The GPMemorandum

TO: OUR FRANCHISE CLIENTS AND FRIENDS

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

Quentin R. Wittrock, Editor of The GPMemorandum

Iris F. Rosario, Assistant Editor

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This issue of The GPMemorandum focuses on topics of interest to companies that use distributors and dealers rather than manage a business format franchise system. We begin with a report on legislation, followed by cases on page 2.

LEGISLATION AND RULEMAKING

BILL TO RENEW VERTICAL PRICE-FIXING BAN MAY HEAD TO FULL VOTE IN THE U.S. HOUSE OF REPRESENTATIVES

Congress is considering overruling the United States Supreme Court’s decision in Leegin Creative Leather Products, Inc. v. PSKS, Inc., in which the court overturned near century-old precedent and held that manufacturers could set minimum price standards for retailers if they encouraged competition. Some have believed that by eliminating the threat of per se liability, Leegin provided suppliers and franchisors with at least limited comfort in setting minimum resale prices for their dealers and franchisees. But even this may be short-lived. On January 13, 2010, the Discount Pricing Consumer Protection Act of 2009 (H.R. 3190) cleared the judiciary committee of the House of Representatives and could head to the House for a full vote. The bill states: “Any agreement setting a price below which a product or service cannot be sold by a retailer, wholesaler, or distributor shall violate section 1 of the Sherman Act.”

A related bill (S. 148) was introduced in the Senate on January 6, 2010, by Senator Kohl (D-Wis.) and was referred to the Senate’s judiciary committee for consideration. The purpose of the Senate bill is to “correct the Supreme Court’s mistaken interpretation of the Sherman Act in the Leegin decision.”
NEW JERSEY EXPANDS ITS FRANCHISE PRACTICES ACT

New Jersey recently expanded the scope of its Franchise Practices Act to include persons or entities who do not make a majority of their sales directly to consumers and who have “an office or warehouse from which franchisee personnel visit or call upon customers or from which the franchisor’s goods are delivered to customers.” Before, a franchisee was entitled to the Act’s protections only if it maintained “a fixed geographical location at which the franchisee offers and displays for sale the franchisor’s goods or offers for sale and sells the franchisor’s services.” Under the new amendment, franchisors need good cause to terminate, cancel, or fail to renew agreements with this new class of franchisees.

RECENT CASES

Here are summaries of recent court decisions of interest to companies that sell through dealers and distributors:

ANTITRUST

THIRD CIRCUIT CONFIRMS NARROW SCOPE OF ROBINSON-PATMAN ACT

Feeser’s, Inc. v. Michael Foods, Inc., 2010 U.S. App. LEXIS (3d Cir. Jan 7, 2010), involved alleged price discrimination under the Robinson-Patman Act (RPA). Ruling against the plaintiff, the Third Circuit construed strictly the RPA’s requirement that, to be actionable, a seller must discriminate in price between “competing purchasers.” As reported in Issue No. 121 of The GPMemorandum (July 2009), the price discrimination claim arose in the supply of food products to institutional food service providers, such as schools and hospitals. The defendant, Michael Foods, a large manufacturer of egg and potato products, utilized a pricing structure that resulted in drastic product discounts to Sodexo, a multinational food management company (and a co-defendant), as compared to the prices charged to plaintiff Feeser’s, a distributor operating on a regional level and selling to self-operators of food service businesses. As we previously reported, the district court found that institutions routinely switch between acting as self-operators and utilizing the services of food management companies. Thus, the district court found, Sodexo and Feeser’s competed for “the same portion of an institution’s food service budget,” and price discrimination between them violated the RPA.

The Third Circuit disagreed. Relying on its previous rulings as well as an admonition from the Supreme Court to construe RPA claims narrowly, the appellate court found that the relevant “sale” of food products, for purposes of the RPA “competing purchaser” analysis, does not occur until after an institution has chosen whether to
engage a food management company or to act as a self-operator. Thus, Sodexo and Feeser’s are never in direct competition for the institution’s food product dollars because, by the time a sale of food products is made to the institution, the customer has already decided whether to buy from a distributor (like Feeser’s) or through a food management company (like Sodexo). The district court’s factual finding that institutions routinely switch between using food management companies and self-operating was of no importance, given the strict requirement that two competitors be in actual competition with one another at the time of sale.

TERMINATIONS

SUPREME COURT HEARS ORAL ARGUMENT ON PMPA CLAIMS FOR CONSTRUCTIVE TERMINATION AND NONRENEWAL

In a case that could have broad implications for franchisors, the United States Supreme Court heard oral argument on cross appeals involving two related questions arising under the Petroleum Marketing Practices Act (PMPA): (1) whether a gas station franchisee who continues to operate the franchise using the franchisor’s marks may bring a valid claim for “constructive termination,” and (2) whether executing a renewal franchise agreement “under protest” precludes a claim for “constructive nonrenewal.” The consolidated petitions, Mac’s Shell Service, Inc. v. Shell Oil Products Co., No. 08-240, and Shell Oil Products Co. v. Mac’s Shell Service, Inc., No. 08-372, will result in the first Supreme Court decision to interpret the PMPA.

The plaintiffs had Shell franchise agreements that specified the monthly rent for their property leases. Shell, however, since 1982 had offered a variable rent program to its franchisees that reduced the monthly rent payment depending on a franchisee’s volume of gasoline sales. According to the plaintiff franchisees, Shell promised that this program would always be available even though the written terms of the program allowed Shell to cancel after giving notice. Thereafter, Motiva Enterprises, LLC, a joint venture between Shell and Texaco, notified Shell franchisees that the “volume-based” variable rent program would be discontinued. The franchisees sued, claiming that Shell’s assignment of the franchise agreements to Motiva was a “constructive” termination and nonrenewal of their franchise agreements because Motiva’s modification to their lease terms resulted in a substantial increase to the rent, which was driving the franchisees out of business. Shell and Motiva argued, however, that termination and nonrenewal claims cannot be brought under the PMPA unless an actual cessation of the franchise has occurred. The jury awarded $3.3 million in damages for termination of the franchise agreements and for nonrenewal.

The Supreme Court will have an opportunity to resolve a split among the circuits on whether constructive termination claims are recognized by the PMPA. In an amicus
brief, the United States warned that accepting the franchisees’ broad interpretation of
the PMPA would “federalize” all disputes between oil companies and their franchisees.
Whatever the result, the Supreme Court decision could be an important one for both
franchisors and franchisees, possibly even outside the gas station context.

KENTUCKY FEDERAL COURT GRANTS SUPPLIER SUMMARY JUDGMENT
DISMISSING DEALER’S CLAIMS

A Kentucky federal court has granted a motion for summary judgment on a dealer’s
claims for breach of contract and tortious interference in Western Kentucky Coca-Cola
Western alleged wrongful termination of its distributor agreement by Red Bull,
contending that it did not receive an opportunity to cure prior to Red Bull terminating
the agreement. It also alleged that Royal Crown Bottling Company had tortiously
interfered with its contract with Red Bull when Royal Crown began distributing Red Bull
products. The court rejected the claim because Western failed to show that the parties
had agreed to a cure period. The court also rejected the claim of tortious interference,
because the termination itself was lawful.

LICENSE AGREEMENT DID NOT CONSTITUTE A FRANCHISE;
LICENSOR’S REQUEST FOR INJUNCTIVE RELIEF IS DENIED

In Englert, Inc. v. LeafGuard USA, Inc., WL 5031309 (D.S.C. Dec. 14, 2009), a South
Carolina federal court held that the parties’ license agreement for the distribution of
LeafGuard brand “leaf rejecting” rain gutters did not constitute a franchise agreement.
The dispute arose when Englert, the licensor, terminated its license agreement with
LeafGuard USA for nonpayment of royalties. Englert then sued LeafGuard for the unpaid
royalties, for an injunction seeking the return of a gutter-fabricating machine that the
license agreement provided would be sold back to Englert if the agreement was
terminated, and for the discontinuance of use of its trademarks. LeafGuard USA filed
numerous counterclaims and a motion for summary judgment asserting that the
parties’ agreement created a franchise.

The court denied LeafGuard USA’s summary judgment motion. Englert did not exert
sufficient control over LeafGuard’s business to create a franchise because it controlled
only one of the licensee’s multiple product lines. In addition, the purchase price paid for
the gutter-fabricating machine was not a franchise fee. The court also denied Englert’s
motion to enjoin the licensee’s continued use of the gutter-fabricating machine and its
trademarks. There was no irreparable harm given that the licensee had been using the
trademarks in the eight years the parties were litigating their claims, and most of the
issues raised in the injunction motion revolved around the proper termination of the
agreement, which soon would be addressed at trial.
CLAIMS AGAINST MAJOR DISTRIBUTOR SURVIVE MOTION TO DISMISS

In In re U.S. Foodservice Inc. Pricing Litigation, 2009 WL 5064468 (D. Conn. Dec. 15, 2009), a Connecticut federal court denied U.S. Foodservice’s (USF’s) motion to dismiss a RICO claim filed by plaintiffs Frankie’s Franchise System and others. The plaintiffs alleged that USF had created a number of shell companies to procure products, which then were sold to USF at inflated prices. In turn, USF allegedly would pass on the inflated prices to plaintiffs, thus receiving a higher profit margin than it would have otherwise received under the parties’ contracts.

USF contended that plaintiffs’ claim failed because it was not properly pled or did not state a claim, and because certain claims of the plaintiffs lacked standing. The court denied USF’s motion, finding that plaintiffs had properly pled the existence of a RICO enterprise under the statute. The court also found that plaintiffs had properly alleged wire and mail fraud against USF, by alleging that USF had sent its fraudulent invoices through the mail. Finally, the court rejected USF’s claim that two of the plaintiffs lacked standing because they were not parties to cost-plus contracts with USF. The court found that plaintiffs had alleged that cost-plus purchases had been made, which was sufficient to survive the motion to dismiss.

AUTO MANUFACTURER’S REQUEST FOR SPECIFIC PERFORMANCE REJECTED

In Mercedes-Benz USA v. Concours Motors, 2010 WL 55473 (E.D. Wis. Jan 4, 2010), a Wisconsin federal court denied Mercedes-Benz’s motion for partial summary judgment on its breach of contract claim against its dealer, Concours. At issue was the parties’ oral agreement to allow the dealer to construct a new facility. Because of low sales at the dealership, MB and Concours agreed to relocate the dealership to another location. When Concours started constructing a new facility but then stopped, MB sued claiming promissory estoppel and breach of contract. The court refused to grant specific performance, as to do so would require the court to imply details of location, construction, cost, and deadlines related to the new facility, as well as to serve as an ongoing referee of the parties’ relationship.

The court, however, granted MB’s motion for summary judgment on Concours’ various counterclaims. Among other things, the court rejected Concours’ claims that MB had violated the Wisconsin Motor Vehicle Dealer Law and that MB unfairly cancelled the parties’ agreement.
PLAINTIFF’S CLAIM THAT AUTO MANUFACTURER PROMISED DEALERSHIP IS REJECTED BY THE COURT

In Luther v. Kia Motors Am., Inc., 2009 WL 4906878 (W.D. Pa. Dec. 18, 2009), the court granted summary judgment to Kia on a rejected applicant’s claim that he had been promised a dealership. The applicant claimed that a Kia representative told him he had been approved at the regional level, and that in the past, those approved at that level were approved by the ultimate national-level decision makers. The applicant claimed that this constituted an oral contract. The court disagreed, holding that the conversation did not amount to an oral contract, that the representative did not have the authority to bind the company, and that the applicant had not suffered any damages. It also held that the integration clause contained in the application, which expressly noted that only the written execution of a franchise agreement would constitute approval of the application, foreclosed the claim.

CHOICE OF FORUM/VENUE

WISCONSIN COURT DISMISSES CLAIM THAT FORUM SELECTION CLAUSE VIOLATES THE WISCONSIN FRANCHISE INVESTMENT LAW

In Trakloc Midwest LLC v. Trakloc Int’l, LLC, 2009 WL 4878578 (Wis. App. Dec. 17, 2009), the Wisconsin Court of Appeals affirmed the dismissal for improper venue a case brought by technology distributor Trakloc Midwest against manufacturer Pacific Rollforming. Midwest argued that it had a franchise relationship with Pacific and that the forum-selection clauses in the contracts violated the Wisconsin Franchise Investment Law (WFIL). Alternatively, Midwest argued that using different forum selection clauses (Alaska and California) in two separate agreements created an unenforceable ambiguity.

After pointing out that there was scant case law finding forum selection clauses a per se violation of the WFIL, the court concluded that “Midwest [did] not carry its burden of demonstrating that it is entitled to whatever protection it might be afforded as a franchisee under the WFIL because it has not proven as a matter of law that the . . . [two] Agreement[s] create a franchise under [WFIL].” On the issue of ambiguity, the court found “no apparent reason why disputes related to the [first] Agreement cannot be litigated in California, as that agreement plainly requires, and similarly, there is no apparent reason why disputes related to the [second] Agreement cannot be litigated in Alaska, as that agreement plainly provides.” The dismissal of the case was affirmed.
STATE LAWS

WISCONSIN COURT ALLOWS TERMINATED DISTRIBUTOR’S CLAIMS TO PROCEED UNDER WFDL

Last week, a federal district court judge in Wisconsin issued a comprehensive opinion that elucidates what a terminated distributor or dealer must show to survive summary judgment under the Wisconsin Fair Dealership Law. The case is Brio Corp. v. Meccano S.N., 2010 U.S. Dist. LEXIS 11711 (E.D. Wis. Feb. 10, 2010). In denying summary judgment to defendant Meccano, which is the French maker of the “Erector” brand of toys, the court ultimately determined that fact questions precluded summary judgment. But the length and detail of the court’s opinion could recommend it as a helpful guide in future cases.

Two key components of the WFDL, and thus the court’s opinion, are: (1) whether there was a “community of interest” between the defendant and plaintiff Brio (which had exclusive distribution rights in the United States); and (2) whether Brio was “situated in” Wisconsin such that the WFDL applied. On the first point, the court found it particularly important that Brio was an exclusive distributor and was prohibited from selling competitive products. These facts and others were deemed sufficient for the court to find Meccano had Brio sufficiently “over the barrel” at least to create a triable issue on the community of interest element. The “situated in” Wisconsin issue was even stronger for the plaintiff. Although Brio made less than five percent of its overall sales in Wisconsin, it did have facilities and employees in the state, and was a corporation formed under Wisconsin law.
Minneapolis, MN Office

John W. Fitzgerald, cochair (612.632.3064)  
Megan L. Anderson (612.632.3004)  
Wade T. Anderson (612.632.3005)  
Phillip W. Bohl (612.632.3019)  
Jennifer C. Debrow (612.632.3357)  
Elizabeth S. Dillon (612.632.3284)  
* Collin B. Foulds (612.632.3388)  
* Michael R. Gray (612.632.3078)  
Laura J. Hein (612.632.3097)  
* Kelly W. Hoversten (612.632.3203)  
Franklin C. Jesse, Jr. (612.632.3205)  
Cheryl L. Johnson (612.632.3271)  
* Jeremy L. Johnson (612.632.3035)  
Gaylen L. Knack (612.632.3217)  
Kirk W. Reilly, cochair (612.632.3305)  
* Kate G. Nilan (612.632.3419)  
Craig P. Miller (612.632.3258)  
Bruce W. Mooty (612.632.3333)  
John W. Mooty (612.632.3200)  
* Kevin J. Moran (612.632.3269)  
Max J. Schott II (612.632.3327)  
Daniel R. Shulman (612.632.3335)  
* Jason J. Stover (612.632.3348)  
Michael P. Sullivan, Sr. (612.632.3351)  
Michael P. Sullivan, Jr. (612.632.3350)  
* Henry Wang (612.632.3370)  
Lori L. Wiese-Parks (612.632.3375)  
* Quentin R. Wittrock (612.632.3382)

Washington, DC Office

* Robert Zisk, cochair (202.295.2202)  
* Arthur I. Cantor (202.295.2227)  
* Jimmy Chatsuthiphan (202.295.2217)  
* Ashley M. Ewald (202.294.2221)  
* Jeffrey L. Karlin (202.295.2207)  
* Peter J. Klarfeld (202.295.2226)  
* Iris F. Rosario (202.295.2204)  
* Stephen J. Vaughan (202.295.2208)  
* Katherine L. Wallman (202.295.2223)  
* David E. Worthen (202.295.2203)  
* Eric L. Yaffe (202.295.2222)  
* Carl Zwisler (202.295.2225)

* Wrote or edited articles for this issue.

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GRAY PLANT MOOTY

500 IDS Center  
80 South Eighth Street  
Minneapolis, MN 55402-3796  
Phone: 612.632.3000  
Fax: 612.632.4444

Suite 1111, The Watergate  
2600 Virginia Avenue, N.W.  
Washington, DC 20037-1905  
Phone: 202.295.2200  
Fax: 202.295.2250

franchise@gpmlaw.com

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