You are receiving this periodical based upon previous specific and general contacts with the Goldstein Law Group regarding franchise law issues. We look forward to keeping you updated on the current trends in franchise court decisions around the country in both state and federal courts.

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FRANCHISE TRENDS

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Franchisee Fails to Move Fast Enough and Gets Snared in Statute of Limitations Bar

Robert Gainer v. Hickory Dickory Decks, E.D. Michigan (2011)

Plaintiff franchisee Robert Gainer filed this action against Defendants Hickory Dickory Decks ("HDD"), and Thomas Jacques ("Jacques") (collectively, "Defendants")alleging fraud, among other claims. The franchisee plaintiff had purchased a "Hickory Dickory Decks" design and installation of residential decks franchise business. Specifically, the franchisee alleged that the franchisor provided it with false information regarding the profit that Plaintiff would derive as a HDD franchisee, and falsely indicated that Plaintiff's Michigan franchise would benefit from advertising and goodwill associated with the "Hickory Dickory Decks" trade name. Plaintiff contended that he relied on these alleged misrepresentations to his detriment.

Although neither a UFOC or franchise agreement was provided to the franchisee, the parties entered into an oral agreement making Plaintiff an HDD affiliate authorizing him to sell and construct HDD residential decks in Michigan. Per the oral agreement, Plaintiff was to pay HDD 6% royalties on all his HDD deck sales. Although HDD believed Plaintiff also had other obligations, including the obligation to pay joint advertising fees like those paid by HDD franchisees, Plaintiff did not agree, and did not pay HDD any joint advertising fees. In exchange for paying a royalty, Plaintiff was able to operate an HDD business, generating revenue and profits in accordance with his abilities to operate the business. Plaintiff acknowledged that their oral agreement did not require Plaintiff to maintain his business relationship with HDD for any specific duration and he could walk away from his affiliation with HDD at any time.

Franchise Discrimination - Video 1 of 2

Franchise Discrimination - Video 2 of 2

Franchisor Could Have Violated the Covenant of Good Faith and Fair Dealing by Competing Directly with Franchisee's Customers Below Cost

G.L.M. Security & Sound, Inc. V. Lojack Corp. (2011)

Plaintiff was a New York franchisee corporation that sold, among other things, car security systems to car dealers in New York City and the suburbs. Defendant is a Delaware corporation that manufactures and distributes car security systems. In 2002, Plaintiff and Defendant entered into a "Distributorship and Installation Agreement", which provided, in general terms, that Defendant franchisor would sell its security systems to Plaintiff franchisee. During the course of their relationship, Defendant and Plaintiff freely traded customers, and jointly serviced customers in the New York area. Defendant both helped Plaintiff sell Defendant's products to Plaintiff's car dealership-clients and sold its security systems directly to car dealers. Plaintiff claimed that Defendant sold its security systems to car dealers more cheaply than it sold them to Plaintiff.

Plaintiff confronted Defendant about the pricing discrepancy, but Defendant assured

The franchisee began generating revenue and paid royalties to HDD on his deck sales. He continued to make monthly royalty payments to HDD for nearly three years. Plaintiff's HDD deck-building business generated significant sales from February 2004 through November 2006, after which Plaintiff sent a letter to Jacques informing him that Plaintiff was terminating his relationship with HDD. HDD's on-line manuals and documents were accessed and downloaded the next day and again two days later using Plaintiff's HDD-assigned access code. Plaintiff denied that he downloaded the HDD materials after the date he terminated his relationship with HDD.

Plaintiff subsequently started his own franchise system to license others to design and construct residential decks in 2009 under the name DECKStraodinaire. DECKStraodinaire provided franchise materials that Plaintiff alleges he created with his friend, Patti. The court pointed out that under Michigan's Franchise Investment Act"[a]n action shall not be maintained to enforce a civil or criminal liability created under this act unless brought before the expiration of 4 years after the act or transaction constituting the violation." Defendants' alleged acts of fraudulent representations giving rise to the purported violations, however, occurred seven years before this lawsuit was filed and more than 3 years beyond the applicable statute of limitations set forth in Michigan Compiles Laws.

Plaintiff, however, contended that Defendants' statute of limitations argument only applies to wrong-doing beyond the applicable statutory period. Any allegedly wrongful acts that occurred within the statutory period thus remain viable even in the absence of fraudulent concealment. For example, Plaintiff contended that each "franchise fee" collected within the statutory period is a violation of the Michigan Franchise Investment Act as well as the Franchise Opportunity information sheet containing viable fraudulent misrepresentations that were made within six years of the filing date. The court rejected the franchisees' argument in this regard, and dismissed the claims.

Individual Officers/Owners of Franchisee Avoid Liability Based on Signature Block

Free Green Can, Llc V. Green Recycling Enterprises, Llc, Edward Jarzobski, Dedric Gill, And Robb Jorgensen N.D., Illinois, (Oct. 2011)

Plaintiff Free Green Can LLC ("Free Green Can") developed the business concept of providing dual purpose recycle and trash bins to public and private institutions and selling advertising rights on those bins to third-parties. Free Green Can envisioned the placement of the bins in heavily-trafficked "host site" locations. Host sites would receive a cost-free trash and recycling solution and earn a share of the advertising revenue. Free Green Can licenses its registered trademarks to Plaintiff FGC Franchises, LLC ("FGC Franchises"), who in turn sub-licenses the trademarks to Free Green Can franchises. (Id.)

In October 2009, Free Green Can and GRE and Defendants Gill, Jarzobski, and Jorgensen executed a franchise agreement. The preamble to the franchise agreement states that the agreement was entered into by and between Free Green Can Products, LLC and "the individual or business entity indentified in the signature block of this Agreement ("Franchisee")." Green Recycling Enterprises, Inc. was listed in the signature block as the Franchisee. Defendants Gill, Jorgensen, and Jarzobski signed the franchise agreement without indicating their corporate affiliation. Steve Holland executed the franchise agreement on behalf of Green Can Products, LLC in his

Plaintiff that it was not offering its direct-sales customers a better price than what Plaintiff was receiving. Plaintiff, in turn, reassured its dealership customers that they were getting the same price as those dealerships who bought straight from Defendant. At some point, however, an unnamed employee of Defendant sought out Defendant's Director of Sales for New York and New Jersey. The employee, who had been selling security systems directly to car dealers for a lower price than what Plaintiff was required to charge to dealers in the same geographic area, complained to the franchisor's Director of Sales that that Defendant's business tactics were injuring Plaintiff. "F*ck [Plaintiff/Franchisee]," the Director of Sales replied.

The franchisee's and franchisor's business relationship fell apart after that. Plaintiff demanded that Defendant compensate Plaintiff for the difference between the price it charged Plaintiff and the price it charged its direct dealership customers, plus extra to reimburse the labor cost of installing the security systems. Defendant refused and informed Plaintiff that it would not sell Plaintiff any security systems except on a "pre-paid" basis and only after Plaintiff's account, which had previously been payable on 120-day terms, had been paid in full. The franchisee interpreted this as a material breach, and it terminated the Agreement.

The court dismissed the franchisee's fraud claims because they arose directly out of the franchise agreement and were not 'free-standing.' New York law also requires that a fraud claim raised in a case stemming from breach of contract be "sufficiently distinct from the breach of contract claim." More specifically, under New York law, "where a fraud claim arises out of the same facts as plaintiff's breach of contract claim, with the addition only of an allegation that defendant never intended to perform the precise promises spelled out in the contract between the parties, the fraud claim is redundant and plaintiff's sole remedy is for breach of contract."

In the end, the court permitted the franchisee's breach of contract and breach of the covenant of good faith and fair dealing claims, and a couple of price discrimination claims, to go forward, given that the franchisee claimed that the franchisor did not sell Plaintiff its SVRU product at its "best price," was dishonest in telling Plaintiff that it was, and sold their SVRUs at cheaper prices to other dealers.

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capacity as its president.

After purchasing the dual purpose containers, GRE allegedly placed these bins in several venues and secured advertising commitments from major organizations. However, the GRE Defendants allegedly violated the franchise agreement by failing to pay Free Green Can the advertising fees due under the franchise agreement. Additionally, the GRE Defendants failed to report on the placement and solicitation of the dual purpose bins, submit financial statements to Free Green Can and permit Free Green Can to inspect their financial books and records.

Free Green Can advised Gill, Jarzobski and Jorgensen that these actions constituted an Event of Default and were grounds for terminating the franchise agreement. In response, GRE Defendants informed Free Green Can that the franchise agreement was null and void because Free Green Can did not register its franchise with the Nebraska Department of Banking. Later, however, Free Green Can denied the franchise agreement was a nullity and demanded the GRE Defendants comply with the agreement. Plaintiffs also provided the GRE Defendants with notice that their acts infringed Free Green Can's trademarks.
v Interestingly, and additionally, Plaintiffs further alleged that the Individual Defendants themselves, not just the corporate entity, had violated the franchise agreement and trademark laws. The court initially pointed out that corporate officers are not generally held liable for a corporation's contractual obligations solely by their association with the corporation. Here, however, plaintiffs argued that the Individual Defendants should be held liable for wrongdoings committed under the franchise agreement based on their belief that the Individual Defendants entered into the franchise agreement in their individual capacities. Plaintiffs' belief stemmed from allegations that the Individual Defendants, Jarzobski, Gill, and Jorgensen solicited the plaintiffs to grant the defendants franchise rights, negotiated the terms of the franchise agreement without using corporate formalities, and signed the franchise agreement without indicating their official capacities or corporate titles. The court rejected this argument stating that the defendants' intention to enter the franchise agreement on behalf of GRE is clear. The court pointed out that the opening paragraph of the franchise agreement provides that "this Agreement is made and entered into ... by and between [Free Green Can as Free Green Can Products, LLC] ... and the individual or business entity identified in the signature block of this agreement ("Franchisee")." Then, in the agreement, the signatory block specifically identifies "Green Recycling Enterprises, Inc." as the franchisee. Thus, while in isolation, failing to include corporate titles on the signature block is somewhat ambiguous, when viewing the Franchise Agreement in its entirety, the defendants' intent to have GRE serve as the Franchisee is apparent.

The Plaintiffs also prayed to have the Court pierce the corporate veil of GRE to hold the Individual Defendants (of the franchisee) personally liable by piercing the corporate veil. The court rejected the franchisor's argument stating that it would pierce the corporate veil only where: (1) there is such a unity of interest and ownership that separate personalities of the corporation and the individual no longer exist; and (2) where adherence to the fiction of separate corporate existence would promote injustice or inequity. The court stated that under this test the Individual Defendants could not be held liable because there was no evidence by the franchisor that the Individual Defendants directed the actions and decisions of GRE, engaged in business without regard to corporate formalities and that Defendant Jorgensen made significant financial investments in GRE due to the corporation's undercapitalization.

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Franchisor's Hard-Bargaining With Franchisee Not

Franchisor's Failure to Disclose Requested Earnings Information Was Not Fraud

7-Eleven, Inc. v. Spear, DC Ill. (2011)

A convenience store franchisor did not commit common law fraud or violate either the Illinois Franchise Disclosure Act (IFDA) or Illinois "little FTC Act" by failing to provide material information concerning the historical performance of a store to a prospective franchisee even though the franchisee had requested such information in connection with her consideration and purchase of the franchise for the store. Therefore, the franchisee was permitted to continue its case against the franchisor.

After terminating the franchisee for failing to meet the franchise's minimum net worth requirements, the franchisor brought suit seeking a preliminary injunction forcing the franchisee to surrender the store premises and meet her other post-termination obligations. The franchisee's counterclaims alleged that the franchisor was required to disclose financial information concerning the particular store she was considering and eventually purchased especially because the store's financial performance was allegedly "below average" compared to the operating statistics for other franchises in the region. The store had been operating for less than one year.

The court ruled that the franchisor was not required by either the FTC Franchise Rule to disclose earnings information for any of its stores, let alone the store that the franchisee decided to purchase. Although the franchisor did elect to include an earnings claim in its UFOC, that was a specific disclosure of merely "the most recently available annual averages of the actual sales, earnings and other financial performance" of stores that were not representative of stores operating nationally. The franchisor specifically disclosed in its UFOC that it was not providing information related to stores that had been opened for less than 12 months. Further, the franchisor allegedly informed the franchisee that it would not provide such information.

The franchisee argued that she should have been provided with information on the Davis Street store's "historical poor performance" in order to correct a misimpression created by the earnings claim. The court specifically rejected the franchisee's argument concluding that a fallacy of the franchisee's argument was that, contrary to her accusations, the earnings claim in the UFOC was not offered as indicative of the actual performance of the specific store she purchased.

Coercion or Duress

Pizzeria Uno Corporation V. Pizza By Pubs, Inc., Civil Action No. 09-12015 (Sept. 9, 2011)

Plaintiff Pizzeria Uno ("Uno") brought a complaint against its franchisee, Defendant Pizza By Pubs, Inc. ("PBP"), and PBP's controlling principals, Defendants Joseph Eways and Laila Moore, alleging nine separate counts of breach of contract and fraud.

Between November 2000 and March 2004, Uno entered into a series of franchise agreements with Defendant PBP to open and operate four restaurants. Defendant Eways (PBP's President) and his sister Defendant Moore (PBP's Secretary) each executed personal guarantees through which they jointly and severally agreed to be bound by the franchise agreements and to guarantee to Uno and its successors that all of PBP's obligations and fees under the franchise agreements would be paid punctually to Uno. PBP, however, became unable to pay certain fees set forth in the franchise agreements.

Defendants argued that Uno breached the implied covenant of good faith and fair dealing in two ways: by failing to disclose its impending bankruptcy filing when it negotiated the note with Defendants, and by adding "higher-priced, up-scale items like lobster" to the menu.

The court held that the franchisees' argument regarding the Uno bankruptcy is baseless. First, Defendants cannot claim on the facts of this case that Uno's bankruptcy itself excuses Defendants' breach of the note, since Uno filed for bankruptcy on January 20, 2010, after Defendants had already breached the note both by failing to make their monthly payment due on January 1, 2010 and by closing one of the franchises on December 1, 2009. Further, the court pointed out that there is no evidence in the record that, at the time the note was executed, Uno was planning on filing for bankruptcy.

The court also held that the franchisees' argument regarding lobster was, legally if not taxonomically, a red herring. Defendants assert that Uno breached the covenant of good faith and fair dealing when it added to its fare "items like lobster" and, in so doing, "became a completely different restaurant" four years before Defendants executed the note. Defendants' argument, whatever its merits, thus relates only to the underlying franchise agreements entered into by the parties between 2000 and 2004, not to the note, which was the sole subject of the breach of guaranty claim.

Defendants also claimed that they only executed the note as a result of economic duress. A contract entered into under economic duress is voidable. The court then cautioned that the standard for establishing economic distress under Massachusetts law is difficult to meet since:

It is not infrequent that when two commercial parties enter into an agreement, one of them has a decided economic advantage over the other, and that the weaker party often must often enter into the bargain because of his economic circumstances, a disparity in bargaining power to his disadvantage, or some combination of the two. Because an element of economic duress is thus present when many contracts are formed or releases given, the ability of a party to disown his obligations under a contract or release on that basis is reserved for extreme and extraordinary cases. Hard bargaining is not unlawful; it is not only acceptable, but indeed, desirable, in our economic system, and should not be discouraged by the courts.

Here, it is clear that Defendants ratified the note. Eways' counsel sent a letter to Uno on July 28, 2009-more than five months after the note was signed on February 19, 2009-asserting that the franchisee Defendant planned to pay off all of its past due royalties and co-op fees as set forth in the note. Defendants do not dispute that they made payments under the note until December 2009, over ten months after executing the note. Indeed, the first time Defendants raised the possibility of duress was when they filed their

The franchisee also argued that while the information provided by the franchisor may not have been false, the franchisor was under a duty to make more representations than it had made in order to prevent the provided information from being misleading. However, the court chastised the franchisee by pointing out that the earnings claim made by the franchisor could only have been "misleading" if the franchisee ignored the express terms of the earnings claim and made projections based upon her own assumptions concerning historical information of other stores, the court decided. The franchisee could not have done so consistent with the disclaimers in her franchise agreement and in the UFOC.

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answers this action and 10, nearly a year after signing the note and months after they had already made ten months' worth of payments thereunder. Thus, even if Defendants had entered into the note under economic duress, their subsequent conduct precluded any reliance on a duress defense.

Even if the Defendants had not ratified the note, the record in this case does not support the conclusion that Defendants were unlawfully coerced into signing the note. Eways conceded that after the note was negotiated, Uno offered him a choice between one alternative, where Eways could reject the note and "continue to accrue increasing penalties under the Franchise Agreements for failure to make Fee payments that Uno's knew Pizza By Pubs could not afford to make," or another alternative wherein Eways could sign the note and "pay outstanding fees, with interest, subject to non-negotiable, one-sided terms, thereby keeping the four restaurants afloat." Even crediting Eways' assertion in full, this is "hard bargaining," not coercion.

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