believed she was owed by Mary Kay and brought multiple claims against Mary Kay, including breach of contract, deceptive trade practices and intentional infliction of emotional distress.

The court of appeals concluded that Mary Kay did not breach the

160. *Id.*
161. *Id.*
162. *Id.*
163. No. H-08-3587, 2009 WL 3012835 (S.D. Tex. Sept. 17, 2009).
164. *Id.* at *3.
165. *Id.*
166. No. H-08-3587, 2009 WL 866214 (Tex. App.—Dallas, Apr. 1, 2009, pet. denied).
167. *Id.* at *1.
168. *Id.*

agreement or an oral contract with Ms. Blackmon-Dunda.[169] As to the claim for breach of an oral contract, the court of appeals noted the agreement's integration clause and concluded that Ms. Blackmon-Dunda's claim, that Mary Kay breached an oral promise by its representation to her and other business consultants that "by purchasing Mary Kay Products [they] were building [their] 'businesses' with sales volume and new Consultants," to be without merit.[170] Ms. Blackmon-Dunda was not entitled to commissions for as long as her former sales unit was active, but instead, for only so long as the agreement was in effect.[171] The agreement specified that it was not transferable, and thus Ms. Blackmon-Dunda could not assign or will her income stream from the agreement.

The court of appeals also considered Ms. Blackmon-Dunda's assertion that a "special relationship" existed between her and Mary Kay which thereby precluded summary judgment on her claim for breach of duty of good faith and fair dealing , but the court found the assertion to be without merit.[172] The agreement clearly stated that Ms. Blackmon-Dunda was an independent contractor and there is no authority to support a finding that "an independent contractor has a special relationship with a company for which it sells products."[173] Similarly, the court of appeals held that Mary Kay's refusal to allow Ms. Blackmon-Dunda to be a seminar speaker could not support a claim for intentional infliction of emotional distress.[174] Finally, the court of appeals upheld summary judgment on Ms. Blackmon-Dunda's Deceptive Trade Practices Act, claim since, as Mary Kay's products did not form the basis of her complaint, she was not a consumer for purposes of the Act.[175]

VI. COMMON-LAW CLAIMS

A. Contract Issues

In *Cottman Transmission Systems, L.L.C. v. FVLR Enters., L.L.C.*,[176] a landlord sued its tenant's franchisor for breach of contract, promissory estoppel, fraud, and negligent misrepresentation. FVLR entered into a ten-year commercial lease agreement, which contained a rider, with LBR, L.L.C., in 2001. LBR was the franchisee of Cottman, a transmission repair shop franchisor. Cottman was involved in the negotiations of the lease and demanded that the rider—which gave Cottman the option to assume the lease upon expiration or termination—be part of the lease. The rider required Cottman to assume obligations and replace LBR as lessee within thirty days of termination or expiration of the license agree-

169. *Id.* at *2-4.
170. *Id.* at *3.
171. *Id.* at *4.
172. *Id.*
173. *Id.*
174. *Id.* at *5.
175. *Id.* at *6.
176. 295 S.W.3d 372 (Tex. App.—Dallas 2009, pet. denied).

ment between Cottman and LBR.[177]

In March 2003, LBR moved out of the premises. FVLR informed Cottman that LBR had abandoned the premises, and Cottman consequently terminated its license agreement with LBR. Cottman took over the premises and paid one month's rent. Although Cottman promised its manager that it would pay the rent, Cottman did not pay any further rent. Cottman moved out of the premises in May 2003.[178]

FVLR filed a lawsuit against Cottman, asserting causes of action for breach of contract and promissory estoppel, among others. The jury awarded judgment in favor of FVLR and granted damages of over $175,000 for loss of rent payments, triple net charges, and advertising for new tenants. Cottman appealed.[179]

Cottman argued that it was not bound by the lease or rider and that the jury instruction on partial performance was flawed. On appeal, however, Cottman did not "identify the language [it] wanted included in the instruction or explain the basis for its objection."[180] Therefore, the Dallas Court of Appeals held that "Cottman failed to preserve its [objection] relating to the instruction on partial performance."[181]

The court of appeals noted that "the lease agreement and lease rider [were] subject to the statute of frauds because they concern[ed] the lease of commercial real estate for a period of greater than one year."[182] Although involved in the negotiations, Cottman did not sign the lease agreement or the rider. At trial, FVLR relied on Cottman's alleged partial performance as an exception to the statute of frauds. For actions to constitute partial performance, the actions must be "unequivocally referable" to the alleged oral agreement.[183] Despite Cottman's objections, the evidence supported a finding that Cottman partially performed.[184] Cottman's president testified that Cottman was a beneficiary of the rider, which gave it the option to assume the lease. Moreover, the rider did not require Cottman to provide written notice to FVLR in order to assume the lease. The court of appeals further held that Cottman's payment of the rent for thirty days was a "good indication that Cottman was assuming the lease."[185] Cottman also entered into a management agreement with its manager to operate the repair shop at the premises. In light of this evidence, the court of appeals overruled Cottman's objections and held that Cottman was bound by the rider.[186]

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177. *Id.* at 375.
178. *Id.*
179. *Id.* at 375-76.
180. *Id.*
181. *Id.*
182. *Id.* at 377 (citing TEX. PROP. CODE ANN. § 5.021 (Vernon 2004)).
183. *Id.* (quoting Exxon Corp. v. Breezevale Ltd., 82 S.W.3d 429, 439-40 (Tex. App.—Dallas 2002, pet. denied)).
184. *Id.* at 379.
185. *Id.* at 378.
186. *Id.* at 379.

B. Vicarious Liability

In *Nears v. Holiday Hospitality Franchising, Inc.*,[187] former employee Sharon Nears appealed the trial court's granting of a motion for summary judgment in favor of Holiday Hospitality Franchising, Inc. and Six Continents Hotels, Inc. Nears originally filed a lawsuit in 2000 for wrongful termination. She alleged that her immediate supervisor, Jack Marshall, acted "toward her as an abusive and tyrannical martinet."[188] Holiday and Six Continents filed separate but similar traditional and no-evidence motions for summary judgment. The trial court granted the motions, and Nears timely appealed.[189]

In support of her wrongful-termination claim, Nears alleged that Marshall was violent, drank excessively, and directed his anger toward her. Nears claimed that she "experienced [several] stress-related health problems as a result of Marshall's conduct."[190] At the time Holiday filed its motion for summary judgment, Nears alleged that Holiday was vicariously liable for Marshall's actions, which caused Nears emotional distress. Nears alleged that Marshall and Holiday's management company, ETEX, were Holiday's agents, and that Holiday should be liable "based on franchisor/franchisee liability, respondeat superior, and because Marshall and ETEX were [Holiday's] independent contractors."[191]

Because Nears raised only the theory of actual authority in her summary judgment response, the Texarkana Court of Appeals initially decided that it would not consider Nears's arguments of franchisor/franchisee liability or respondeat superior liability.[192] The court of appeals, however, did note that the franchisor/franchisee liability theory, which was analyzed "in terms of duty and breach of duty," was a "markedly different analysis [from] that of agency based on actual authority."[193] Nevertheless, the court did not address the theory on appeal.[194]

On appeal, Holiday argued that the trial court's granting of its motion for summary judgment should have been sustained "because Nears's intentional infliction of emotional distress claim [was] barred because it [was] covered by a statutory remedy for unlawful retaliation."[195] However, the court of appeals did not consider this ground.[196] Holiday "did not raise the issue of legal impermissibility of Nears's intentional infliction of emotional distress claim in its motion for summary judgment," and thus the court of appeals did not consider that argument.[197]

187. 295 S.W.3d 787 (Tex. App.—Texarkana 2009, no pet. h.).
188. *Id.* at 789.
189. *Id.*
190. *Id.* at 790.
191. *Id.*
192. *Id.* at 791-92.
193. *Id.* at 792 n.4.
194. *Id.* at 792.
195. *Id.*
196. *Id.* at 793.
197. *Id.* at 792-93.

The court of appeals evaluated the summary judgment evidence and determined that Holiday "disprove[d] that any actual and/or apparent authority of ETEX and Marshall existed."[198] "An agent acting within the scope of apparent authority binds a principal as though the principal performed the action."[199] The summary judgment evidence showed that Holiday was not aware of the "material facts" that were the basis of Nears's lawsuit.[200] No Holiday employee or representative oversaw the management or inspection intricacies of the facility at which Nears worked. The court of appeals held that no evidence existed that "would lead a reasonably prudent person to conclude that [Holiday] had any control or right to control Marshall's conduct in any manner."[201]

Nears, likewise, could not provide actual authority. Nears relied on the standards manual promulgated by Holiday Inn Worldwide that required all general managers, such as Marshall, to be certified through Holiday Inn's training program.[202] The court of appeals, however, rejected this argument.[203] The training program and standards set by Holiday were "geared toward ensuring guest satisfaction, not toward the treatment of hotel employees."[204] "Quality control standards for operating a franchise should not be construed to create an agency relationship. The implementation of standards to ensure guest satisfaction in this case [did] not evidence express or implied actual authority flowing from [Holiday] to ETEX or Marshall pertaining to the treatment of hotel employees."[205] As such, the court of appeals held that there was no genuine issue of material fact on the issue of whether Holiday expressly or impliedly delegated authority to ETEX or Marshall to manage the hotel and control the supervisory interactions with Nears. Therefore, the court of appeals sustained the motion for summary judgment.[206]

VII. STATUTORY CLAIMS

A. Covenants Not to Compete

Section 15.50 of the Texas Business and Commerce Code provides that in order for a covenant not to compete to be enforceable, its restrictions must be reasonable as to time, area, and the scope of the activity to be restrained.[207] In *RE/MAX International, Inc. v. Trendsetter Realty, LLC*, a former employee of a RE/MAX franchisee, Deborah Miller, claimed that a provision in her "Independent Contractor Agreement" with the franchisee which stated that, upon termination of the agreement, she

198. *Id.*
199. *Id.* at 793.
200. *Id.* at 794.
201. *Id.* at 794-95.
202. *Id.* at 795.
203. *Id.*
204. *Id.* at 795-96.
205. *Id.* (internal citations omitted).
206. *Id.*
207. Tex. Bus. & Com. Code Ann. § 15.50 (Vernon 2009).

would not infringe RE/MAX's trademarks or imitate RE/MAX's methods of operation, was an unreasonable covenant not to compete.[208] Miller claimed that the provision at issue was overbroad, vague, and unreasonable in scope, duration, and area under the Texas Business and Commerce Code.[209]

The district court stated that "a provision need not 'expressly prohibit' competition" to fall under the statute.[210] A nondisclosure agreement alone is not a covenant not to compete under Texas law, so there must be something else besides a nondisclosure provision to trigger the statute.[211] The test is that the "practical and economic reality" of the provision must inhibit competition in the same manner as a covenant not to compete.[212] The court interpreted the contract provision at issue in the case as similar to a nondisclosure agreement, and therefore it was not subject to the statute.[213] The court noted that the provision "[did] not prohibit Miller from competing with RE/MAX for listings or clients."[214] The court stated that the provision "[sought] to protect RE/MAX's business goodwill from diminution by former agents who might mislead consumers into thinking the agent [was] still affiliated with RE/MAX," and that this did not make the provision a covenant not to compete.[215] Consequently, since the provision was not a covenant not to compete, the court did not need to address the limitations of section 15.50 of the Business and Commerce Code.[216]

RE/MAX therefore provides some clarification as to what types of future employment restrictions may be placed in franchise agreements or franchise employment contracts. The *RE/MAX* contract at issue did not directly prevent Miller from competing with *RE/MAX*; rather, it prevented her from doing so using *RE/MAX*'s trademarks.[217] *RE/MAX* also serves as a reminder that before a Business and Commerce Code "reasonableness" analysis can be performed on a covenant not to compete, the provision at issue must first actually qualify as such a covenant.

B. Petroleum Marketing Practices Act

In *Bellfort Enterprises*, discussed above, the Fifth Circuit held that the PMPA did not entirely preempt plaintiff Bellfort Enterprises' breach of contract, fraud, negligent misrepresentation, and rescission claims against

208. 655 F. Supp. 2d 679, 718 (S.D. Tex. Sept. 3, 2009).
209. *Id.*
210. *Id.*
211. *Id.* at 719.
212. *Id.* at 718-19 (citing Peat Marwick Main & Co. v. Haas, 818 S.W.2d 381, 385 (Tex. 1991)).
213. *Id.* at 719.
214. *Id.*
215. *Id.*
216. *Id.*
217. *Id.*

defendant PetroTex Fuels.[218] Bellfort originally filed suit in state court, claiming that PetroTex failed to follow through on certain financial incentive promises it made prior to entry into the parties' motor fuel supply agreement, and that PetroTex overcharged Bellfort on delivered fuel.[219] PetroTex removed the case based on federal-question jurisdiction, claiming that the PMPA preempted Bellfort's state-law claims.

The Fifth Circuit held that there was no federal-question jurisdiction, because the PMPA did not completely preempt Bellfort's claims.[220] The Fifth Circuit stated that the purpose of the PMPA is "to protect franchisees from arbitrary or discriminatory termination or nonrenewal of their franchise."[221] PetroTex argued that Bellfort's complaint essentially alleged that PetroTex terminated the franchise agreement at issue, pointing in part to Bellfort's requested declaratory judgment that the franchise agreement be terminated.[222] However, the Fifth Circuit concluded that Bellfort intended only to state a breach of contract claim and that Bellfort's requested declaratory judgment was inconsistent with the position that the franchise agreement had already been terminated.[223] Therefore, the Fifth Circuit held that the face of the complaint did not present a federal question.[224]

PetroTex's second argument was that under the "artful pleading doctrine," the PMPA completely preempted Bellfort's state-law claims.[225] However, again, the Fifth Circuit stated that the PMPA's preemption provision "allows states to regulate aspects of the franchise relationship not affecting termination by a franchisor."[226] Since the PMPA did not preempt Bellfort's state-law claims, those claims could be pursued in state court, and the action was not subject to removal.[227]

C. Texas Deceptive Trade Practices—Consumer Protection Act

In *Momentum Marketing Sales & Service, Inc. v. Curves Int'l, Inc.*,[228] a number of fitness-center franchisees sued their franchisor, Curves, and its CEO, Gary Heavin, for fraudulent inducement and concealment, negligent misrepresentation and omission, breach of contract, and alleged violations of the Texas Deceptive Trade Practices–Consumer Protection Act

218. Bellfort Enters., Inc. v. Petrotex Fuels, Inc., 339 F. App'x 416, 419 (5th Cir. 2009); *see supra* Parts III.A, V.A. .
219. *Id.* at 417.
220. *Id.* at 419.
221. *Id.* at 418 (citing Kostantas v. Exxon Co., U.S.A., 663 F.2d 605, 606 (5th Cir. 1981)).
222. *Id.*
223. *Id.*
224. *Id.*
225. *Id.*
226. *Id.* at 419.
227. *Id.*
228. Business Franchise Guide (CCH) ¶ 14,215 (W.D. Tex. Jul. 28, 2009). (Haynes and Boone attorneys Deborah S. Coldwell, Iris Gibson, Altresha Burchett-Williams and Will White serve as counsel for Curves International, Inc., and Gary Heavin).

(DTPA). In an earlier ruling, the district court dismissed twenty-six of the franchisees' thirty-one asserted claims in response to Curves' and Heavin's motion to dismiss.[229] As a result, the sole claim remaining against the CEO was for alleged violations of the DTPA. Heavin moved to dismiss on the basis that the complaint failed to state a claim upon which relief could be granted. Heavin asserted that even if the allegations were true, the franchisees failed to adequately allege that he violated any provision of the Texas "little FTC Act." The franchisees asserted that Heavin waived his right to assert a second motion to dismiss and, even if he did not, that they had adequately alleged a claim under the DTPA.[230]

The district court ultimately held that Heavin could assert his motion to dismiss pursuant to Federal Rule of Civil Procedure 12(b)(6), because such a claim was not subject to the waiver provisions of Rules 12(g) and 12(h).[231] The court then ruled that the franchisees failed to allege that the CEO engaged in any false, misleading, or deceptive acts or practices.[232] In fact, the majority of the franchisees' allegations related to the franchisor, not Heavin. "In the few paragraphs . . . that [were] directed specifically towards Heavin, [the franchisees] essentially allege[d] [he] incentivized his sales team to over-saturate the markets in which the [franchisees] operate[d]."[233] The franchisees also alleged that Heavin "hired friends as sales people, [employed] a friend as his attorney, and coerced his sales team into signing a new commission agreement."[234] The court noted that hiring friends as business associates was clearly not a false, misleading, or deceptive act.[235] The court also noted that "[w]hether or not coercing employees to enter into a new . . . employment contract" was prohibited conduct under the DTPA, none of the CEO's employees were plaintiffs in this action, making that allegation irrelevant.[236] As to the allegation that Heavin "incentivized" his sales team to over-saturate the market, "[t]he establishment of a commission-based payment structure" or "requiring a sales force to perform to a certain level" were "not unconscionable, fraudulent, deceptive, or misleading."[237] If doing so were an actionable claim under the DTPA, "in addition to car dealerships, Realtors and insurance agencies, law firms with minimum billable hour requirements and bonus structures for attorneys who bring in business could not practice in Texas without violating the DTPA." "Because the only specific allegations against Heavin involve[d] his creation of a

229. Business Franchise Guide (CCH) ¶ 14,047 (W.D. Tex. Dec. 17, 2008); see also Deborah S. Coldwell, Altresha Burchett-Williams, Will White & Suzie Loonam, *Franchise Law*, 62 SMU L. REV. 1221, 1223-25 (2009).

230. *Momentum Mktg.*, Business Franchise Guide (CCH) ¶ 14,215.

231. *Id.*

232. *Id.*

233. *Id.*

234. *Id.*

235. *Id.*

236. *Id.*

237. *Id.*

commission-based pay structure for his sales team," plaintiffs' claim against Heavin was dismissed.[238] Finally, the franchisees' general allegation in their complaint that the defendants' actions constituted deceptive and unconscionable acts and practices was merely conclusory and did not sufficiently allege a cause of action against Heavin.[239]

VIII. REMEDIES

A. COMPENSATORY

In *Progressive Child Care Systems, Inc. v. Kids 'R' Kids International, Inc.*, the Fort Worth Court of Appeals affirmed a jury verdict of over $1.3 million in damages in favor of a franchisor.[240] The case centered on a franchise to operate child care facilities in Plano, Texas, and Flower Mound, Texas, under the "Kids 'R' Kids" name.[241] The franchisee was required to pay royalties of 5% of enrollment-based revenues to the franchisor. The Plano franchise agreement became effective in 1995 and the Flower Mound franchise agreement became effective in 1999. Both franchise agreements had twenty-five-year terms.[242]

Progressive stopped making royalty payments in March 2002 and began operating both franchises under the name "Legacy Learning Center" in the spring of 2003.[243] Kids 'R' Kids sued Progressive and its owners for breach of contract, breach of personal guaranty, fraud, and conspiracy. The jury returned a verdict in favor of Kids R' Kids for $1,385,008.72 based on both future and past-due royalties.[244] The court of appeals applied Georgia law pursuant to the franchise agreements, noting that Texas law provides that contractual choice-of-law provisions "will be given effect [as long as] the contract bears a reasonable relationship to the chosen state" and public policy does not demand otherwise.[245] The court of appeals noted that Georgia, like Texas, had not specifically decided whether a franchisee may be liable for past and future royalties after the termination of a franchise agreement.[246] Progressive relied on *Postal Instant Press, Inc. v. Sealy,* a California case wherein the court held that a franchisor could not recover future royalties after the franchisor terminated the franchise agreement.[247] On the other hand, the *Progressive* court cited an unpublished Sixth Circuit opinion, *American Speedy Printing Centers, Inc. v. AM Marketing, Inc.*,which held that a franchisor was

238. *Id.*
239. *Id.*
240. No. 2-07-127-CV, 2008 WL 4831339, at *2 (Tex. App.—Fort Worth Nov. 6, 2008, pet. denied).
241. *Id.* at *1.
242. *Id.*
243. *Id.*
244. *Id.* at *2.
245. *Id.* (citing SAVA gumarska in kemijska industria d.d. v. Advanced Polymer Scis., Inc., 128 S.W.3d 304, 314 (Tex. App.—Dallas 2004, no pet.)).
246. *Id.* at *3.
247. *Id.* (citing Postal Instant Press, Inc. v. Sealy, 43 Cal. App. 4th 1704, 1707-10 (1996)).

entitled to future lost royalties after it had terminated the franchise agreement for failure to pay royalties.[248] Moreover, the *Progressive* court found it significant that in addition to merely not paying royalties, the franchisee in this case independently withdrew from the franchise altogether.[249] The court of appeals concluded by holding that under traditional Georgia contract law, lost profits may be recovered as damages under the principle that the injured party should be placed in the position it would have occupied absent the breach.[250] In conclusion, the *Progressive* court held that the award of lost future royalties was adequately supported by Kids 'R' Kids' designated forensic accountant, who calculated the amount based on the past performance of the two franchises projected throughout the remainder of their terms and discounted for present value.[251]

Although *Progressive* applies Georgia law, the case is significant in that it demonstrates how a court may analyze the law on whether lost future royalties are available to a franchisor. The court of appeals in *Progressive* ultimately distinguished the *Sealy* case, decided by a California court, and relied on traditional contract damages, which generally can include lost profits.[252] This analysis may prove instructive in other Texas courts tackling the lost future royalties question.

Although not a franchisee–franchisor dispute, *U.S. Bank v. American Realty Trust, Inc.* is significant in the area of franchise financing.[253] The dispute in *U.S. Bank* was between a former Holiday Inn franchisee and its primary lender, which held a note secured by the real and personal property of a former Holiday Inn hotel near the Kansas City airport.[254] When the franchise term for the Holiday Inn was coming close to the end, the franchisor required certain improvements to be made to the property in order for the license to be renewed. An estimate revealed the cost of these improvements to be approximately $1.8 million.[255] Although the parties disputed who made the decision, the Holiday Inn license was not renewed, and the hotel was converted to a Clarion hotel at a lesser cost. Occupancy and revenue subsequently declined, and the hotel was foreclosed.[256]

The loan from the lender was guaranteed by the franchisee. The guarantee included a provision making the franchisee personally liable for "waste" committed on the property.[257] The lender argued that waste occurred as a result of the failure of the franchisee to relicense the hotel as a

248. *Id.* (citing Am. Speedy Printing Ctrs., Inc. v. AM Mktg., Inc., 69 Fed. App'x 692, 699 (6th Cir. 2003)).
249. *Id.* at *4.
250. *Id.*
251. *Id.* at *6.
252. *Id.* at *4.
253. 275 S.W.3d 647 (Tex. App.—Dallas 2009, pet. denied).
254. *Id.* at 648-49.
255. *Id.* at 649.
256. *Id.*
257. *Id.*

Holiday Inn.[258] The lender sought damages representing the difference in appraisal value of the hotel under the cheaper Clarion brand in foreclosure versus the value it would have had as a Holiday Inn, an amount equal to about $3.85 million.[259] The parties' primary argument was whether "waste" in the loan documents could encompass intangible harm to a license.

The Dallas Court of Appeals ultimately did not reach this issue, however. It found that the language requiring the franchisee to "conduct and operate its business as presently conducted and operated" meant only that the property had to continue as a hotel, not specifically as a Holiday Inn.[260] The court of appeals held that even if the franchisee made fraudulent misrepresentations to the lender in connection with the decision not to renew the Holiday Inn license, "the misrepresentations could not have caused . . . damages for something [the franchisee] was not required to do."[261] *U.S. Bank* therefore teaches an important lesson for franchise financing. If a particular brand is a valuable part of the collateral, a prospective lender should be very careful in how the brand of the franchise is addressed in the loan documentation.

B. Injunctive Relief

The Western District of Texas was faced with dueling applications for preliminary injunctions in *Petro Franchise Systems, LLC v. All American Properties, Inc.*, discussed above.[262] The fuel station franchisee complained when the franchisor was acquired by a company that operated competing travel plazas within the franchisee's exclusive franchise area.[263] This dispute, and the franchisees' non-payment of royalties, led to an initial settlement agreement between the parties involving a release of claims existing as of the date of the settlement agreement and a cash payment to the franchisor to cure monetary defaults under the franchise agreements.[264] After the initial settlement agreement, the franchisee continued to fail to make royalty payments. The franchisor terminated the franchises and sought a preliminary injunction under the Lanham Act to prevent the franchisees from using the franchisor's trademarks.[265] The franchisee counterclaimed for breach of the franchise agreement by the franchisor and for breach of the duty of good faith and fair dealing, and sought a preliminary injunction to prevent the franchisor from taking any action to terminate the franchise agreements.[266]

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258. *Id.*
259. *Id.*
260. *Id.* at 651. In addition, nothing in the loan documents specifically required the franchisee to reapply for the Holiday Inn license. *Id.*
261. *Id.* at 654.
262. 607 F. Supp. 2d 781 (W.D. Tex. Mar. 23, 2009); *see supra* Part IV.A.
263. *Id.* at 785.
264. *Id.* at 786.
265. *Id.*
266. *Id.* at 787.

The district court analyzed the four traditional factors in a preliminary injunction analysis: (1) likelihood of success on the merits, (2) the presence of irreparable harm, (3) whether the threatened injury outweighed any damage from the injunction, and (4) the public interest.[267] The first significant holding of the *Petro* case illustrates a classic contract-law analysis of franchise royalty payments. The court noted that the franchisee was using the franchisor's exact trademarks and that there was no dispute that the franchisee had failed to make required royalty payments.[268] The court noted that the franchisor followed the termination procedure under the applicable franchise agreements "to the letter."[269] The franchisee argued that the franchisor did not properly terminate the franchise agreement because of its actions in allowing competing facilities to operate within its exclusive area.[270] By properly following the termination procedure after the franchisee stopped paying royalties, the franchisor established a likelihood of success on the merits.[271] *Petro*, therefore, reinforces that franchisees should take any decision to stop paying royalties very seriously.

The second significant holding of *Petro* demonstrates the difficulty of establishing irreparable harm. The district court found that, under established trademark law, the franchisor would suffer irreparable harm if the franchisee were allowed to continue using the franchisor's trademarks without authorization.[272] Conversely, the court found that the loss of the franchisee's franchise would not necessarily be irreparable harm.[273] The court cited as significant the fact that the franchisees, as part of the earlier settlement, reneged on the opportunity to convert another one of their facilities to the Petro brand.[274] Further, the franchisees ran multiple other facilities outside the Petro brand.[275] Furthermore, the court stated that even if the loss of the franchise meant that the franchisee would be out of business, such loss may indeed be calculable and remedied by monetary damages.[276] *Petro* consequently reinforces the advantages an intellectual property claim has versus other types of claims in an irreparable harm analysis, in that the unauthorized use of intellectual property can easily qualify as irreparable harm, while in certain circumstances even the loss of a business may be deemed compensable by monetary damages.

Finally, the franchisee argued that the franchisor had unclean hands as a result of the acquisition which put competing facilities in the franchisees' area under the franchisor's control.[277] In order for an unclean hands

267. *Id.* (citing Nichols v. Alcatel USA, Inc., 532 F.3d 364, 372 (5th Cir. 2008)).
268. *Id.* at 788-89.
269. *Id.* at 790.
270. *Id.* at 791.
271. *Id.* at 792.
272. *Id.* at 793-94.
273. *Id.* at 796.
274. *Id.*
275. *Id.*
276. *Id.*
277. *Id.* at 798-99.

argument to be successful, however, there must be a connection between the allegedly unclean conduct and the injunction.[278] In this case, the franchisees failed to show how their failure to pay royalties was connected to the unclean conduct.[279] The district court stated that the franchisees did not present enough evidence to prove that the competition from the competing facilities impacted their ability to pay royalties.[280] The unclean-hands holding reinforces the potential negative consequences of the failure to pay royalties. In conclusion, the court held that all of the relevant factors favored the franchisor, and granted the franchisor a preliminary injunction.[281]

IX. CONCLUSION

As noted in the introduction, if there was a general theme among the significant cases in franchise law this year, it was the reaffirmation of the importance of the contractual nature of the relationship between franchisees and franchisors. The importance of the contract was even reaffirmed in the procedural context, specifically in *TGI Friday's Inc. v Great Northwestern Restaurants, Inc.*[282] The *TGI Friday's* court held that the forum selection clause in the franchise agreement was broad enough to encompass the plaintiff's intellectual property claims, and the court mentioned the personal-jurisdiction waiver in the franchise agreement as a factor in holding that personal jurisdiction was proper in Texas as to an out-of-state franchisee.[283] The holding in *Davaco, Inc. v. Dunkin' Brands, Inc.* tempers this result slightly and reminds us that, at least when it comes to jurisdiction, contracts alone are not enough.[284]

In the intellectual property area, in *Petro Franchise Systems, LLC v. All American Properties, Inc.*, the franchisor's intellectual property claims depended on whether the franchisor had properly terminated the franchise under the terms of the franchise agreement.[285] Since the district court determined that the payment requirements and the franchise termination procedure were unambiguous and properly followed by the franchisor, the franchisor was held likely to prevail on its unauthorized use of intellectual property claims.[286] In fact, both *Petro* and *Friday's* reaffirm the basic contract principle that if a defendant believes the other party to the contract is in breach, it may continue to perform and sue for partial breach, or cease performing and treat the contract as terminated.[287] A

278. *Id.* at 799.
279. *Id.* at 800.
280. *Id.*
281. *Id.* at 801.
282. *Id.* at 757-58, 760.
283. 652 F. Supp. 2d 750 (N.D. Tex. Aug. 20, 2009).
284. No. 3:08-cv-0581-m, 2008 WL 4975880, at *3 (N.D. Tex. Nov. 21, 2008) (stating that a Texas choice-of-law provision does not establish jurisdiction absent the existence of traditional minimum contacts).
285. 607 F. Supp. 2d 781, 788-90 (W.D. Tex. Mar. 23, 2009).
286. *Id.* at 790-92.
287. *Id.* at 791; *TGI Friday's*, 652 F. Supp. 2d at 769-70.

franchisee may not cease paying royalties while continuing to receive the benefits of the franchisor's intellectual property.[288]

In addition to the above, other cases this year demonstrate the importance of the contract in franchise-related disputes. In *RE/MAX International, Inc. v. Trendsetter Realty, LLC*, the district court held that a nondisclosure agreement is not a covenant not to compete and is therefore not subject to the Business and Commerce Code's restrictions on such covenants.[289] *U.S. Bank v. American Realty Trust, Inc.* shows that even franchise financing documents should be carefully scrutinized during drafting to account for potential future contingencies. In that case, the court of appeals held that loan documents providing merely that a hotel property must be conducted and operated as presently done was not sufficient to guarantee that the property would have to remain a Holiday Inn.[290] Instead, the language permitted the franchisee operator to shift to another brand that allegedly damaged the bank's collateral.

In summary, a theme of this year's franchise and dealership law is attention to the plain meaning of contracts. The cases discussed above have shown how important a topic this is in areas ranging from procedural steps to substantive law issues and even in the transactional/financing stage. Careful planning and forethought in the drafting and negotiation phases is essential for both franchisors and franchisees and can have an important impact on the outcome of any future disputes in which they become involved.

288. *Petro*, 607 F. Supp. 2d at 790-92.
289. 655 F. Supp. 2d 679, 718-19 (S.D. Tex. Sept. 3, 2009).
290. 275 S.W.3d 647, 651 (Tex. App.—Dallas 2009, pet. denied).