The GPMemorandum

TO: OUR FRANCHISE AND DISTRIBUTION CLIENTS AND FRIENDS

FROM: GRAY PLANT MOOTY'S FRANCHISE AND DISTRIBUTION PRACTICE GROUP

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This issue of *The GPMemorandum* focuses on topics primarily of interest to companies that use distributors and dealers rather than manage a business format franchise system. The distribution-related topics this quarter include damages issues, the application of state laws, and price discrimination.

DAMAGES

THIRD CIRCUIT AFFIRMS SUMMARY JUDGMENT IN FAVOR OF MANUFACTURER ON DISTRIBUTOR'S FRAUD CLAIMS

The United States Court of Appeals for the Third Circuit has affirmed a district court's grant of summary judgment in favor of Terex, a manufacturer of heavy equipment and parts. *TL of Fla., Inc. v. Terex Corp*, 2017 WL 3722718 (3d Cir. Aug. 29, 2017). TL, a nonexclusive distributor of Terex parts, alleged that Terex fraudulently induced it into entering into the parties' distribution agreement by failing to disclose, among other things, that TL's territory in Florida was surrounded by other authorized sellers of Terex parts called "CPEX Accounts." TL claimed that these CPEX Accounts could sell parts at a lower price because, unlike TL, they were not required to maintain a costly inventory of heavy equipment. Upon a motion by Terex, the district court held that TL had not provided sufficient evidence in support of its proffered theory of lost profit damages and, therefore, granted summary judgment in favor of Terex.

Agreeing with the district court, the Third Circuit held that TL could not sustain its burden to survive summary judgment. TL argued that it was entitled to lost profits from sales it could have made to the customers of the CPEX Accounts had they not been in competition. Unconvinced, the Third Circuit explained that there was no evidence suggesting that the CPEX Accounts sold parts within TL's territory, nor was there any dispute that the CPEX Accounts were established to serve international customers. TL also argued that because Terex sold parts to the CPEX Accounts in Florida, Terex displaced sales that otherwise would have gone to TL. The Third Circuit affirmed the lower court's determination that this second theory was "untimely" because it was a new damages theory that had not been advanced until after discovery in the case had closed. Finding no plausible theory of damages, the Third Circuit affirmed the district court's grant of summary judgment in favor of Terex.

TERMINATIONS

TEXAS FEDERAL COURT DENIES DISTRIBUTOR'S MOTION FOR SUMMARY JUDGMENT ON COMPETITIVE ACTIVITIES COUNTERCLAIM DESPITE ABSENCE OF COMPETITIVE SALES

A magistrate judge for the United States District Court for the Southern District of Texas recently denied a distributor's motion for summary judgment on a counterclaim arising from the distributor's alleged competitive activities. *PPD Enters., LLC v. Stryker Corp.*, 2017 WL 4950065 (S.D. Tex. Nov. 1, 2017). The defendants, MAKO/Stryker, make orthopedic implants. They entered into an exclusive sales representative agreement with the plaintiff, PPD, for the sale and distribution of those implants. But a little more than a year after the agreement commenced, MAKO/Stryker terminated the agreement, causing PPD to sue for breach of contract and tortious interference with PPD's business relationships. MAKO/Stryker asserted a counterclaim alleging that, "among other things," PPD had breached the agreement prior to its termination by selling a competitor's products. However, the agreement specifically acknowledged the sales at issue, and MAKO/Stryker impliedly conceded that the competitor's products were not "Competitive Products" within the meaning of the agreement. Citing a lack of evidence of prohibited competitive activities, PPD sought summary judgment on MAKO/Stryker's counterclaim.

The court denied PPD's motion. Without addressing the *Iqbal/Twombly* federal pleading standard, the court found that PPD interpreted MAKO/Stryker's counterclaim too narrowly, agreeing with MAKO/Stryker that the counterclaim included a claim that PPD had failed to use commercially reasonable efforts to sell MAKO/Stryker's implants, even though the counterclaim did not contain any explicit allegation to that effect. Ultimately, the court found the issue of commercially reasonable efforts to be a question of fact sufficient to warrant denial of PPD's motion for summary judgment.

FRANCHISOR FOUND NOT LIABLE FOR CONSTRUCTIVE TERMINATION AND BREACH OF THE COVENANT OF GOOD FAITH AND FAIR DEALING

Meanwhile, a federal court in Nevada granted summary judgment in favor of a franchisor on franchisees' claims for, among others, wrongful termination in violation of the Petroleum Marketing Practices Act ("PMPA"), breach of contract, and breach of the implied covenant of good faith and fair dealing. *Nev. W. Petroleum, LLC v. BP W. Coast Prods., LLC*, 2017 WL 4172269 (D. Nev. Sept. 20, 2017). The franchisees' claims arose when BP allegedly took various actions to force them out of their businesses, which they claimed amounted to a constructive termination of their franchise rights. In rejecting the franchisees' PMPA and breach of contract claims, the district court found that no constructive termination had occurred because BP had literally complied with the terms of the applicable franchise agreements.

The court also rejected the franchisees' claims that BP had breached the implied covenant of good faith and fair dealing by refusing to extend credit to the franchisees for fuel and requiring them to pre-pay for inventory; overcharging for the point-of-sale system; refusing to refund the franchise fee for a planned, but abandoned, location; and not allowing for an extension of time to build a planned location. In reaching its decision, the court determined that BP reasonably exercised its discretion in making these decisions because the agreements gave it sole discretion to act. For instance, the agreements allowed BP to extend credit to franchisees in its sole discretion, and here, BP extended credit until the franchisees stopped timely repaying the debt. Likewise, the agreements provided BP with sole discretion to extend deadlines for new construction, which it did beyond what was contemplated by the agreements. With respect to the franchisees' other implied covenant claims, the court found that the agreements expressly identified the cost of the point-of-sale system, and stated that the franchise fees were nonrefundable absent circumstances not present in the case before the court. In sum, the court found that no valid claim existed under the implied covenant because BP had complied with its express obligations under the franchise agreements.

STATUTE OF LIMITATIONS

WISCONSIN FEDERAL COURT USES STATE'S ANTI-FORUM SHOPPING STATUTE OF LIMITATIONS IN DISMISSING ACCIDENTAL FRANCHISE CLAIM

A Wisconsin federal court declined to reach a distributor's claims that it had entered into an accidental franchisor-franchisee relationship with a manufacturer, instead dismissing the case by applying the limitations period dictated by the parties' contract. *Faxon Sales, Inc. v. U-Line Corp.*, 2017 WL 4990617 (E.D. Wis. Oct. 31, 2017). The case arose when manufacturer U-Line unilaterally terminated its contract with distributor Faxon, ending a twenty-five-year relationship. The contract disavowed the formation of a franchise, permitted termination without cause, and required that claims arising from the agreement be brought within a year of the date the claim "arose." U-Line notified Faxon by letter dated May 30, 2016 that it was electing to terminate the parties' relationship effective June 25, 2016. Faxon brought its action against U-Line on June 22, 2017, claiming breach of its rights under various franchise, dealership, and consumer protection laws of Connecticut, Rhode Island, New York, Massachusetts, and New Hampshire.

The court first turned to Wisconsin's "borrowing statute" (Wis. Stat. § 893.07), which seeks to reduce forum shopping by requiring that in a case involving a foreign cause of action, the shortest statute of limitations, whether from Wisconsin or the foreign state, must apply. Given that the parties' contract provided for a one-year limitations period, and because it was well-settled under Wisconsin law that parties can agree upon limitations periods that are shorter than those provided by statute, the court compared the contractual limitations period to the three- and four-year limitations periods available under the statutes cited by Faxon, and determined that the one-year period contemplated by the parties' contract should apply. The court also noted that this one-year limitations period was the same as the limitations period afforded by the Wisconsin Fair Dealership Law. The court then determined that, under Wisconsin law, a claim for wrongful termination accrues upon the sending of a notice of termination, rather than on the effective date of termination. Because Faxon filed its claims more than one year after U-Line's notice of termination, the court dismissed the lawsuit as untimely filed. Faxon has now appealed the decision to the Seventh Circuit Court of Appeals.

STATE LAWS

MANUFACTURER VIOLATED STATE DEALER LAW BY FAILING TO COMPLY WITH THE STATUTE'S NOTICE AND RIGHT-TO-CURE REQUIREMENTS

A federal district court in South Dakota recently held that a truck trailer manufacturer violated the South Dakota motor vehicle dealer law by terminating and failing to renew its dealer without providing the requisite notice and opportunity to cure. *Black Hills Truck & Trailer, Inc. v. MAC Trailer Mfg., Inc.*, 2017 WL 4236546 (D.S.D. Sept. 22, 2017). Black Hills claimed it was wrongfully terminated when, less than a year after entering into a written distributor agreement, MAC sought to amend the agreement and refused to accept any orders until Black Hills signed an amended dealer agreement that circumscribed Black Hills' territory, among other modifications. Because Black Hills refused to sign the amendment, MAC informed Black Hills that it would not renew the agreement for calendar year 2014. Black Hills filed a lawsuit in response, bringing various state law claims and a claim for violation of the South Dakota motor vehicle dealer law. Both MAC and Black Hills filed cross-motions for summary judgment.

The court held that Black Hills was entitled to partial summary judgment on its claim that MAC had violated the South Dakota motor vehicle dealer law, which requires that a manufacturer provide a dealer with at least ninety days' written notice of termination or nonrenewal, that the notice state the reasons constituting good cause for the nonrenewal, and that the manufacturer allow the dealer sixty days to cure any deficiencies. MAC argued that there were several reasons amounting to good cause not to renew its agreement with Black Hills, but the court rejected that argument because MAC had not fully articulated the reasons for its decision in the nonrenewal notice. Moreover, according to the court, even if MAC's stated reasons for terminating Black Hills were true, they did not amount to good cause under the statute.

The court also denied MAC's motion for summary judgment, rejecting MAC's argument that Black Hills' claims for breach of contract, breach of the implied covenant of good faith and fair dealing, and deceit were preempted by the South Dakota motor vehicle dealer law. The court reasoned that although the dealer law contains numerous rules and regulations governing the relationship between manufacturers and dealers, it does not supplant a contract. Thus, a manufacturer could violate the dealer law without breaching the contract, and vice versa. Finally, the court rejected MAC's argument that there was insufficient evidence that Black Hills sustained any damage from the nonrenewal of the dealer agreement. It found that Black Hills presented enough evidence to form a reasonable basis for measuring its loss, including expert testimony on lost profits as discussed in Issue 220 of *The GPMemorandum*.

DISTRICT COURT GRANTS SUMMARY JUDGMENT FOR SUPPLIER, DENYING CLAIM THAT SUPPLIER UNLAWFULLY REFUSED TO GRANT TRANSFER REQUEST

The United States District Court for the Southern District of Texas has granted supplier Thermo King Corporation's motion for summary judgment, finding that Thermo King did not violate Texas' Fair Practices of Equipment Manufacturers, Distributors, Wholesalers, and Dealers Act by denying a dealer's request to transfer its dealership to Doggett Company, LLC. *Doggett Co., LLC v. Thermo King Corp.*, 2017 WL 3267796 (S.D. Tex. Aug. 1, 2017). Thermo King's basis for denying the transfer was that Doggett was affiliated with another trucking company. Doggett alleged that this rationale was not a "reasonable requirement consistently imposed by the supplier," as required by the Texas law. The court held, however, that the protections of the Texas law did not apply because the dealer had not formally submitted a request to sell its dealership to Doggett. The court found that neither the informal emails and conversations between the dealer and Thermo King—nor the letter from Doggett to Thermo King asking to buy the dealership—satisfied the plain language of the statute requiring the dealer to submit a prescribed written request to transfer. Accordingly, the court granted Thermo King's motion for summary judgment, and denied Doggett's cross-motion. The case has now been appealed to the Fifth Circuit.

DISTRIBUTOR LIMITED TO LOST PROFIT DAMAGES INCURRED DURING 90-DAY NOTICE PERIOD

The Supreme Court of Missouri recently reversed an award of lost profits as damages for an improper notice of termination of a distributorship under the Missouri Franchise Act. *Sun Aviation, Inc. v. L-3 Commc'ns Avionics*, 2017 WL 4930870 (Mo. Oct. 31, 2017). Sun Aviation, a former distributor of L-3's aircraft instrument products, sued L-3 on the grounds that L-3 had failed to provide 90 days' written notice of termination as required by the Missouri Franchise Act when it terminated Sun's distributorship. The trial court found L-3 liable and awarded Sun eighteen years of lost profits as damages.

L-3 appealed, arguing that Sun's damages should have been limited to the lost profits sustained during only the ninety-day notice period, and not a subsequent eighteen year period. The court agreed. The court initially overruled a finding of liability under Missouri's power equipment distributor laws, which require good cause for termination and repurchase of inventory, finding that L-3's products were not covered by those statutes. Next, the court observed that the plain language of the Franchise Act connotes a causal connection between the particular statutory violation and the injury. The court then reasoned that damages are intended to compensate a plaintiff whose expectations have been frustrated by failure to give the requisite notice. The court held that damages must be limited to those sustained due to reliance on the expectation that the relationship would continue for at least a ninety-day period after notice of termination, and the costs of filing suit. The court further reasoned that its decision was supported by the fact that under the Franchise Act, a franchise may be lawfully terminated so long as the requisite notice is given. Accordingly, the court held that Sun's damages were limited to those sustained as a result of the failure to provide ninety days' notice, and nothing more.

ANTITRUST

ROBINSON-PATMAN ACT CLAIM SURVIVES SUMMARY JUDGMENT IN PRICE DISCRIMINATION SUIT AGAINST MAKER OF 5-HOUR ENERGY

A price discrimination suit against the maker of 5-hour Energy is heading to trial after a federal court in California denied cross-motions for summary judgment. In *ABC Distributing, Inc. v. Living Essentials, LLC*, 2017 WL 3838443 (N.D. Cal. Sept. 1, 2017), several Los Angeles area wholesalers brought suit against Living Essentials for allegedly offering 5-hour Energy drinks to Costco at lower prices than it did to the plaintiffs, in violation of the Robinson-Patman Act and California's unfair competition laws. Because a price discrimination claim requires competitive injury, Living Essentials argued that the case should be dismissed on the grounds that Costco was a club store that was never in actual competition with the wholesaler plaintiffs for the same customers. Conversely, the plaintiffs argued that they operated at the same level of the distribution chain as Costco, and that their geographic proximity demonstrated competition as a matter of law. The court rejected both arguments. Although Living Essentials differentiated Costco's business model from that of the plaintiffs, circumstantial evidence demonstrated that at least some Living Essentials employees actually did believe that Costco was in direct competition with the plaintiffs for the same customer dollars, and this dispute of fact precluded summary judgment for either side.

The court also ruled that summary judgment was improper because of disputed facts regarding the price difference paid by the plaintiffs and Costco. Although the plaintiffs (for the most part) did not attempt to show that they actually lost sales to Costco, case law permits an inference of competitive injury where a favored purchaser has received a significant price reduction for a substantial period of time. It was undisputed that Costco received some level of price reduction over the relevant time period, but Living Essentials argued that this was in part because of functional discounts that related to Costco's different status in the supply chain. Because of the dispute as to whether Costco held a distinct or overlapping status in the supply chain, the court could not determine on summary judgment whether Costco's service provided functional benefits to Living Essentials that would justify such discounts. The court did note, however, that rebates offered to Costco customers and payments for Costco advertising promotions, to the extent they exceeded the actual promotional value enjoyed by Living Essentials, should be factored into the net price calculation for Costco. Whether that difference in net price was "significant" or *de minimis*, and whether it was otherwise justified by functional benefits provided by Costco, will ultimately be determined by a jury.

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