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FRANCHISE LAW

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I. INTRODUCTION

THIS article provides an update of case law during the Survey period that has had, or may have, an impact on franchises and dealerships in Texas. In reviewing the opinions from Texas courts and federal courts in the Fifth Circuit that dealt with franchise and dealership

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issues, however, 2010 was not a year of significant decisions. Nonetheless, it was a period during which courts continued to refine and answer questions about jurisdictional issues, enforce the plain meaning of agreements between the parties—including forum selection and arbitration clauses—and advise parties under what circumstances courts would dismiss or uphold antitrust and trademark claims.

II. FRANCHISE BASICS

There were no significant developments in basic franchise, business opportunity, or dealership laws in Texas or the Fifth Circuit during the Survey period. It has been a few years since the Federal Trade Commission (“FTC”) issued the revised Federal Franchise Rule (“the Rule”) and there have yet to be major developments since the Rule was issued.

III. PROCEDURE

A. JURISDICTION

“[I]nexact compliance is no compliance.”¹ During the Survey period, the Fifth Circuit reminded us that jurisdiction is a “strict master.”² In *SmallBizPros, Inc. v. MacDonald*, the Fifth Circuit re-examined the immediate effect of Federal Rule of Civil Procedure 41(a)(1)(A)(ii), holding that unless the order’s language provides otherwise, a stipulation of dismissal under Rule 41 will be effective upon filing, notwithstanding any other action by the district court.³ In *SmallBizPros v. MacDonald*, SmallBizPros (which does business as Padgett Business Services) filed suit against Frank MacDonald in district court in the Western District of Texas.⁴ The suit arose from the termination of a franchise agreement.⁵ Following the initial complaint, Padgett and MacDonald settled their dispute, announced the settlement to the district court, and filed a stipulation of dismissal pursuant to Rule 41.⁶ The stipulation attached a stipulated settlement order (the Order), which the district court signed a week after the parties filed the stipulation.⁷

MacDonald refused to comply with certain terms of the settlement agreement, and the district court issued a contempt order a little over a month after signing the Order.⁸ The district court stated that it retained jurisdiction to enforce the settlement agreement by signing the Order, thus retaining the jurisdiction to issue the contempt order.⁹ MacDonald appealed. MacDonald asserted that the district court did not retain juris-

1. *SmallBizPros, Inc. v. MacDonald*, 618 F.3d 458, 464 (5th Cir. 2010).

2. *Id.*

3. *Id.* at 462.

4. *Id.* at 460.

5. *Id.*

6. *Id.*

7. *Id.*

8. *Id.*

9. *Id.*

diction to issue the contempt order because the court's jurisdiction ceased with the filing of the stipulation.¹⁰

The Fifth Circuit agreed. The Fifth Circuit highlighted that “[e]xcept in special circumstances . . . a voluntary order of dismissal requested by both parties is *effective upon filing* and does not require the approval of the court.”¹¹ The court noted that unless the parties provide for an express contingency or an express extension of jurisdiction, the district court's jurisdiction will not extend past the filing of the stipulation.¹² In support of its holding, the Fifth Circuit reviewed the Supreme Court's decision in *Kokkonen v. Guardian Life Insurance Co. of America*.¹³ In *Kokkonen*, the Supreme Court analyzed a district court's ancillary jurisdiction under Rule 41 and held:

[P]ursuant to Federal Rule of Civil Procedure 41(a)(1)(ii), the parties executed a Stipulation and Order of Dismissal with Prejudice, dismissing the complaint and cross-complaint . . . [T]he District Judge signed the Stipulation and Order under the notation “It is so ordered.” The Stipulation and Order did not reserve jurisdiction in the District Court to enforce the settlement agreement; indeed it did not so much as refer to the settlement agreement.¹⁴

The Supreme Court in *Kokkonen* unanimously held that the district court did not retain jurisdiction to issue any enforcement order.¹⁵

The Fifth Circuit, nevertheless, did suggest ways in which the district court could have retained jurisdiction to enforce the terms of the settlement agreement.¹⁶ The parties could have required compliance with the terms of the settlement agreement as part of the dismissal order, could have incorporated such terms in the dismissal order,¹⁷ or, the dismissal order could have expressly stated that the court retained jurisdiction over the settlement agreement.¹⁸

In any of the scenarios, however, the parties must agree that the district court retain ancillary jurisdiction. Here, the stipulation did not contain such language. Although the stipulation did include language requesting the district court to sign the order, the Fifth Circuit held that the stipulation's effectiveness was not “expressly contingent” upon the entry of the order.¹⁹ Therefore, the Fifth Circuit held that the order was “superfluous;” it did not contain any agreed upon language for the district court to retain jurisdiction.²⁰ The Fifth Circuit held that the district court lacked

10. *Id.*

11. *Id.* at 461 (citing *Ramming v. Natural Gas Pipeline Co. of Am.*, 390 F.3d 366, 369 n.1 (5th Cir. 2004) (emphasis added)).

12. *Id.*

13. 511 U.S. 375, 377 (1994).

14. *Id.* at 376–77.

15. *Id.* at 381–82.

16. *SmallBizPros*, 618 F.3d at 462–63.

17. *Id.*

18. *Id.* at 462.

19. *Id.* at 463.

20. *Id.*

jurisdiction to issue any contempt order because the district court did not retain jurisdiction over the settlement agreement.²¹

These reminders by the court are excellent practice pointers for litigators. To ensure that a court maintains jurisdiction simply requires inclusion of settlement agreement compliance language as part of the order of dismissal, incorporation of the settlement terms into the dismissal order, or a clear statement that the court will retain jurisdiction in the dismissal order. Doing none of these things will ensure that the court does not retain jurisdiction, which ultimately occurred in *SmallBizPros*.

In franchise litigation, federal jurisdiction may often be established through Lanham Act claims. Franchisors and franchisees are commonly in dispute regarding use of the franchisor's trademarks, trade dress, logos, and other proprietary and confidential information, particularly after the expiration or termination of a franchise agreement. What is not as common is a declaratory judgment action between a franchisor and an exclusive distributor for which federal jurisdiction is established when the initial use of the trademark arose from a contract. In *Go Figure, Inc. v. Curves International, Inc.*,²² the district court addressed whether it had subject matter jurisdiction where an exclusive distributor sought a declaration of the right to use Curves' trademark to sell key tags.

Go Figure, Inc. developed and sold club management software to Curves' franchisees.²³ The software used key-tags with Curves' logo engraved on each key-tag. Curves and Go Figure executed a contract, whereby Curves granted Go Figure the right to be the exclusive provider of this software (with an incidental intellectual property right to use Curves' logo). The contract terminated in May 2009. Go Figure, however, continued to sell the software with the engraved key tags to Curves' franchisees following termination. Curves alleged that Go Figure no longer had authorization to use the key-tags with Curves' logo after termination.²⁴

Go Figure filed a declaratory judgment action seeking a declaration that it had the right to continue to sell the key tags with Curves' logo, notwithstanding termination of the contract. Curves filed a motion to dismiss asserting that the district court lacked subject matter jurisdiction. Curves contended that Go Figure's claim was simply based on a breach of contract theory. Conversely, Go Figure argued that any suit against it would be based on trademark infringement under the Lanham Act—a federal question. The district court agreed with Go Figure.²⁵

The district court explained that although the Declaratory Judgment Act ("Act") authorizes certain remedies, jurisdiction cannot be based on

21. *Id.*

22. No. H-09-2930, 2010 WL 142441, at *1 (S.D. Tex. Apr. 8, 2010) (Haynes and Boone attorneys Michael Powell, Yasser A. Madriz and Mike P. Raab represent Curves in this matter.).

23. *Id.*

24. *Id.*

25. *Id.*

this Act.²⁶ “[T]o award relief under the Declaratory Judgment Act, courts must have an independent basis for jurisdiction.”²⁷ Go Figure had the burden to show that there would be jurisdiction over any claim by Curves against Go Figure.²⁸ Go Figure met its burden.²⁹ Go Figure acknowledged that the contract did not expressly grant Go Figure any right to use Curves’ trademark. Therefore, any issue regarding the improper use of Curves’ trademark, particularly following termination of the contract, would be based on a claim for trademark infringement. Although the district court held that Go Figure established federal question jurisdiction and denied Curves’ Rule 12(b)(1) motion, Go Figure’s concession that the contract did not permit—implicitly or otherwise—its use of Curves’ trademark was an interesting position to take. Go Figure survived Curves’ jurisdictional challenge, but survival of the substantive claims may be more difficult.³⁰

During the Survey period, the Dallas appellate court outlined the separateness of franchisors and franchisees, such that jurisdiction cannot be established based on “necessary forms of franchise operations [that] are common between franchisors and franchisees.”³¹ In *Tampa Bay Towing v. Moyer*, a franchisee’s employee sued the Florida franchisee and its franchisor in Texas under a corporate veil-piercing theory.³² The employee’s injury occurred in Florida. The employee, however, alleged that Texas had jurisdiction over both the franchisee, Tampa Bay, and its franchisor, Sea Tow International, because Sea Tow controlled Tampa Bay’s boat types, insurance carrier, corporate software, logo, marketing materials, e-mail capability, and membership directory, among other things.³³ Tampa Bay argued that it was a separate business entity that maintained separate officers, directors, financials, and day-to-day operations.³⁴ The trial court denied Tampa Bay’s special appearance and Tampa Bay appealed.

The trial court discussed the standards for jurisdiction—general and specific. The trial court further discussed the standard for personal jurisdiction under a corporate veil-piercing theory in particular. Unlike the traditional burden whereby the nonresident defendant must negate all bases of jurisdiction, the plaintiff must prove jurisdiction over the defendant if jurisdiction is based on a theory of piercing the corporate veil.³⁵ Therefore, Moyer had the burden to prove that Tampa Bay and Sea Tow

26. *Id.* at *3.

27. *Id.*

28. *Id.* at *2.

29. *Id.* at *4.

30. *Id.*

31. *Tampa Bay Marine Towing & Serv., Inc. v. Moyer*, No. 05-08-01727-CV, 2009 WL 3956450, at *4 (Tex. App.—Dallas Nov. 20, 2009, no pet.) (mem. op.).

32. *Id.* at *1.

33. *Id.* at *1–2.

34. *Id.* at *4.

35. *Id.* at *2 (citing *BMC Software Belgium, N.V. v. Marchand*, 83 S.W.3d 789, 798–99 (Tex. 2002); *Wolf v. Summers-Wood, L.P.*, 214 S.W.3d 783, 787 (Tex. App.—Dallas 2007, no pet.)).

operated as a single business enterprise and should be “jurisdictionally fused.”³⁶ The appellate court held that Moyer failed to meet this burden.³⁷

The appellate court acknowledged that Sea Tow retained control over many of Tampa Bay’s operations, including logos, vehicles, methods of operations, and marketing. Nevertheless, the appellate court held that “[r]etention of such control as well as the right to veto proposed structural changes is not sufficient to support a determination that a franchisor ‘operates’ the franchisee or its premises.”³⁸ The court briefly noted that the degree of control was not so great that the separateness of Tampa Bay and Sea Tow should be disregarded to prevent fraud or injustice. Here, Moyer had knowledge that Tampa Bay was a franchisee. The injury took place in Florida. Tampa Bay had no sufficient contacts with Texas and did not do business in Texas. A franchisor may exercise control (even substantial control to protect its brand) without subjecting its nonresident franchisees to jurisdiction in Texas.³⁹

Evaluating the control that a parent corporation/franchisor has over its subsidiary/franchisee is one method used to “fuse” two corporations for jurisdictional purposes. Another approach is to analyze the parent’s contacts with Texas directly. In *Spir Star AG v. Kimich*, the Texas Supreme Court held that “a manufacturer is subject to specific personal jurisdiction in Texas when it intentionally targets Texas as a marketplace for its products, and that using a distributor-intermediary for that purpose provides no haven from the jurisdiction of a Texas court.”⁴⁰

Spir Star AG (“AG”) was a German manufacturer of hoses.⁴¹ A few of AG’s executives established Spir Star Limited (Limited), a Texas distributorship. AG specifically elected Texas as its distribution location based on Texas’s refineries and AG’s energy-related products. Limited purchased hoses from AG and sold those same hoses to various companies, including Louis Kimich’s employer. When an AG-manufactured hose injured Kimich, Kimich sued his employer, AG, and Limited. AG filed a special appearance challenging personal jurisdiction over it in Texas. AG argued that it structured its transactions to avoid jurisdiction with the forum state. In support of its argument, AG showed that it and Limited did not share profits or finances. The two companies were separate entities; AG argued that it did not have control over Limited’s business operations and affairs such that jurisdiction over Limited would “fuse” to jurisdiction over AG.⁴²

36. *Id.* at *1.

37. *Id.* at *4–5.

38. *Id.* at *4 (citing *Alonzo v. Mr. Gatti’s Pizza, Inc.*, 933 S.W.2d 294, 296 (Tex. App.—Corpus Christi 1996, no writ)).

39. *Id.*

40. 310 S.W.3d 868, 871 (Tex. 2010).

41. *Id.*

42. *Id.*

The Texas Supreme Court, however, did not focus on the theory of piercing the corporate veil. The supreme court directed its attention to AG's own conduct and marketing in Texas. The supreme court recognized that more is needed to establish personal jurisdiction than a seller simply placing its product into the stream of commerce.⁴³ Here, AG did more; AG satisfied the "additional conduct" standard.⁴⁴ The supreme court explained that because AG specifically targeted Texas as a market for its hoses, AG subjected itself to a product liability suit in Texas, even if the actual sale of the product occurred through a Texas distributor. AG intended to profit from the Texas economy, from which AG received 35% of its annual sales.⁴⁵

A plaintiff has a heightened burden to prove specific jurisdiction over a nonresident defendant when the sale occurred through an intermediary. Kimich had to show a "substantial connection" between AG and the facts underlying the litigation.⁴⁶ "A nonresident manufacturer does not avoid Texas law merely by forming a Texas affiliate or utilizing a Texas distributor to sell its products in Texas markets."⁴⁷ The supreme court concluded that because AG and Limited agreed to be a Texas sales agent, AG's marketing efforts directed toward Texas established jurisdiction.⁴⁸ The supreme court also did not forgo ensuring the basic standard we learned from *International Shoe*:⁴⁹ exercising personal jurisdiction over AG did not offend traditional notions of fair play and substantial justice.⁵⁰

B. FORUM SELECTION

Forum selection clause issues arise when a dispute involves multiple parties to an agreement or multiple documents to a single agreement. A franchise or distribution agreement may contain exhibits or attachments, and there may be an issue of whether a forum selection clause contained in one of the attached documents will apply to the underlying dispute. During the Survey period, the Texas Supreme Court and a Dallas appellate court upheld enforcement of forum selection clauses involving both multiple parties and multiple documents.

In *Lisa Laser USA, Inc.*, the supreme court addressed the enforceability of a forum selection clause that was contained in an exhibit to a distribution agreement, which was signed by all parties.⁵¹ The exhibit specifically referenced only one of the two defendants, however.⁵² Lisa Germany manufactured medical lasers, and Lisa USA was the distributor

43. *Id.* at 874.

44. *Id.*

45. *Id.*

46. *Id.*

47. *Id.* at 875.

48. *Id.* at 880.

49. *Int'l Shoe Co. v. Washington*, 326 U.S. 310, 316 (1945).

50. *Spir Star AG*, 310 S.W.3d at 878-79.

51. *In re Lisa Laser USA, Inc.*, 310 S.W.3d 880, 881 (Tex. 2010).

52. *Id.* at 881-82.

of those products in the United States. Lisa Germany, Lisa USA, and HealthTronics, Inc. signed a distribution agreement in 2007 whereby HealthTronics became the exclusive distributor for certain Lisa Laser medical devices. The distribution agreement attached eight exhibits, including a “Standard Terms and Conditions” exhibit. The terms and conditions applied to sales by Lisa USA to HealthTronics and designated California as the venue for any disputes arising out of the distribution agreement. About a year after entering into the distribution agreement, HealthTronics filed suit against Lisa Germany and Lisa USA alleging violations of the right of first refusal and breach of the confidentiality and non-solicitation agreements. HealthTronics filed its suit in Texas where HealthTronics’s headquarters were located. Lisa Germany and Lisa USA filed a motion to dismiss based on improper venue, but the trial and appellate courts denied the motion. The defendants filed a mandamus petition to the Texas Supreme Court.⁵³

HealthTronics made two principal arguments against enforcement of the forum selection clause. First, HealthTronics argued that the clause did not apply to its claims because the clause was limited to claims specifically related to sales by Lisa USA (which was stated in the preamble preceding the venue provision). Second, HealthTronics argued that the clause did not apply to its claims against Lisa Germany because Lisa Germany, although a party to the distribution agreement, was omitted from the terms of the exhibit containing the forum selection clause. The supreme court rejected both these arguments.⁵⁴

The supreme court held that the standard terms and conditions were not separate from the main document of the distribution agreement.⁵⁵ The supreme court observed that the distribution agreement required and incorporated the additional terms set forth in the exhibits, including the standard terms and conditions, to “fully elucidate the parties’ agreement.”⁵⁶ The supreme court analyzed the parties’ intent when entering into the distribution agreement with several exhibits attached. “The Distribution Agreement and the Exhibits were intended to be one document.”⁵⁷ Because the forum selection clause contained broad language intended to cover “*any* dispute,” the clause was not limited to only disputes from sales transactions.⁵⁸

The supreme court also rejected HealthTronics’ argument that sought to disallow Lisa Germany’s reliance on the clause.⁵⁹ Lisa Germany was not a party to a prior agreement between Lisa USA and HealthTronics. Also, Lisa Germany was not referenced in the exhibit containing the standard terms and conditions. HealthTronics, therefore, argued that the

53. *Id.*

54. *Id.*

55. *Id.* at 885.

56. *Id.*

57. *Id.*

58. *Id.*

59. *Id.* at 886–87.

forum selection clause was not intended to apply to disputes involving Lisa Germany. The supreme court expressly stated, “[a] plaintiff cannot both have his contract and defeat it too.”⁶⁰ The supreme court concluded that the standard terms and conditions were the default terms applicable to the distribution agreement in general.⁶¹ HealthTronics’s claims against Lisa Germany arose from Lisa Germany’s purported obligations under the distribution agreement. Therefore, the parties intended that the forum selection clause apply to all claims between all parties to the agreement.⁶² The supreme court directed the trial court to vacate its order and grant the motion to dismiss.⁶³

Similarly, in *Dunlap Enterprises v. Roly Poly Franchise Systems, L.L.C.*, several franchisees sought to hold a forum selection clause unenforceable because “requiring them to litigate their claims in the selected forum [Georgia] would be unreasonable and would effectively deprive them of their day in court.”⁶⁴ The franchisees conceded that the forum selection clause applied to their claims against the franchisor, Roly Poly. The franchisees argued that the suit should remain in Texas, however, because their claims were also asserted against Roly Poly’s master developer, Summers-Wood, who they argued was not subject to jurisdiction in Georgia. The franchisees’ argument was based on a prior federal lawsuit between Roly Poly and Summers-Wood in which a district court held that the forum selection clause found in the franchise agreement (i.e., an exhibit to the master development agreement) was not incorporated into the master development agreement. Based on that ruling, the Georgia district court held that Georgia lacked personal jurisdiction over Summers-Wood. The franchisees asserted that because Georgia did not have jurisdiction over all necessary parties, enforcement of the forum selection clauses in the franchise agreement would be “unreasonable and unjust.”⁶⁵ First, the trial court, and later, the appellate court, disagreed.⁶⁶

The court of appeals noted that the franchisees were not parties to the prior federal action in Georgia. The franchisees thus failed to show that *res judicata* would apply since they would not be bound by the prior ruling of the Georgia district court. Moreover, a different agreement was at issue in the present suit—the franchise agreement, not the master development agreement. Although Summers-Wood was not a party or signatory to the franchise agreement, Summers-Wood could be a “transactional participant” and thus subject to the forum selection

60. *Id.* at 886 (citing *In re Weekley Homes, L.P.*, 180 S.W.3d 127, 135 (Tex. 2005) (internal quotation marks omitted)).

61. *Id.*

62. *Id.* at 887.

63. *Id.*

64. No. 05-08-01556-CV, 2010 Tex. App. LEXIS 5832, at *1 (Tex. App.—Dallas July 23, 2010, no pet.) (Haynes and Boone attorneys Deborah S. Coldwell, Ben Mesches, and Altresha Burchett-Williams represented Roly Poly in this action.).

65. *Id.* at *3.

66. *Id.* at *8.

clauses.⁶⁷ The franchisees' argument that Summers-Wood would not be subject to jurisdiction was "mere speculation."⁶⁸ Despite arguments of difficulty, expense, and potential for the "empty-chair" defense cited by the franchisees, the appellate court concluded that the trial court acted reasonably in upholding the forum selection clauses.⁶⁹

Although not technically an issue that arises pursuant to a contractual forum selection clause, the "first-to-file" rule is important to note when a forum battle takes place. In *Buffalo Wild Wings, Inc. v. BWR McAllen, Inc.*, franchisor Buffalo Wild Wings (BWW) sued three franchisees of Minnesota franchisor Buffalo Wings & Rings (BWR) in a Texas district court.⁷⁰ BWW alleged that the franchisees committed trademark and trade dress violations and had engaged in unfair competition. A year prior, BWW sued BWR in a Minnesota district court asserting the same claims for relief. In *BWR McAllen*, the franchisees sought to stay the Texas action based on the "first-filed rule."⁷¹

The district court followed the Fifth Circuit's rule when deciding whether to maintain jurisdiction: "Under the first-to-file rule, when related cases are pending before two federal courts, the court in which the case was last filed may refuse to hear it if the issues raised by the cases substantially overlap."⁷² The district court emphasized that the issues do not need to be identical; the standard is that the issues only need to "substantially overlap." The district court held that BWW's factual issues against BWR as a franchisor were different from BWW's issues with BWR's franchisees. The franchisees use their own advertisements, wear different uniforms, and generally adopt individual practices.⁷³ Therefore, the Texas district court denied the franchisees' motion to stay, also noting that the Minnesota court's lack of jurisdiction over the franchisees further supported the Texas court maintaining jurisdiction.⁷⁴

C. ARBITRATION

Timeliness is important when seeking to enforce arbitration. In *Cottman Transmission v. FVLR*,⁷⁵ a landlord (FVLR) sued a franchisor (Cottman) based on the franchisor's alleged assumption of its franchisee's lease obligation after termination of the franchise agreement. The suit went to trial, and the jury returned a verdict in FVLR's favor and held

67. *Id.* at *7 (citing *Accelerated Christian Educ., Inc. v. Oracle Corp.*, 925 S.W.2d 66, 75 (Tex. App.—Dallas 1996, no writ) ("A valid forum selection clause governs all transaction participants, regardless of whether the participants were actual signatories to the contract.")).

68. *Id.* at *8.

69. *Id.*

70. No. H-10-1265, 2010 U.S. Dist. LEXIS 65051, at *2-3. (S.D. Tex. June 30, 2010).

71. *Id.*

72. *Id.* at *4.

73. *Id.* at *6.

74. *Id.* at *6-7.

75. *Cottman Transmission Sys., L.L.C. v. FVLR Enters, L.L.C.*, 295 S.W.3d 372, 375 (Tex. App.—Dallas 2009, pet. denied).

against Cottman on its counterclaim. Cottman appealed on ten issues, including a request for post-verdict arbitration. Cottman asserted that if it was bound by the lease at issue, it was entitled to resolve its dispute with FVLR through arbitration. The appellate court ruled that Cottman was too late.⁷⁶ “A party waives arbitration if it takes an action inconsistent with its right to arbitration, that is prejudicial to the other party.”⁷⁷ This appeared to be a simple issue for the court of appeals. A trial and jury verdict was considered inconsistent with Cottman’s right to arbitration. The appellate court, therefore, held that Cottman waived its right to arbitration.⁷⁸

In *U-Save v. Furlo*,⁷⁹ the Fifth Circuit summarized a few basic principals involving arbitration clauses. The franchise agreement between U-Save and the Furlos contained an arbitration clause. Pursuant to motions by U-Save, the district court compelled arbitration and later confirmed the arbitrator’s award.⁸⁰ The Fifth Circuit did not provide many background facts or the procedural history that had taken place between the parties. Nevertheless, the Fifth Circuit affirmed several basic principals. First, it is important to remember that an appellate court has limited judicial review of arbitration awards under the Federal Arbitration Act (“FAA”).⁸¹ The bases for review are limited. Second, an arbitration clause will not be void for public policy when access to a reasonable substitute is provided for causes of action denied based on a choice-of-law provision.⁸² Third, an award of zero damages will not strip the district court of jurisdiction when the amount in controversy exceeds \$75,000; the district court can retain jurisdiction to address issues arising from its order to compel arbitration.⁸³ Lastly, when an arbitration agreement is controlled by the FAA, a state’s common law doctrine for enforceability is negligible.⁸⁴

Pillar to Post, Inc. v. Weible emphasizes the court’s limited judicial review of arbitration awards.⁸⁵ “A court’s review of an arbitration award is ‘exceedingly deferential,’ and any doubt or uncertainty is resolved in favor of upholding the award.”⁸⁶ In *Pillar to Post*, a franchisor sought to confirm an arbitration award against its franchisees, restraining the franchisees from using its trademarks without authorization, from violating the covenant not to compete, and from divulging confidential or other proprietary information. The arbitration award also granted monetary relief to the franchisor. In addition to the arbitration award, the

76. *Id.* at 380.

77. *Id.*

78. *Id.*

79. *U-Save Auto Rental of Am. Inc. v. Furlo*, 368 Fed. Appx. 601, 601 (5th Cir. 2010).

80. *Id.* at 602.

81. *Id.*

82. *Id.*

83. *Id.*

84. *Id.*

85. No. H-09-3227, 2010 U.S. Dist. LEXIS 64551, *1 (S.D. Tex. June 29, 2010).

86. *Id.* at *4.

franchisor sought to enforce the prevailing party's attorneys' fee provision in the franchise agreement. The district court agreed.⁸⁷ The district court, however, "encouraged" the parties to agree on the amount of attorneys' fees and expenses that would be awarded to the franchisor.⁸⁸ Because the franchisees did not provide any evidence or authority to overcome the deference given to the arbitrator's award, the district court granted the motion to confirm.⁸⁹

The Fifth Circuit revisited the "direct benefits estoppel" doctrine in a distribution dispute. In *Noble Drilling Services, Inc. v. Certex USA, Inc.*, Noble, (a purchaser of wire mooring rope) sued Bridon (the manufacturer) and Certex (the distributor) based on breach of warranty and fraud claims.⁹⁰ Noble entered into a sales contract with Certex to purchase ropes that met the specifications Noble required. Certex, who had a distribution agreement with Bridon, entered into purchase order agreements for the specified ropes. Certex and Bridon were the only parties to the distribution agreement and subsequent purchase order agreements. The distribution agreement and purchase order agreements each contained an arbitration clause. When Noble sued Certex and Bridon in district court, both defendants moved to compel arbitration on the theory that Noble was bound under the "direct benefits estoppel" rule. Although the district court dismissed the action, the Fifth Circuit disagreed and reversed the district court's dismissal.⁹¹

"Direct-benefit estoppel involve[s] non-signatories who, during the life of the contract, have embraced the contract despite their non-signatory status but then, during litigation, attempt to repudiate the arbitration clause in the contract."⁹² The non-signatory embraces the contract by seeking (i) benefits under the contract or (ii) to enforce the contract's terms. Here, the Fifth Circuit held that Noble did not "embrace" either the distribution agreement or the purchase order agreements.⁹³ First, Noble had no knowledge of either agreement prior to litigation. Therefore, no evidence existed to establish that Noble sought benefits of either contract. Noble did not know of the agreements' terms and, thus, could not have "knowingly exploited" the agreements.⁹⁴ Second, the evidence established that Noble's lawsuit was not based on either agreement; Noble's lawsuit against both defendants was based on representations prior to the purchase of any ropes and duties imposed on the manufacturer and distributor by law.⁹⁵ The Fifth Circuit disagreed with the defendants' argument that Noble's lawsuit was an effort to enforce the specifications in

87. *Id.* at *4–5.

88. *Id.* at *8.

89. *Id.* at *4.

90. 620 F.3d 469, 471 (5th Cir. 2010).

91. *Id.* at 471.

92. *Id.* at 473 (citing *Hellenic Inv. Fund, Inc. v. Det Norske Veritas*, 464 F.3d 514, 517–18 (5th Cir. 2006)).

93. *Id.* at 474.

94. *Id.*

95. *Id.* at 474–75.

the purchase order agreements. The Fifth Circuit, therefore, reversed the district court's dismissal and remanded the action.⁹⁶

IV. THE FRANCHISE RELATIONSHIP, TERMINATION, AND NON-RENEWAL

Two cases regarding termination and non-renewal of a franchise agreement came out in favor of the franchisor and set a high bar for franchisees seeking to bring claims of constructive termination/non-renewal and ineffective termination due to technical non-compliance with the notice of termination.

The United States Supreme Court issued a rare opinion which relates directly to franchise law. The case involved constructive termination and constructive nonrenewal claims brought by sixty-three Shell franchisees pursuant to the Petroleum Marketing Practices Act ("the PMPA").⁹⁷ In *Mac's Shell Service Inc., v. Shell Oil Products Co.*,⁹⁸ the Shell franchisees brought suit after the franchisor 1) eliminated a volume-based rent subsidy, and 2) offered the franchisees new agreements which changed the formula for calculating rent, which increased rent for some franchisees.⁹⁹ Although the franchisees purportedly considered the franchisor's actions with respect to the modified rent to be wrongful and a constructive termination of their existing agreements, the franchisees continued operating their Shell service stations, purchasing fuel from Shell, and using Shell's trademarks. Although the franchisees objected to the terms the franchisor offered for a renewal franchise agreement, the franchisees also executed the renewal franchise agreements that the franchisor offered upon expiration of the franchisees' existing agreements.

The Court rejected the franchisees' assertion that the actions of the franchisor amounted to constructive termination and constructive nonrenewal of the franchise relationship.¹⁰⁰ While specifically reserving judgment as to whether causes of action for constructive termination or constructive nonrenewal exist under the PMPA at all,¹⁰¹ the Court held that in order for a franchisee to bring a claim for constructive termination, a franchisee must abandon the use of the franchisor's trademark, cease purchasing the franchisor's fuel, or abandon occupation of the franchised premises.¹⁰² That is, to claim construction termination under the PMPA, the franchisee must actually stop its franchised business. The Court analogized the franchisees' situation to the employer/employee context and landlord/tenant context, which each require as part of a claim for constructive termination that the employee no longer be employed and the tenant have left the premises. The Court similarly held that by

96. *Id.* at 471.

97. 15 U.S.C. §§ 2801–2891 (2006).

98. 130 S. Ct. 1251, 1251 (2010).

99. *Id.* at 1256.

100. *Id.* at 1254–55.

101. *Id.* at 1257 n.4.

102. *Id.* at 1261–62.

signing a renewal agreement, even under protest, a franchisee is precluded from bringing a claim for constructive nonrenewal under the PMPA.¹⁰³ The Court emphasized the limited scope of the PMPA, which regulates only termination and nonrenewal of agreements.¹⁰⁴ The Court noted that to expand constructive nonrenewal claims under the PMPA to instances in which franchisees were to sign a new agreement and *then* object to its terms would “chill franchisors from proposing new terms in response to changing market conditions and consumer needs.”¹⁰⁵

Since the PMPA preempts state law on the termination and nonrenewal of petroleum franchises, the U.S. Supreme Court set a high bar for franchisees seeking to bring such claims in Texas, while explicitly leaving the door open for claims based on state law rather than the PMPA.¹⁰⁶

There was another significant termination case during the Survey period. In *Ultimate Ford, Inc. v. Motor Vehicle Division of the Texas Department of Transportation*,¹⁰⁷ the Austin Court of Appeals addressed an ineffective termination claim of two franchised Ford dealerships. The dealerships did not claim that Ford lacked good cause to terminate their franchise agreements, but rather asserted on appeal that their substantive rights were prejudiced because Ford’s notices of termination did not contain the exact language of the appropriate statute.¹⁰⁸

In *Ultimate Ford*, Mohammed Assadi owned two Ford dealerships, which had each gone through bankruptcy proceedings twice.¹⁰⁹ Ford sought to terminate the dealerships and sent the franchisee notices of termination. Although the notices partially conformed to the relevant section of the Texas Occupations Code¹¹⁰ by providing statements of the right of the dealerships to file protests, the notices did not track the language of the code verbatim.¹¹¹ Specifically, Ford’s notices failed to state the correct agency to which the franchisee had the right to appeal, and did not cite the correct statute, chapter 2301 of the Texas Occupations Code. Instead, the notices cited the predecessor statute, the Motor Vehicle Commission Code, and stated that the franchisee had a right to file a protest with the Motor Vehicle Commission, which is no longer the proper entity.¹¹²

The dealerships cited *Buddy Gregg Motor Homes, Inc. v. Motor Vehicle Board*¹¹³ for the proposition that a notice of termination “[M]UST contain the EXACT word-for-word language” of the disclaimer found in

103. *Id.* at 1264.

104. *Id.*

105. *Id.*

106. *Id.* at 1260.

107. No. 03-09-00548-CV, 2010 Tex. App. LEXIS 7055, *1 (Tex. App.—Austin 2010, pet. denied).

108. *Id.* at *7–8.

109. *Id.* at *2.

110. TEX. OCC. CODE § 2301.453(c)(2) (West 2011).

111. *Ultimate Ford*, 2010 Tex. App. LEXIS 7055, at *4–5.

112. *Id.* at *5.

113. 179 S.W.3d 589, 596, 605–07 (Tex. App.—Austin 2005, pet. denied).

the statute.¹¹⁴ The court disagreed, holding that “any non-compliance with the notice requirements” does not necessarily invalidate a determination of good cause.¹¹⁵

The court in this case found unpersuasive the argument that the dealerships were prejudiced by the non-complying language in the notices, in part, because the dealerships had, in fact, filed timely protests with the correct entity and cited the correct statute.¹¹⁶ Moreover, the dealerships went on to exercise their rights by participating in the contested case hearing that ensued.¹¹⁷ Based on this lack of prejudice, the court held that Ford’s notice did not render its termination of the dealerships invalid.¹¹⁸

V. INTELLECTUAL PROPERTY

Trademark-related litigation often plays a large part in franchisee-franchisor legal disputes. The ability of a franchisor to use the Lanham Act to prevent a terminated franchisee from using the franchisor’s trademarks is one of a franchisor’s most powerful tools in litigation. Furthermore, the fact that courts are generally willing to grant preliminary injunctive relief to protect trademarks means that trademark claims are often featured prominently early in franchisee-franchisor litigation.

In *7-Eleven, Inc. v. Puerto Rico-7, Inc.*, the franchisor sought to enforce its trademark rights by seeking injunctive relief.¹¹⁹ Puerto Rico-7, Inc. (PRSI) owned area development rights to develop 7-Eleven franchises in Puerto Rico.¹²⁰ In exchange for the rights to develop 7-Eleven in Puerto Rico, PRSI was required to develop certain numbers of 7-Eleven stores in Puerto Rico by certain dates, pay monthly royalties to 7-Eleven, and maintain a certain amount of operational capital.¹²¹ In 2007, PRSI had failed to open the required number of stores, failed to make royalty payments, and failed to maintain the required level of capital, as evidenced by payment disputes with vendors.¹²² 7-Eleven, Inc. sent PRSI a default notice and provided an opportunity for a cure period, but PRSI failed to cure its defaults apart from paying the past-due royalties.¹²³ 7-Eleven brought suit, alleging claims of, among other things, trademark infringement, unfair competition, and breach of contract, they also sought a declaratory judgment that the development agreement was validly terminated.¹²⁴

114. *Ultimate Ford*, 2010 Tex. App. LEXIS 7055, at *10.

115. *Id.* at *12.

116. *Id.* at *6, *14.

117. *Id.* at *6.

118. *Id.* at *16–17.

119. *See generally* 7-11, Inc. v. Puerto Rico-7 Inc., No. 3:08-CV-0140-B, 2009 U.S. Dist. LEXIS 115064, *1 (N.D. Tex. Dec. 9, 2009).

120. *Id.* at *2–3.

121. *Id.* at *3–4.

122. *Id.* at *6–7.

123. *Id.* at *7–8.

124. *Id.* at *9–10.

The court granted 7-Eleven's motion for summary judgment.¹²⁵ The court first recognized that "[w]hether Defendants' alleged use of the 7-ELEVEN Marks constitute[d] infringement or unfair competition turns on [whether 7-Eleven] validly terminated the [development agreement] that had previously authorized PRSI to use those marks."¹²⁶ The court therefore analyzed 7-Eleven's contract claims before it even reached the trademark claims.¹²⁷ When the court did turn to 7-Eleven's trademark claims, its analysis was straightforward. The court noted that any use of 7-Eleven's trademarks by PRSI after the development agreement was terminated was unauthorized and that "PRSI 'is an ex-licensee, and the law is clear that termination of a trademark license precludes further use by the licensee.'"¹²⁸ The court stated that the primary purpose of alleging trademark infringement is to "protect the ability of consumers to distinguish among [competitors],"¹²⁹ and that "[c]ommon sense compels the conclusion that a strong risk of consumer confusion arises when a terminated franchisee continues to use the former franchisor's trademarks."¹³⁰ The court granted 7-Eleven an injunction on its trademark claim, recognizing that PRSI's continued use of 7-Eleven's trademarks impacted the entire 7-Eleven chain: "When unauthorized use of service marks wrongly identify Defendants' formerly-licensed locations with [7-Eleven], the resulting injury impacts the entire [7-Eleven] chain."¹³¹

From a trademark perspective, *7-Eleven* presents a good recent example of the relatively straight-forward elements involved in obtaining relief when a former franchisee operates without an in-force trademark license. In addition, *7-Eleven* shows the crucial importance for a franchisor to make sure it carefully follows the proper procedure under the relevant contracts to terminate the franchise agreement. The *7-Eleven* court explicitly recognized that 7-Eleven's trademark claims depended upon whether its contract with PRSI was appropriately terminated, and the court went into great factual detail in analyzing 7-Eleven's various default notices.¹³² Consequently, franchisors must always be mindful of concepts such as cure periods, notice requirements in that they may well ultimately prove vital in protecting a franchisor's intellectual property. Conversely, franchisee counsel should never assume that a franchise agreement has been properly terminated and should always make sure that the

125. *Id.* at *36.

126. *Id.* at *16.

127. For a discussion of the contract-related elements of the court's decision, *see infra* p. 134-35.

128. *Id.* at *27 (quoting *Ramada Franchise Sys. Inc. v. Jacobcart, Inc.*, No. 3:01-CV-0306-D, 2001 U.S. Dist. LEXIS 6650, at *7 (N.D. Tex. May 17, 2001)).

129. *Id.* (quoting *Epperdorf-Netheter-Hinz GMBH v. Ritter GMBH*, 289 F.3d 351, 355 (5th Cir. 2002)).

130. *Id.* at *28 (quoting *Hawkins Pro-Cuts, Inc. v. DJT Hair, Inc.*, No. 3:96-CV-1728-R, 1997 U.S. Dist. LEXIS 22418, at *5 (N.D. Tex. July 25, 1997)).

131. *Id.* at *30.

132. *Id.* at *6-10.

franchisor has adequately complied with all of the franchise agreement's requirements for termination.

Century 21 Real Estate LLC v. Gharbi presents a franchise-related cybersquatting case out of the bankruptcy court for the Western District of Texas.¹³³ Mohammad Gharbi operated as a Century 21 real estate sales franchise in Austin and Bastrop, Texas.¹³⁴ Gharbi's franchise was terminated for failure to pay amounts due to Century 21.¹³⁵ Gharbi filed for bankruptcy, and Century 21 Real Estate LLC (Century 21) filed a motion for summary judgment on its adversary claims alleging trademark infringement and cybersquatting.¹³⁶ Gharbi was involved with four relevant websites: www.texascentury21.com; www.century21online.com; www.texasproperties.com/century21capitalteam; and www.austinhomeland.com.¹³⁷ The Century 21 trademark was either explicitly part of the domain name of these sites or was displayed on the front page.¹³⁸ Century 21 contended that the websites violated the Lanham Act and the Anti-cybersquatting Consumer Protection Act ("ACPA").¹³⁹

First, the court considered the websites under the Lanham Act. Gharbi argued that he was not using the trademarks "in commerce" as required by 15 U.S.C. §§ 1114 and 1125 because he was selling his own property.¹⁴⁰ It was undisputed that Century 21 itself had no interest in any of the properties sold by Gharbi.¹⁴¹ The court rejected this argument, holding that "whether or not the Debtor was only selling his own property does not make the Defendant's use of the Century 21 mark non-commercial."¹⁴² Moreover, as the websites were offering real estate services to the general public, Gharbi's use of the Century 21 mark in connection with them was commercial.¹⁴³ *Century 21* thus provides a reminder of the wide reach of the Lanham Act's "commerce" requirement.

Turning to the traditional Lanham Act analysis, the court stated that "selling real estate from a website with a domain name that includes Century 21 or that displays the Century 21 mark on its front page would cause a consumer to assume the agent is someone connected to Century 21."¹⁴⁴ The court concluded that Century 21 was entitled to an injunction on its Lanham Act claim.¹⁴⁵

133. No. 08-11023-CAG, Adv. No. 08-01099-CAG, 2010 Bankr. LEXIS 1247, at *1 (Bankr. W.D. Tex. April 19, 2010). For a discussion of a damages-related element of the court's decision, *see infra* p. 144-45.

134. *Id.* at *1-2.

135. *Id.* at *2.

136. *Id.* at *2-3.

137. *Id.* at *3.

138. *Id.* at *10-11.

139. *Id.* at *3.

140. *Id.* at *9.

141. *Id.* at *13.

142. *Id.* at *9.

143. *Id.* at *9-10.

144. *Id.* at *11 (citing *Marathon Mfg. Co. v. Enerlite Prod. Corp.*, 767 F.2d 214, 220 (5th Cir. 1985)).

145. *Id.* at *16.

Lastly, the court considered Century 21's ACPA claims. Under ACPA, a person is liable if the person:

- (i) has a bad faith intent to profit from that mark, including a personal name which is protected as a mark under this section; and
- (ii) registers, traffics in, or uses a domain name that—
 - (I) in the case of a mark that is distinctive at the time of registration of the domain name, is identical or confusingly similar to that mark;
 - (II) in the case of a famous mark that is famous at the time of registration of the domain name, is identical or confusingly similar to or dilutive of that mark; or
 - (III) is a trademark, word, or name protected by reason of section 706 of title 18 or section 220506 of title 36.¹⁴⁶

ACPA provides a list of nonexclusive factors for a court to use in determining bad faith.¹⁴⁷ The court held that there was insufficient evidence to grant summary judgment for Century 21 on its ACPA claim.¹⁴⁸ The court stated that although Gharbi did not change the websites when his Century 21 franchise was terminated, that, in itself, does not show bad faith because "it is also possible that the Defendant was simply slow to act in removing the mark and shutting down the businesses' websites."¹⁴⁹ Moreover, although registering a domain name with intent to profit from a lawful trademark owner indicates bad faith under the statute, the court noted that "at the time the Defendant registered the domain names he had the right to use the Century 21 mark and used the mark specifically because of its association with the Plaintiff's services, real estate brokering."¹⁵⁰

Century 21 therefore demonstrates a potential roadblock for franchisors attempting to use ACPA against terminated franchisees. The statute requires showing bad faith, and as was the case in *Century 21*, most franchisees will have initially registered their domain names and set up their websites in the beginning of the franchise relationship, when the franchise agreement's trademark license was in effect. *Century 21* thus illustrates the difference between traditional Lanham Act claims, for which the court granted Century 21's motion for summary judgment, and an ACPA claim, for which the court denied summary judgment.

VI. COMMON LAW CLAIMS

A. BREACH OF CONTRACT

The majority of contract-related disputes center around the most central document to the franchise relationship, the franchise agreement. In pursuing claims based on misuse of intellectual property, the courts make

146. 15 U.S.C. § 1125(d)(1)(A) (2006).

147. *Id.* at § 1125(d)(1)(B) (2006).

148. *Century 21*, 2010 Bankr. LEXIS 1247, at *20–22.

149. *Id.* at *21.

150. *Id.*

clear that the key to obtaining injunctive relief to protect a franchisor's trademarks is to show that the trademark license agreement (the franchise agreement) and/or the development agreement have been terminated. The case of *7-Eleven, Inc. v. Puerto Rico-7, Inc.*, discussed in Part IV for its trademark-related holdings, emphasizes the importance of proper termination.

As noted above, the court in *7-Eleven, Inc.* first analyzed the plaintiff franchisor 7-Eleven's contract claims in order to determine whether the defendant franchisee PRSI's intellectual property license was properly terminated.¹⁵¹ 7-Eleven claimed that PRSI was in default of the development agreement for failure to pay royalties, failure to maintain adequate capitalization, and failure to open enough stores to meet the area development schedule.¹⁵² PRSI claimed that it repaid all the delinquent royalties and that the other defaults were not material.¹⁵³

The court held that failure to open the required number of stores under the area development agreement was a material breach.¹⁵⁴ Furthermore, PRSI did not rebut the evidence presented by 7-Eleven that PRSI was operating with insufficient capital resulting in stores with empty shelves, and the court granted 7-Eleven summary judgment.¹⁵⁵ The court also granted 7-Eleven summary judgment on its claim for breach of the development agreement's post-termination provisions requiring, among other things, discontinuing the use of 7-Eleven's trademarks.¹⁵⁶ This holding was key to the court's intellectual property rulings, discussed in Part V above: "[b]ecause the Court determined that the ALA was appropriately terminated, any continued use of the 7-ELEVEN Marks was unauthorized."¹⁵⁷ The court in *7-Eleven, Inc.* thus spelled out the importance of the franchise agreement in franchisor-franchisee litigation.

B. FRAUD AND MISREPRESENTATION

Although mostly concerned with federal pleading requirements, *Wilkin Partners, L.P. v. Champps Operating Corp.* provides a demonstration of the federal pleading requirements for fraud and misrepresentation.¹⁵⁸ The *Wilkin Partners* plaintiff alleged that representatives of the "defendants" fraudulently induced it to enter into a Champps franchise agreement by failing to disclose certain negative information about the

151. *7-Eleven, Inc. v. Puerto Rico-7, Inc.*, No. 3:08-CV-0140-B, 2009 U.S. Dist. LEXIS 115064, at *16 (N.D. Tex. Dec. 9, 2009).

152. *Id.* at *18.

153. *Id.* at *19.

154. *Id.* at *20 (citing *Bennigan's Franchising Co., L.P. v. Swigonski No. 3*, No. 06-CV-2300-BH, 2008 U.S. Dist. LEXIS 14871, at *10 (N.D. Tex. Feb. 26, 2008)).

155. *Id.* at *20-21.

156. *Id.* at *21-23. See Section VIII, *infra* 144-45, for a discussion of the specific performance remedy ordered by the court.

157. *Id.* at *27.

158. See generally *Wilkin Partners, L.P. v. Champps Operating Corp.*, No. SA-10-CV-562-XR, 2010 U.S. Dist. LEXIS 90808, *1 (W.D. Tex. Sept. 1, 2010).

location in question.¹⁵⁹ The plaintiff names Champps Operating Corporation and Champps Entertainment of Texas, Inc. in the petition, which was originally filed in Texas state court.¹⁶⁰ The defendants removed to the Western District of Texas based on diversity jurisdiction even though Champps Entertainment was a Texas company, arguing that it had been improperly joined.¹⁶¹

In analyzing the improper joinder argument, the court first conducted a Federal Rule of Civil Procedure 12(b)(6) analysis.¹⁶² The plaintiff alleged that the “‘defendants’ made misrepresentations or failed to disclose material information it was under a duty to disclose, without specifying whether any particular misrepresentation or knowing omission was made by a representative of Champps Operating or Champps Entertainment.”¹⁶³ The court held that this was not enough to satisfy Federal Rule of Civil Procedure 9(b)’s heightened pleading requirements for fraud, which requires specifying the allegedly fraudulent statements, including stating when and where they were made, and explaining why the statements were fraudulent.¹⁶⁴ The ultimate decision of the court in *Wilkin Partners* did not depend on this analysis since it applied to both defendants equally and a finding of improper joinder cannot be based on a deficiency applicable to both diverse and non-diverse defendants.¹⁶⁵ Nonetheless, *Wilkin Partners* is a reminder of the necessity of pleading fraud with particularity even in state court, since the plaintiff’s petition will be subject to a Federal Rule 9(b) analysis if a defendant chooses to remove the case.

C. VICARIOUS LIABILITY

In *Ascension v. Thind Hotels, LLC*, the Southern District of Texas considered a vicarious liability claim brought against Holiday Inns, Inc. in an employment discrimination context.¹⁶⁶ Plaintiff Edgar Ascension alleged that he was sexually harassed at work at a Holiday Inn Express in The Woodlands, Texas.¹⁶⁷ Ascension brought suit against his employer (an employment agency), the corporate owner of the hotel franchise, and the franchisor, Holiday Inns, Inc. (“HII”), alleging claims under Title VII of the Civil Rights Act of 1964.¹⁶⁸ HII moved to dismiss under Federal Rule of Civil Procedure 12(b)(6) and for summary judgment.¹⁶⁹

159. *Id.* at *1–2.

160. *Id.*

161. *Id.* at *2.

162. *Id.* at *2–3 (citing *Smallwood v. Ill. Cent. R.R. Co.*, 385 F.3d 568, 573 (5th Cir. 2004)).

163. *Id.* at *7.

164. *Id.* at *7–8 (citing *Sullivan v. Leor Energy*, 600 F.3d 542, 550 (5th Cir. 2010)).

165. *Id.* at *8.

166. No. H-09-792, 2010 U.S. Dist. LEXIS 10504, *2 (S.D. Tex. Feb. 8, 2010).

167. *Id.*

168. *Id.* at *3.

169. *Id.*

HII made a creative argument for dismissal under Rule 12(b)(6): because the complaint alleged that HII was not registered to do business in Texas, HII could not have been Ascension's employer and thus would not be liable under the Title VII claims.¹⁷⁰ The court rejected this argument on the basis that it ignored the possibility of a non-registered entity nonetheless operating in Texas in violation of the Business Organization Code.¹⁷¹ The court did accept HII's more conventional argument that it was not Ascension's employer as demonstrated by the affidavit of HII's vice president of franchise operations, which essentially provided that HII did not own or control the hotel at issue.¹⁷² *Ascension* provides a concise demonstration that vicarious liability claims against franchisors, such as Ascension's Title VII claims, that may be defeated on a motion for summary judgment may nonetheless pass Rule 12(b)(6) muster.

VII. STATUTORY CLAIMS

A. ANTITRUST

In *PSKS, Inc. v. Leegin Creative Leather Products, Inc.*, the Fifth Circuit considered whether the district court had properly granted a manufacturer's motion to dismiss after the United States Supreme Court reversed its *Dr. Miles' per se* rule relating to resale price maintenance (RPM) agreements.¹⁷³ Leegin manufactured and distributed handbags, belts, jewelry, and other "Brighton" brand products.¹⁷⁴ Leegin had a dual distribution system, whereby it distributed Brighton products to wholesalers and sold Brighton products in its retail stores.¹⁷⁵ Leegin had a resale price maintenance policy with its wholesalers, whereby the wholesalers could not sell Brighton products below a certain price.¹⁷⁶ PSKS, the owner of a retail store that sold Brighton products, violated that policy and sold its Brighton products at a discounted price.¹⁷⁷ When PSKS refused to abide by Leegin's price policy, Leegin ceased selling Brighton products to PSKS.¹⁷⁸ In this action, PSKS alleged that Leegin had improperly entered into a vertical RPM agreement.¹⁷⁹ A jury awarded nearly \$4 million to PSKS, and Leegin appealed.¹⁸⁰

In *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, the United States Supreme Court held that RPM agreements were *pre se* im-

170. *Id.* at *7-8.

171. *Id.* at *8.

172. *Id.* at *8-9. HII also argued, and the court apparently agreed, that HII was entitled to summary judgment because HII was not named in Ascension's EEOC complaint, and, therefore, Ascension's administrative remedies were not exhausted with respect to HII. *Id.* at *9.

173. 615 F.3d 412, 414 (5th Cir. 2010).

174. *Id.*

175. *Id.* at 414-15.

176. *Id.* at 415.

177. *Id.*

178. *Id.*

179. *Id.*

180. *Id.*

proper.¹⁸¹ Upon reexamination, the Supreme Court held that “vertical price restraints, like vertical nonprice restraints, often have procompetitive justifications and should be judged under the rule of reason.”¹⁸² The Supreme Court “recognized that the ‘economics literature is replete with procompetitive justifications for a manufacturer’s use of resale price maintenance.’”¹⁸³ Instead of a *per se* violation, vertical price restraints are now judged under the rule of reason.¹⁸⁴

On remand, PSKS amended its complaint, asserting additional facts and claims against Leegin.¹⁸⁵ Among other things, PSKS alleged that Leegin was involved in a horizontal price-fixing conspiracy and that consumers were required to pay artificially high and anticompetitive prices for Brighton products.¹⁸⁶ In reviewing the dismissal of PSKS’s complaint for failure to plead a plausible relevant market under the rule of reason, the Fifth Circuit addressed whether PSKS had established that Leegin’s actions had caused an injury to competition.¹⁸⁷ The Fifth Circuit held that PSKS did not meet its burden.¹⁸⁸ PSKS failed to sufficiently define the relevant product and geographic markets.¹⁸⁹ The Fifth Circuit explained that Brighton did not constitute its own market nor did “wholesale sale” adequately define the relevant market (not the distribution level).¹⁹⁰ In addition to its failure to define the market to support its anticompetitive claims, PSKS also failed to show any anticompetitive harm.¹⁹¹ The Fifth Circuit rejected PSKS’s “artificially high prices” claim, explaining that Leegin and its retailers may provide “interbrand competition” through its prices and services.¹⁹² PSKS also failed to allege any facts that would support any plausible anticompetitive effect.¹⁹³ PSKS did not assert that a group of retailers or one dominant retailer was the source of the RPM policy.¹⁹⁴ Leegin was the purported largest single retailer; thus, independent Brighton retailers could not be the source of the RPM policy.¹⁹⁵ The Fifth Circuit, likewise, rejected PSKS’s horizontal restraint claim.¹⁹⁶ Leegin’s actions as a “dual distributor” did not support PSKS’s claim that the RPM policy was a horizontal restraint.¹⁹⁷

181. 220 U.S. 373, 384 (1911).

182. *PSKS, Inc.*, 615 F.3d at 414 (citing *Leegin Creative Leather Prods., Inc. v. PSKS, Inc.*, 551 U.S. 877, 895–96 (2007)).

183. *Id.* at 415.

184. *Id.*

185. *Id.* at 416.

186. *Id.*

187. *Id.* at 417.

188. *Id.*

189. *Id.* at 418.

190. *Id.*

191. *Id.* at 419.

192. *Id.*

193. *Id.*

194. *Id.*

195. *Id.*

196. *Id.* at 420.

197. *Id.* at 420–21.

B. COVENANTS NOT TO COMPETE

1. *Non-Competition Agreement Enforced*

Courts continue to apply a reasonableness test when construing a covenant not to compete, particularly in a franchise context. In *Bonus of America, Inc. v. Angel Falls Services, L.L.C.*, a Minnesota district court, applying Texas law, held that a franchisee “may not avoid his covenant[sic] not to compete” by doing what he agreed not to do himself through a different entity.¹⁹⁸ Bonus of America, Inc. is a cleaning business franchisor.¹⁹⁹ In 2007, Bonus of America entered into franchise agreements with Gavin Hart and his business entity, Angel Falls Services, L.L.C.²⁰⁰ Hart also executed a personal guarantee in connection with the franchise agreements.²⁰¹ Pursuant to the franchise agreements and guarantee (which were governed by Texas law), Hart and Angel Falls agreed not to “[o]wn, maintain, engage in or have any interest in any business which sells goods or services of a like competitive nature” as his Bonus of America franchise.²⁰² In seeking to obtain injunctive relief to enforce its covenant not to compete, Bonus of America alleged that Hart played a significant role in a similar cleaning and maintenance business, Patron Supply, Inc.²⁰³ Hart denied any violation of the covenant not to compete.²⁰⁴

The district court considered four factors for the preliminary injunction: (1) irreparable harm, (2) balance of harms, (3) likelihood of success, and (4) public interest.²⁰⁵ Because the record showed that Hart had been involved with a competing business such as Patron, Bonus of America met its burden to show irreparable harm through loss of goodwill.²⁰⁶ The district court also acknowledged that Patron’s operations may be harmed if Hart was not able to operate.²⁰⁷ The district court held that Hart’s “self-inflicted” harm would not outweigh the harm to Bonus of America’s reputation and goodwill as a result of Hart’s violation of the franchise agreements.²⁰⁸

The district court analyzed enforceability of the covenant not to compete under Texas law.²⁰⁹

Under Texas law, covenants not to compete are enforceable if they are: ancillary to or part of an otherwise enforceable agreement at the time the agreement is made to the extent that it contains limitations

198. No. 10-2111, 2010 U.S. Dist. LEXIS 67079, at *8 (D. Minn. July 6, 2010).

199. *Id.* at *2.

200. *Id.* at *2–3.

201. *Id.* at *3.

202. *Id.* at *3–4.

203. *Id.* at *5.

204. *Id.* at *6.

205. *Id.* at *6–7.

206. *Id.* at *8.

207. *Id.*

208. *Id.*

209. *Id.* at *12.

as to the time, geographical area, and scope of activity to be restrained that are reasonable . . .²¹⁰

The “otherwise enforceable” requirement for enforcement of covenants not to compete occasionally creates an issue in franchisor/franchisee disputes. The Minnesota district court outlined the promises outside the covenant that constitute an enforceable agreement.²¹¹ Bonus of America disclosed confidential information and permitted Hart and Angel Falls to use its system.²¹² In return, Hart and Angel Falls agreed to pay royalties, keep the disclosed information confidential, and to refrain from competition within the assigned franchise territory.²¹³ Because the time (two years) and geographical area (50-mile radius) were reasonable, the district court held that the covenant not to compete was enforceable.²¹⁴ The district court, therefore, granted the preliminary injunction.²¹⁵

VIII. REMEDIES: DAMAGES AND INJUNCTIVE RELIEF

In *7-Eleven, Inc.*, discussed above in Parts V and VI.A, 7-Eleven sought specific performance as a remedy for the breach of the post-termination provisions, and the court granted 7-Eleven’s request.²¹⁶ The court noted that specific performance is appropriate under Texas law when monetary damages are insufficient, and the court found that PRSI’s continued display of 7-Eleven’s trademarks constituted such irreparable harm.²¹⁷ Although requests for injunctive relief concerning post-termination franchise agreement provisions most often come in the form of Lanham Act-based relief, *7-Eleven* demonstrates that the contract law remedy of specific performance can be asserted as an alternative means to protect intellectual property.

In addition to *7-Eleven, Inc.*, one other noteworthy damages-related analysis occurred in *Century 21*. As discussed above in Part V, the *Century 21* court denied Century 21’s motion for summary judgment on its ACPA claim, holding that there was insufficient evidence of the required bad faith.²¹⁸ Century 21 argued that in the event that there is eventually a finding of bad faith under ACPA, that finding would demonstrate the “willful and malicious injury” by the debtor that would make the resulting debt in bankruptcy non-dischargeable under 11 U.S.C. § 523(a)(6).²¹⁹ The court disagreed and noted that for there to be the level of “willful

210. *Id.* at *12–13 (citing TEX. BUS. & COM. CODE ANN. § 15.50 (West 2011)).

211. *Id.* at *13.

212. *Id.* at *14.

213. *Id.*

214. *Id.*

215. *Id.* at *17.

216. *7-Eleven, Inc. v. Puerto Rico-7, Inc.*, No. 3:08-CV-0140-B, 2009 U.S. DIST. LEXIS 115064, at *23–24 (N.D. Tex. Dec. 9, 2009).

217. *Id.* at *23 (citing *Stafford v. Southern Vanity Magazine, Inc.*, 231 S.W.3d 530, 535 (Tex. App.—Dallas 2007, pet. denied)).

218. *Century 21 Real Estate, LLC v. Gharbi*, No. 08-11023, Adv. No. 08-01099-CAG, 2010 Bankr. LEXIS 1247, at *21–22 (Bankr. W.D. Tex. April 19, 2010).

219. *Id.* at *23–24.

and malicious injury” required for non-dischargeability in bankruptcy, the debtor “must have intended the actual injury to result from his actions.”²²⁰ At least according to this court, even if a franchisor could establish bad faith in a cybersquatting case against a bankrupt franchisee, that alone would not be enough to make the resulting debt non-dischargeable.

IX. CONCLUSION

Similar to years past, during the Survey period, Texas and federal courts reaffirmed the importance of the contractual nature of the relationship between franchisors and franchisees, and also continued to emphasize compliance with procedural requirements. In *SmallBizPros*, the Fifth Circuit reminded franchisors and district courts alike that some of the terms of any settlement agreement should be incorporated into a stipulated settlement order for the district court to retain jurisdiction, as “inexact compliance is no compliance.”²²¹ Where exact compliance would be illogical, however, as in *Ultimate Ford, Inc. v. Motor Vehicle Division of the Texas Department of Transportation*, courts recognize it may not be required.

Throughout the past year, multiple franchisors also addressed the inappropriate and continued use of their marks by franchisees and other parties following termination of an agreement. Such cases highlight the importance of ensuring that agreements adequately address the use of trademarks upon termination and that agreements are, in fact, terminated properly. In *7-Eleven, Inc. v. Puerto Rico-7, Inc.*, the court relied upon a finding that the agreement had been validly terminated to determine whether unauthorized use of the marks occurred. In *Century 21 Real Estate, LLC v. Gharbi*, Century 21 fought the continued use of its trademarks and name by a terminated franchisee. Even though the court granted the injunction against further use of the marks under the Lanham Act, the court did not find that the franchisee had acted in bad faith, precluding claims under the ACPA.

220. *Id.* at *24 (citing *In re Delaney*, 97 F.3d 800, 802 (5th Cir. 1996)).

221. *SmallBizPros v. MacDonald*, 618 F.3d 458, 464 (5th Cir. 2010).

