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FRANCHISE LAW

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I. INTRODUCTION

THIS article provides an update of case law and legislative efforts that had, or will have, a significant impact on franchise and dealership law in Texas and in the Fifth Circuit. Of note, the biggest development in franchising occurred after the Survey period for this article, namely a January 23, 2007, announcement that the revised Federal Franchise Rule will be effective July 1, 2007, with mandatory application on July 1, 2008. In addition, the Federal Trade Commission (“FTC”) issued a Notice of Public Rulemaking on a proposed trade-regulation rule for business opportunities. Both are discussed below.

With respect to case law, the Texas Supreme Court overturned a jury’s finding that a soft drink company committed certain antitrust violations in connection with its marketing agreements with retailers. Also, the Fifth Circuit and the Western District of Texas upheld arbitration clauses and forum-selection clauses in franchise agreements further strengthening the general consensus in Texas that contractual provisions regarding dispute resolution will be enforced. Finally, the United States Supreme Court effectively limited the scope of price discrimination liability in a case where a truck manufacturer was accused of violating the Robinson-

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Patman Act by providing more favorable discounts, or price concessions, to some of its regional dealers than to others.

II. FRANCHISE BASICS

A. AMENDED FTC FRANCHISE RULE RELEASED—FINALLY!

Franchise disclosure laws require franchisors to disclose to prospective franchisees certain items about the franchise system.¹ The guidelines set forth by the North American Securities Administrators Association (“NASAA”) require franchisors to provide specific information about their officers, the franchise system, the relationship between the franchisor and the franchisee, and the documents the franchisee will be required to sign.² This information is contained in a document called the Uniform Franchise Offering Circular (“UFOC”). The FTC has its own form of disclosure format under the Franchise Rule³ but has accepted the UFOC disclosure format in lieu of its own.⁴

The Franchise Rule was adopted in 1978. In 1995, however, the FTC began reviewing the Franchise Rule to determine whether changes were necessary. If it was determined that changes were necessary, the FTC said it would revise the Franchise Rule. In 1997, the FTC published an Advanced Notice of Proposed Rulemaking⁵ and, two years later, published a Notice of Proposed Rulemaking,⁶ containing the first draft of proposed changes to the Franchise Rule.

After a prolonged gestation and comment period, the FTC finally published its Amended Franchising Rule (the “Amended Rule”) on January 23, 2007.⁷ The new disclosures *may* be used effective July 1, 2007, and they *must* be used for all franchises offered or sold after July 1, 2008.⁸ The Amended Rule prescribes a disclosure format, which largely mirrors the UFOC format, and modifies it in certain places by adding new disclosures. The FTC plans to publish compliance guidelines, which will use

1. RUPERT M. BARKOFF & ANDREW C. SELDEN, *FUNDAMENTALS OF FRANCHISING* 121-22 (ABA Publishing 2004).

2. *Id.* at 98-99.

3. 16 C.F.R. § 436.1 (2004).

4. Rupert M. Barkoff, Mary Beth Brody & Lane Fisher, *The Basics of Disclosure*, IFA 37th Annual Legal Symposium, Tab 8, ii-iii (May 23-25, 2004); FTC Summary of the Franchise Rule, Paragraph F., *reprinted in* CCH Business Franchise Guide Paragraph 6027.

5. Trade Regulation Rule on Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures, 62 Fed. Reg. 9,115 (1997) (the “Current Rule”).

6. Franchise Rule, 64 Fed. Reg. 57,294 (Oct. 22, 1999).

7. Portions of this discussion about the Amended Rule were previously published by the Haynes and Boone Franchise and Distribution Group on Haynes and Boone’s website. See Carl E. Zwisler and Jan S. Gilbert, *Amended FTC Rule Released Yesterday* (Jan. 24, 2007) http://www.haynesboone.com/FILES/tbl_s12PublicationsHotTopics/publicationPDF60/1855/Amended%20FTC%20Rule.pdf. The “Amended Rule” was published by the FTC as a part of a 398 page Report <http://www.ftc.gov/os/2007/01/R511003FranchiseRuleFRNotice.pdf> (the “Report”).

8. Report, *supra* note 7, at 1.

the current UFOC guidelines as their point of departure.⁹

Franchisors will favorably receive many aspects of the Amended Rule. Requirements related to the delivery of disclosures will be welcomed by all, while exemptions for high-investment franchises and for sales to certain high net worth franchisees will eliminate compliance obligations altogether for some franchisors. Franchisors will be allowed to use electronic means to deliver disclosure documents. Financial Performance Representations (*i.e.*, earnings claims) remain optional, not mandatory. New franchisors may continue to phase into the financial audit requirement if they have not previously had audits.

The Amended Rule has addressed many of the concerns raised by the franchising community since the Revised Proposed Rule was issued in 1999. For example, thresholds for large-investment franchises have been lowered, and the number of franchisor employees, who are entitled to qualify for a new exemption, have been expanded. Franchisee advocates will appreciate added prohibitions concerning the use of merger and integration clauses to deflect liability for disclosures made in offering circulars. They also will like several new disclosure requirements, and they should like being able to negotiate amendments to franchise agreements at a closing without being subject to a five business-day delay.

1. *New Exemptions*

The Amended Rule creates several new exclusions and exemptions, including:

1. Sales of franchises to be located outside the United States;¹⁰
2. Franchises involving investments of at least \$1 million (excluding unimproved land and amounts financed by the franchisor). This initial investment would be calculated to include multi-unit development commitments and the value of a business, which is converted to a franchise through an affiliation franchise agreement;¹¹
3. Investments by high net worth, experienced franchisees, *i.e.*, those with five years of business experience and a net worth of at least \$5 million;¹² and
4. Sales to certain officers, owners, and managers of franchisors.¹³

2. *No More Broker Disclosures or Venue/Law Choice Risk Factors*

Franchisors that use franchise brokers will find that their burdens are relaxed considerably, as disclosures about franchise brokers are no longer required.¹⁴ The UFOC's required use of "risk factors" based upon a franchisor's choice of law or venue for disputes no longer will be required

9. *Id.* at 15-16.

10. See Amended Rule § 436.2.

11. Amended Rule § 436.8(5)(i).

12. Amended Rule § 436.8(5)(ii).

13. Amended Rule § 436.8(6).

14. Report, *supra* note 7, at 90.

either.¹⁵

2. *Timing and Delivery of Disclosures Simplified*

The rules for when disclosures must be given to prospective franchisees also provide a welcome change. The duty to provide a disclosure at the "first personal meeting" has been deleted, and the cumbersome ten business day counting problem has been eliminated. Now, disclosures must be provided fourteen calendar days before the franchisee makes a payment to the franchisor or an affiliate in connection with a franchise purchase, or fourteen days before the franchisee signs a binding agreement with the franchisor.¹⁶ However, if a prospective franchisee "reasonably requests" a disclosure document earlier than fourteen days before the agreement is signed or money is paid, he is entitled to receive it earlier.¹⁷ Completed agreements must be provided to prospects seven days before signing, only if the franchisor has unilaterally made a change to the standard form agreement provided with the disclosure document.¹⁸

Disclosure documents may be delivered in electronic form without any of the accompanying notices required in earlier drafts of the Proposed Rule.¹⁹ The Amended Rule even creates a presumption that paper or tangible copies of a disclosure are received three days after they have been mailed with the proper postage and address.²⁰

4. *New Disclosure Highlights*

The new disclosure requirements include:

1. Information about the franchisor's parent in items 1, 3, and 4.²¹ Financial statements of the parent must be included if the parent will provide services to franchisees or if a parent guarantees obligations of the franchisor;²²
2. Information about franchisor-initiated litigation against franchisees. Disclosure must cover the franchisor's previous fiscal year only;²³
3. Information about the franchisor's use of confidentiality clauses;²⁴
4. Information about the existence of "trademark-specific franchisee associations;"²⁵
5. Franchisee turnover information will be presented in a way which will substantially reduce the likelihood of "double counting"

15. *Id.* at 14.

16. Amended Rule § 436.2(a).

17. Amended Rule § 436.9(e).

18. Amended Rule § 436.2(b).

19. Amended Rule § 436.2(c).

20. Amended Rule § 436.2(c)(3).

21. Amended Rule §§ 436.5(a), (c), (d).

22. Amended Rule § 436.5(u)(1)(v).

23. Amended Rule § 436.5(c)(1).

24. Amended Rule § 436.5(t)(7).

25. Amended Rule § 436.5(t)(8).

transfers and terminations;²⁶ and

6. Annual updates to disclosures are not required until 120 days after a franchisor's fiscal year end.²⁷

5. *New Prohibitions*

The Amended Rule contains several new prohibitions. Franchisors may no longer require a prospective franchisee to waive reliance on any representation made in a disclosure document, its exhibits, or its amendments.²⁸ The use of "shills" to promote franchises also is prohibited.²⁹

6. *Conclusion*

These highlights of changes to the Rule are just that. The Amended Rule is part of a 398-page document, which contains the details with which franchisors and their lawyers will need to become familiar to meet the new requirements. Still unknown is exactly how quickly states with franchise registration laws will be able to adapt to the changes and the extent to which they will require additional information.

B. NEW FTC BUSINESS OPPORTUNITIES RULE

On April 12, 2006, the FTC issued a Notice of Proposed Rulemaking ("NPR") seeking public comment on a proposed trade-regulation rule for business opportunities. The NPR sets forth certain disclosures that business opportunity sellers would be required to provide to prospective purchasers to assist in creating an informed purchase decision. In addition to these disclosure requirements, the proposed rule would prohibit common deceptive business opportunity sales practices.³⁰

Among other things, the new business opportunities rule would require a one-page disclosure covering five specific points: (1) whether or not sellers make earnings claims, and if so, whether sellers are required to provide substantiation and make additional disclosures; (2) a list of any criminal or civil actions against the seller or its representatives that involve fraud, misrepresentations, securities, or deceptive or unfair trade practices; (3) whether the seller has in place cancellation or refund policies and such policies' terms; (4) the total number of purchasers in the past two years and the number of those purchasers seeking a refund or cancellation in that time period; and (5) a list of business opportunity seller references.³¹

In addition to the required disclosures, the proposed rule would prohibit sellers of business opportunities from misrepresenting a laundry list

26. Amended Rule § 436.5(t)(2).

27. Amended Rule § 436.7(a).

28. Amended Rule § 436.9(h).

29. See Amended Rule § 436.9(b).

30. Business Opportunity Rule; Notice of Proposed Rulemaking, 70 Fed. Reg. 19,054 (2006) (to be codified at 16 C.F.R. pt. 437).

31. *Id.* at 19,058.

of points, including: (1) earnings; (2) costs or the efficacy, nature, or central characteristics of the business opportunity or the goods and services sold to the purchaser as part of the business opportunity; (3) cancellation or refund policies; (4) promised assistance; (5) the calculation and distribution of commissions, bonuses, incentives, premiums, or other payments from the seller; (6) the likelihood of finding locations for equipment or accounts for services; (7) a business opportunity as an offer of employment; (8) territorial exclusivity or more limited territorial protections; (9) endorsements; and (10) skills as references.³² Further, the proposed rule would prohibit business opportunity sellers from failing to make promised refunds, as well as assigning "to any purchaser a purported exclusive territory that, in fact, encompasses the same or overlapping areas already assigned to another purchaser."³³

While the proposed business opportunity rule would streamline disclosures that currently must conform with the Franchise Rule, the scope of the proposed business opportunity rule is extremely broad since it has no minimum cost threshold, no inventory exemption, and no limit on scope based on the type of assistance promised as part of the offer. Further, the scope is not limited to transactions where the purchaser of the opportunity sells goods or services directly to end-users other than the business opportunity seller.³⁴

III. PROCEDURE

A. JURISDICTION

At times, corporate leaders seek to shield themselves from jurisdiction in a foreign state when they act in their corporate capacity. A corporate officer, however, may be subject to specific jurisdiction, even in a foreign state, based on their alleged acts or omissions that give rise to tort claims. In *Lewis v. Indian Springs Land Corporation ("ISLC")*,³⁵ plaintiff Thomas E. Lewis, a Florida resident, challenged a trial court's order overruling his special appearance. In particular, Lewis argued that: (1) he was a Florida resident; (2) he served as President of ISLC, a Nevada corporation; (3) the corporation received certain contested funds in Florida; and (4) he was acting in his capacity as president of ISLC when he issued checks from a Florida bank account to ISLC's acknowledged creditors, some of whom lived in Texas.³⁶

Several corporate entities and shareholders, which Lewis served as a partner, venture, or shareholder, initiated a lawsuit against Lewis regarding his distribution of ISLC funds. The transactions between the parties related to the acquisition and development of a tract of residential real estate location in Los Angeles County, California. Specifically, on Au-

32. *Id.*

33. *Id.*

34. See 71 Fed. Reg. 19,054.

35. 175 S.W.3d 906 (Tex. App.—Dallas 2005, no pet. h.).

36. *Id.* at 912.

gust 12, 2004, Lewis, acting as ISLC's President, negotiated and obtained an agreement whereby Toll Brothers, Inc. made a partial payment on a promissory note payable to ISLC of over \$9 million. Toll Brothers made this payment to ISLC's Miami bank account, on which Lewis was a signatory. Lewis then distributed over \$3 million of that money into his personal Florida bank account and sent six checks to Dallas—payable to two Texas residents and a Texas corporation. The two Texas residents claimed they had no knowledge that Lewis negotiated these prepayments until their checks were received. Upon receipt, these Texas residents notified Lewis that he had improperly distributed these funds. They claimed that Lewis deliberately ignored other debts that should have been paid, in particular, certain alleged obligations to repay advances made by a Texas resident for the development of the California property.³⁷

The Dallas Court of Appeals explained that the Texas long-arm statute permits Texas courts to exercise jurisdiction over a nonresident defendant that does business in Texas.³⁸ The long-arm statute defines “doing business” as: (1) contracting by mail or otherwise with a Texas resident with performance either in whole or in part in Texas; (2) commission of a tort in whole or in part in Texas; (3) recruitment of Texas residents directly or through an intermediary located in Texas; or (4) performance of any other act that may constitute doing business.³⁹ The court of appeals concluded that “the broad language of the long-arm statute permits Texas courts to exercise personal jurisdiction ‘as far as the federal constitutional requirements of due process will permit.’”⁴⁰ The court of appeals further explained that the “touchstone” of jurisdictional due-process analysis is “purposeful availment.”⁴¹

The court of appeals noted that the Texas Supreme Court recently addressed the proper application of the concept of “purposeful availment” outlining three important aspects to be considered:⁴²

First, it is only the defendant's contacts with the forum that count: purposeful availment “ensures that a defendant will not be haled into a jurisdiction solely as a result of . . . the unilateral activity of another party or a third person.” Second, the acts relied upon must be “purposeful” rather than “random, isolated or fortuitous.” Third, a defendant must seek some benefit, advantage, or profit by “availing” itself of the jurisdiction.⁴³

The court of appeals pointed out that the *Michiana* court held that a non-resident may purposefully avoid a jurisdiction, rather than purposefully

37. *Id.* at 909-12.

38. *Id.* at 913; TEX. CIV. PRAC. & REM. CODE ANN. § 17.041-.045 (Vernon 1997).

39. § 17.042.

40. *Lewis*, 175 S.W.3d at 913 (quoting *id.*).

41. *Id.*

42. *Id.* at 913-14.

43. *Id.* at 914 (quoting *Michiana Easy Livin' Country, Inc. v. Holten*, 168 S.W.3d 777, 785 (Tex. 2005)) (citations omitted).

avail itself of a jurisdiction, by structuring its transactions so as neither to profit from the forum's law nor be subject to its jurisdiction.⁴⁴

The court of appeals held that Lewis had purposefully availed himself of the laws of Texas.⁴⁵ The record reflects that Lewis had extensive contacts, which he voluntarily made with the forum. For the court of appeals' analysis, these contacts began because of Lewis's involvement in developing the California property and culminated with the contested disbursement of ISLC's funds. Lewis was a part of several business entities, organized under Texas law and based in Texas, with Texas citizens. Moreover, Lewis claimed entitlement to millions of dollars from promissory notes made payable to his order by ISLC. Importantly, as the court of appeals noted, at least one of those promissory notes, which was governed by Texas law, was executed by ISLC and made payable in Dallas, Texas, in the principal amount of \$2.2 million to its payees, including Lewis.⁴⁶

In addition, the court of appeals observed that over a period of five years, Lewis traveled to Texas at least five times to negotiate and manage his Texas-based business interests involved in the underlying suit, and he communicated extensively regarding those interests in writing, electronically, and by telephone with his Texas business associates.⁴⁷ The court of appeals also addressed Lewis's argument that his contacts were not in his individual capacity and, therefore, might not be used as a basis for the exercise of personal jurisdiction (*i.e.*, the fiduciary-shield doctrine).⁴⁸ The court of appeals, however, held that the Texas Supreme Court had never specifically recognized the fiduciary-shield doctrine and that Texas Court of Appeals had applied the doctrine only on questions of whether general jurisdiction existed over nonresidents.⁴⁹ "Further, corporate officers are not shielded from the exercise of specific jurisdiction for fraudulent or tortious acts for which they may be liable."⁵⁰ Thus, the court of appeals could not conclude that Lewis's contacts with Texas did not include those made in his individual capacity.⁵¹

Finally, the court of appeals held that based on the quality, nature, and extent of Lewis's activity in Texas, he should expect to be called into Texas courts.⁵² As such, the exercise of specific jurisdiction over Lewis by a Texas court did not offend traditional notions of fair play and substan-

44. *Id.* at 914 (citing *Michiana*, 168 S.W.3d at 790).

45. *Id.* at 918.

46. *Id.* at 916.

47. *Id.*

48. *Id.* at 916-17.

49. *Id.* at 917 (citing *Siskind v. Villa Found. For Educ., Inc.*, 642 S.W.2d 434, 438 (Tex. 1982); *Morris v. Kohls-York*, 164 S.W.3d 686 (Tex. App.—Austin 2005, pet. dismissed); *SITQ E.U., Inc. v. Reata Rests., Inc.*, 111 S.W.3d 638, 651 (Tex. App.—Fort Worth 2003, pet. denied)).

50. *Lewis*, 175 S.W.3d at 917 (citing *Calder v. Jones*, 465 U.S. 783, 790 (1984); *SITQ*, 111 S.W.3d at 651; *Tuscano v. Osterberg*, 82 S.W.3d 457, 467-68 (Tex. App.—El Paso 2002, no pet.)).

51. *Lewis*, 175 S.W.3d at 917.

52. *Id.* at 918.

tial justice. Accordingly, the trial court's implied findings were legally and factually sufficient to exercise personal jurisdiction over Lewis.⁵³

In *Hanson Pipe & Products, Inc. v. Bridge Technologies, LLC*,⁵⁴ the Fifth Circuit confirmed its long-standing rule that jurisdiction must be sufficient to establish general or specific jurisdiction over a particular entity, not its affiliates. In *Hanson Pipe*, the licensee Hanson Pipe & Products sued its licensor Con/Span Bridge Systems, Ltd., and its subsidiary Bridge Tek, claiming that they were interfering with Hanson Pipe's contracts with customers. The United States District Court for the Eastern District of Texas dismissed the suit against Con/Span for lack of personal jurisdiction, since its contacts with Texas were insufficient to support general jurisdiction.⁵⁵

The Fifth Circuit agreed that Bridge Tek's contacts with Texas could not support general jurisdiction over Con/Span where there was no showing that Bridge Tek was Con/Span's alter ego.⁵⁶ The Fifth Circuit held that Con/Span's website and other incidental contacts with the state of Texas were insufficient to subject Con/Span to the general jurisdiction of Texas courts.⁵⁷

Franchise litigants sometimes resolve their dispute within a short time after commencement of the lawsuit. When this occurs, the court may be left to decide that it no longer has jurisdiction over the dispute. In *Kothari v. Motiva Enterprises, LLC*,⁵⁸ Virendra Kothari, a Shell franchisee, sued Motiva Enterprises for violations of the Petroleum Marketing Practices Act ("PMPA"), the Texas Deceptive Trade Practices Act ("DTPA"), fraud, and breach of contract. Kothari also brought a request for declaratory relief. All of Kothari's claims arose out of a franchise agreement to operate a Shell service station.

In 2004, Kothari renewed his agreements with Motiva by executing a new Retail Facility Lease and Sales Agreement. In the spring of 2004, Kothari protested the real estate value of his service station pursuant to the Retail Facility Lease, which formed the basis for determining the rent to be paid. Shortly thereafter, Kothari received notice that his station failed Motiva's image inspection. Motiva conducted two additional inspections, but the parties disagreed on the results of these inspections. Kothari argued that he passed the second inspection but failed the next. Conversely, Motiva argued that Kothari failed the next two inspections. Nevertheless, in November 2004, Motiva sent a formal termination notice to Kothari. Kothari subsequently filed suit.

In February 2005, the district court entered an Agreed Temporary Restraining Order, preserving the status quo pending resolution on the merits. Also, in February 2005, the parties followed with an Agreed

53. *Id.* at 919.

54. 160 F. App'x 380 (5th Cir. 2005).

55. *Id.* at 381.

56. *Id.*

57. *Id.*

58. No. H-05-0499, 2006 WL 2129097 (S.D. Tex. July 27, 2006).

Preliminary Injunction, entered by the court, which continued the status quo through the trial. In the spring and summer of 2005, Motiva decided to change its program to rescind termination for program violations, provided that the franchisee attended image training and pass two additional inspections by a third party. Motiva offered to rescind Kothari's notice of termination if he complied with these provisions. Kothari complied, and Motiva rescinded his termination notice. At no time had Kothari's operation of his station been interrupted by Motiva. Moreover, since his retraining, Kothari had passed all subsequent inspections and was in no danger of terminations on the basis of inspections, which were the subject of the lawsuit.⁵⁹

Motiva moved for summary judgment, arguing that under Federal Rule of Civil Procedure 12(b)(1), the court lacked subject matter jurisdiction because Kothari's claims were moot. The district court agreed with Motiva and dismissed Kothari's PMPA claim.⁶⁰ At the time the action was filed, Kothari sought injunctive relief to prevent his service station from being shut down, since he was in danger of being terminated. Since that time, however, the district court noted that Motiva had rescinded the termination notice. Kothari argued that his request for permanent injunctive relief was not moot because Motiva continued to operate a discriminatory dual system of inspections that subjected Kothari to danger of termination. The district court disagreed, finding that a yet-unrealized, purely speculative danger of termination was insufficient to obtain PMPA injunctive relief.⁶¹ As such, the district court held that Kothari's franchise was never terminated and was not subject to cancellation, and Kothari could not maintain a PMPA action.⁶² The district court also denied Motiva's motion for summary judgment on Kothari's state-law claim, declining to exercise supplemental jurisdiction over these claims.⁶³

B. CHOICE OF LAW

Choice-of-law provisions have played a part in establishing jurisdiction over a party. In *Marathon Metallic Building Co., L.P. v. A&H Supply, Inc.*,⁶⁴ a Colorado company, Mountain Empire, distributed in Colorado the products of Marathon, a Texas corporation. A Mountain Empire principal and two associates entered into a broad guaranty of Mountain Empire's obligations to Marathon. Soon after the guaranty was sent to Texas, the parties memorialized their business relationship in a contract that contained a Texas choice-of-law clause. Mountain Empire failed to pay its debts to Marathon, and Marathon sued Mountain Empire and an

59. *Id.* at *2.

60. *Id.* at *4-5.

61. *Id.*

62. *Id.* at *4.

63. *Id.* at *5.

64. *Id.* at *3 (quoting *Goodman Co., L.P. v. A&H Supply, Inc.*, 396 F. Supp. 2d 766, 771-72 (S.D. Tex. 2005) (citing *Marathon Metallic Bldg. Co. v. Mountain Empire Constr. Co.*, 653 F.2d 926, 923 (5th Cir. 1981))).

individual guarantor in Texas. The Fifth Circuit Court of Appeals found that the choice-of-law clause contained in the general contract between the parties involved “purposeful and affirmative action, resulting in, at least, a minimum contact with Texas by the guarantor.”⁶⁵

In *NE Corp. v. Fish*,⁶⁶ NE Corporation sued Scott Fish, among others, for breach of contract, alleging that Fish, as the guarantor, failed to pay certain monies due under a promissory note once it matured. Fish filed several motions challenging personal jurisdiction, since Fish was a resident of Tennessee and did not conduct business in Texas. Fish also argued that jurisdiction may be proper in Colorado (*i.e.*, the situs of the property made the basis of the underlying sale). The United States District Court for the Northern District of Texas evaluated Fish’s contacts with Texas to determine whether personal jurisdiction existed.⁶⁷

The district court found that personal jurisdiction over Fish for the breach of contract claim was appropriate. The district court observed that the guaranty, which he executed for the promissory note, specifically stated that it would be “governed by and construed and enforced in accordance with the laws of the State of Texas.”⁶⁸ While the district court noted that “the presence of a choice-of-law clause in a contract would not alone support personal jurisdiction in an action based on that contract,”⁶⁹ the district court held that the guaranty at issue was of an expansive, absolute, and continuing type.⁷⁰

The language of the guaranty provided that “Guarantor hereby absolutely and unconditionally guarantees the prompt, complete, and full payment when due. . . .”; “[t]his Guaranty is an irrevocable, absolute, continuing guaranty of payment. . . .”⁷¹ The district court found that this broad guaranty, together with the Texas choice-of-law provision embodied within it, supported personal jurisdiction over NE’s breach of contract claim.⁷²

Choice-of-law provisions, however, may not apply to all claims. In *Red Roof Inns, Inc. v. Murat Holdings*,⁷³ Murat Holdings, LLC sued Red Roof Inns, Inc. and Accor Economy Lodging, Inc. (collectively, “Red

65. *NE Corp. v. Fish*, No. Civ.A. 3:05 CV 1525-B, 2006 WL 196951, at *3 (N.D. Tex. 2006) (citing *Marathon*, 653 F.2d 922-23). Other district courts in the Fifth Circuit were noted for having found personal jurisdiction to exist where expansive guarantees are paired with a choice of law clause. *See, e.g.*, *Plainscapital Bank v. Malina*, No. Civ.A. 3:05-CV-0469, 2005 WL 3454017, at *2 (N.D. Tex. Dec. 14, 2005); *Goodman Co., L.P. v. A & H Supply, Inc.*, 396 F.Supp.2d 766, 771 (S.D. Tex. 2005).

66. No. Civ.A. 3:05CV1525-B, 2006 WL 196951 (N.D. Tex. Jan. 25, 2006).

67. *Id.* at *1.

68. *Id.* at *3.

69. *Id.*

70. *Id.* at *4.

71. *Id.*

72. *Id.*

73. *Red Roof Inns, Inc. v. Murat Holdings, LLC*, 223 S.W.3d 676 (Tex. App.—Dallas 2007, pet. filed). The first appellate opinion was withdrawn and superseded. *See Red Roof Inns, Inc. v. Murat Holdings, LLC*, No. 05-05-00240-CV, 2006 WL 2458563 (Tex. App.—Dallas 2006, *opinion superseded*).

Roof"). Murat alleged contract, statutory, and tort claims. Red Roof moved for summary judgment on all claims. The trial court granted summary judgment against Murat on the statutory and tort claims. The contract claims were tried to a jury. The trial court rendered judgment on the jury verdict in the amount of \$5,806,000.00 plus prejudgment interest, court costs, and attorney's fees in favor of Murat. Both Murat and Red Roof appealed.

A few background facts are relevant. In 1998, Murat entered into a franchise agreement with Red Roof Inns and commenced renovations at the hotel. The following year, Accor acquired Red Roof Inns and later decided that (1) it would abandon the Red Roof Inn & Suites concept, and (2) it did not want Murat's hotel in the Red Roof system. Red Roof offered to terminate the franchise agreement, but Murat refused. Although Murat continued renovations at the hotel, disputes arose regarding whether Murat's renovations were sufficient for opening. This lawsuit followed with Murat asserting contract, statutory and tort claims against Red Roof.

Red Roof moved for summary judgment on Murat's statutory and tort claims. The trial court granted summary judgment against Murat, and Murat contended that the trial court erred on its claims for: (1) tortious interference; (2) violation of the Louisiana Unfair Trade Practices Act ("LUTPA"); (3) fraud and negligent misrepresentation; and (4) breach of fiduciary duty.

The franchise agreement contained a choice-of-law provision, which provided that it would "be interpreted, construed and enforced in accordance with the internal substantive laws of the State of Ohio, without regard to conflicts of laws principles."⁷⁴ The court of appeals held that by its language, the choice of Ohio law was limited to the interpretation and enforcement of the franchise agreement.⁷⁵ Therefore, Ohio law did not necessarily govern Murat's statutory and tort claims.⁷⁶

The court of appeals noted that Texas courts use the "most significant relationship" test to decide choice of law issues. Under that test, a court must consider which state's law has the most significant relationship "to the particular substantive issue to be resolved."⁷⁷ Moreover, the appellate court set out the Restatement's general principals relevant in a choice of law analysis:

- (a) The needs of the interstate and international systems;
- (b) The relevant policies of the forum;
- (c) The relevant policies of the other interested states and the relative interests of those states in determination of the particular issue;
- (d) The protection of justified expectations;
- (e) The basic policies underlying the particular field of law;

74. *Id.* at 684.

75. *Id.*

76. *Id.*

77. *Id.* (quoting *Hughes Wood Prods., Inc. v. Wagner*, 18 S.W.3d 202, 205 (Tex. 2000)).

(f) Certainty, predictability, and uniformity of result; and

(g) Ease in the determination and application of the law to be applied.⁷⁸

The court of appeals noted that these contacts were to be evaluated according to their relative importance with respect to the particular issue. Instead of the number of contacts being determinative, a court must evaluate the contacts in light of the state policies underlying the particular substantive issue.⁷⁹

The court of appeals commented that the choice of law was relevant to Murat's claims for tortious interference, LUTPA violation, fraud/negligent misrepresentation, and breach of fiduciary duty. The court of appeals concluded that Louisiana had the most significant relationship to the parties and the dispute.⁸⁰ The Murat's hotel was located in Louisiana. The franchise agreement was signed in Ohio and Murat paid the initial franchise fee in Ohio. Murat's alleged damages flowed from expenditures it incurred in renovating the hotel and profits it lost when not allowed to open as a Red Roof Inn. Murat was a Louisiana limited liability company whose principal office was located in Florida. Appearing to be most significant, the court of appeals found that Murat's performance under the franchise agreement occurred primarily in Louisiana. Many of the alleged misrepresentations by Red Roof occurred in Louisiana. As such, the court of appeals found that Louisiana had a "greater stake in the outcome than Ohio."⁸¹ Furthermore, "the purpose of Louisiana's unfair trade and consumer protection act is to protect consumers in its state and to deter injury to competition."⁸²

Applying Louisiana law, the court of appeals held that the summary judgment evidence was sufficient to raise a fact issue on Murat's tortious interference claim.⁸³ The court of appeals held that Murat failed to file its LUTPA claim within the one year statute of limitations period so the trial court properly granted summary judgment on that claim.⁸⁴ The court of appeals also concluded that the trial court properly granted summary judgment on Murat's fraud/negligent misrepresentation and breach of fiduciary duty claims.⁸⁵ Because the trial court committed a reversible error on the jury charge regarding the oral modification instruction for the breach of contract claim, the court of appeals reversed the trial court's judgment and remanded this case for a new trial.⁸⁶

78. See RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6(2) (1971).

79. *Murat Holdings*, 223 S.W.3d at 685.

80. *Id.*

81. *Id.*

82. *Id.* at 685.

83. *Id.* at 687.

84. *Id.* at 689.

85. *Id.* at 690.

86. *Id.* at 683, 690.

C. FORUM SELECTION

In *Youngblood v. JTH Tax Services, Inc.*,⁸⁷ the United States District Court for the Western District of Texas affirmed the concept that forum-selection clauses in franchise agreements should be enforced. The plaintiff William Youngblood opened a Liberty Tax Service franchise in San Antonio in January 2006. After the franchise closed its doors in March 2006, Youngblood filed a lawsuit in state court against JTH Tax for fraudulent inducement, DTPA violations, and negligent misrepresentation. JTH Tax removed the case and filed a motion to dismiss or, in the alternative, a motion to transfer venue. JTH Tax argued that the franchise agreement contained an exclusive mandatory forum-selection clause designating Virginia as the proper forum.⁸⁸ Youngblood argued that this lawsuit should be abated pending determination of a Virginia court's decision, involving the same parties and issues.⁸⁹ Although the district court denied JTH Tax's motion to dismiss, the district court granted its motion to transfer venue.⁹⁰

First, the district court analyzed whether the forum-selection clause applied to Youngblood's claims. The franchise agreement contained a paragraph entitled "Jurisdiction and Venue," providing:

[i]n any suit brought against us, including our present and former employees and agents, which in any way relates to or arises out of this Agreement, or any of the dealings of the parties hereto, venue shall be proper only in the federal court located nearest our National Office (presently the U.S. District in Norfolk, Virginia), or if neither federal subject matter or diversity jurisdiction exists, in the city or county state court located where our National Office is (presently the City of Virginia Beach, Virginia.).⁹¹

The district court held that because the forum-selection clause included language such as "venue shall be proper only," the forum-selection clause was "exclusive and mandatory."⁹²

Second, the district court determined whether the clause should be enforced. The district court determined that, based on federal law, the forum-selection clause was enforceable because Youngblood had "not established that it was included in the franchise agreement as a product of fraud or overreaching or that its enforcement would be otherwise unreasonable."⁹³

87. No. SA: 06-CA-380-XR, 2006 WL 1984656 (W.D. Tex. July 17, 2006). Co-Author Deborah S. Coldwell served as lead counsel for JTH Tax Services, Inc. in this matter.

88. *Id.* at *1.

89. About a month after Youngblood filed suit, JTH Tax filed a separate suit against Youngblood in the Eastern District of Virginia, asserting a claim for breach of the franchise agreement. *JTH Tax, Inc. v. William Youngblood & South Texas Finance, Inc.*, No. 2:06-CV-00256-JBF-FBS (E.D. Va.).

90. *JTH Tax*, 2006 WL 1984656, at *6.

91. *Id.* at *2.

92. *Id.*

93. *Id.*

The district court next analyzed JTH Tax's motion to dismiss.⁹⁴ The district court noted that the Fifth Circuit has held that a motion pursuant to Rule 12(b)(3) is a proper method for seeking dismissal based on a forum-selection clause.⁹⁵ However, the Fifth Circuit has not considered the application of Rule 12(b)(3) in a case in which the forum-selection clause designated another federal forum rather than a state court or foreign jurisdiction.⁹⁶ Thus, because JTH Tax moved both to dismiss and to transfer, and because the district court concluded that a transfer was in the interest of justice, the district court denied JTH Tax's motion to dismiss.⁹⁷

In evaluating JTH Tax's motion to transfer pursuant to 28 U.S.C. § 1404(a), the district court first concluded that this suit could have been brought in the transferee district (*i.e.*, the Eastern District of Virginia).⁹⁸ The district court next examined the § 1404(a) factors. The private concerns include: (1) the relative ease of access to sources of proof; (2) the availability of compulsory process to secure the attendance of witnesses; (3) the cost of attendance for willing witnesses; and (4) all other practical problems that make trial of a case easy, expeditious, and inexpensive. The public concerns include: (1) the administrative difficulties flowing from court congestion; (2) the local interest in having localized interests decided at home; (3) the familiarity of the forum with the law that will govern the case; and (4) the avoidance of unnecessary problems with conflict of laws of the application of foreign law.⁹⁹

After analyzing convenience to the parties and witnesses as well as sources of proof, the district court held that the private factors did not necessarily militate in favor of venue in either Virginia or Texas.¹⁰⁰ The district court, however, held that the public factors weighed in favor of transfer.¹⁰¹ The trial would be more expedient in Virginia; the Virginia court would be better equipped to try the case because Virginia law governed the case; and Virginia had an interest in suits against its residents and their alleged fraudulent conduct.¹⁰² The district court concluded that JTH Tax's numerous franchisees benefit from the savings and certainty inherent in the forum-selection clause and its enforcement.¹⁰³

Finally, the district court pointed out that the mandatory forum-selection clause weighed strongly in favor of a transfer.¹⁰⁴ The district court

94. *Id.* (noting that JTH Tax moved to dismissed under Rule 12(b)(3) and 28 U.S.C. § 1406(a)).

95. *Id.* at *3 (citing *Lim v. Offshore Specialty Fabricators, Inc.*, 404 F.3d 898, 902 (5th Cir. 2005)).

96. *JTH Tax*, 2006 WL 1984656, at *2.

97. *Id.* at *3.

98. *Id.*

99. *Id.* at *4 (citations omitted).

100. *Id.* at *5.

101. *Id.*

102. *Id.*

103. *Id.*

104. *Id.* at *6.

stated that although Youngblood “knew of the potential inconvenience of litigating in Virginia and was aware of his health issues at the time he signed the agreement, he voluntarily consented to the designation of a Virginia forum.”¹⁰⁵ As such, the district court granted JTH Tax’s motion to transfer and ordered that the action be transferred to the United States District Court for the Eastern District of Virginia, Norfolk Division.¹⁰⁶

Forum-selection clauses may also be enforced to determine the particular district of the state in which litigation will take place. For example, in *In re Talent Tree Crystal*,¹⁰⁷ Talent Tree filed a petition for writ of mandamus and an application for temporary relief with the Houston Court of Appeals for the First District. Talent Tree complained that the trial court improperly refused to enforce the forum-selection clause in the franchise agreement.¹⁰⁸

In the underlying suit, DRG, Inc., sued Talent Tree, among other claims, for breach of contract arising from a renewed franchise agreement. The franchise agreement contained a forum selection clause specifying venue:

Any cause of action between [Talent Tree] and [DRG] arising under this Agreement will be brought in the United States District Court for the Southern District of Texas. If that Court lacks jurisdiction, the action will be brought in the state courts in Houston, Texas, and [DRG] submits to the jurisdiction of such courts. No rights or causes of action arising from this Agreement will be lost if these venues are not available.¹⁰⁹

Despite this venue provision, DRG sued Talent Tree in a Texas state court. Talent Tree repeatedly moved to dismiss the original and amended petitions based on the forum-selection clauses. The trial court denied Talent Tree’s motion, and Talent Tree sought mandamus relief.¹¹⁰

The court of appeals first recited its well-settled rule that a motion to dismiss, by which Talent Tree sought to enforce the forum-selection clause, was the correct procedural mechanism to enforce a forum-selection clause.¹¹¹ The court of appeals noted that “a trial court must enforce a forum selection clause unless the opposing party clearly demonstrates that (1) enforcement would be unreasonable and unjust or (2) the clause is invalid for such reasons such as fraud or overreaching.”¹¹²

The court of appeals held that DRG did not show that the contract was invalid, since it did not assert any fraud or overreaching of the franchise agreement.¹¹³ The court of appeals rejected DRG’s contention that the

105. *Id.*

106. *Id.*

107. *In re Talent Tree Crystal*, No. 01-05-00686-CV, 2006 WL 305015 (Tex. App.—Houston [1st Dist.] Feb. 9, 2006, no pet.).

108. *Id.* at *2.

109. *Id.* at *1.

110. *Id.*

111. *Id.* at *2.

112. *Id.*

113. *Id.* at *3.

clause in the franchise agreement was not a forum-selection clause, but, rather, a contractual venue provision.¹¹⁴ The court of appeals held that there was no issue of dominant jurisdiction, which only existed when venue is proper in two or more Texas counties.¹¹⁵ Furthermore, the court of appeals held that DRG did not show that enforcement was unreasonable or unjust, nor did it show any grave difficulty or inconvenience with trying the case in the Southern District of Texas.¹¹⁶ Finally, the court of appeals rejected DRG's argument that laches applied to preclude mandamus relief. As a result, the court of appeals conditionally granted Talent Tree's petition for a writ of mandamus.¹¹⁷

Franchisees and licensees have also challenged whether an agreement's forum-selection clause applies to pre-contractual claims. In *Clark v. Power Marketing Direct, Inc.*,¹¹⁸ two licensees, James Clark and Ricky Pagnozzi, filed a suit against Power Marketing Direct, Inc., in Harris County, Texas, asserting claims for fraudulent inducement, fraud, and violation of the Texas Deceptive Trade Practices Act. Each license agreement, however, contained a forum-selection clause designating Ohio as the proper venue. Clark's license agreement provided that:

[A]ny action, claim or demand arising under or as a result of this Agreement shall be filed in Franklin County, Ohio and [Clark] hereby agrees and consents to the jurisdiction of any court located in Franklin County, Ohio.¹¹⁹

On the other hand, Pagnozzi's license agreement provided that:

[A]ny action, claim or demand arising under or as a result of this Agreement shall be filed in the common Pleas Court of Franklin County, Ohio, and [Pagnozzi] hereby agrees and consents to the jurisdiction of the Franklin County Court of Common Pleas as to any dispute involving the parties' business relationship, including personal jurisdiction over [Pagnozzi] and subject matter jurisdiction over the dispute.¹²⁰

Power Marketing moved to dismiss, and the trial court granted its motion.

Clark and Pagnozzi appealed, arguing that the forum-selection clause must be construed "most strictly" against Power Marketing, the drafter of the license agreement. The Houston Court of Appeals disagreed and held that a contract is interpreted against the drafter only when it is determined to be ambiguous.¹²¹ Since neither party identified any ambiguity and because a contract is interpreted against the drafter only as a last resort, the court of appeals overruled Clark and Pagnozzi's first point of

114. *Id.*

115. *Id.*

116. *Id.* at *3-4.

117. *Id.* at *4.

118. 192 S.W.3d 796 (Tex. App.—Houston [1st Dist.] 2006, no pet. h.).

119. *Id.* at 797.

120. *Id.*

121. *Id.* at 798.

error.¹²²

Similarly, the court of appeals rejected Clark and Pagnozzi's argument that the forum-selection clause did not apply, since their causes of action involved pre-contractual tort claims.¹²³ The court of appeals noted the Texas Supreme Court's holding in *Haase v. Glazner*:¹²⁴ "in the absence of a contract, a plaintiff cannot assert a fraudulent inducement claim."¹²⁵ The court of appeals further noted that the Dallas Court of Appeals and the Texas federal courts had expressly rejected the argument that a forum-selection clause could not encompass pre-contractual tort claims.¹²⁶ The court of appeals held that a forum-selection clause can encompass claims of fraud in the inducement.¹²⁷ The court of appeals further held that the "forum selection clauses were drafted broadly enough to encompass all of Clark and Pagnozzi's claims."¹²⁸

The court of appeals also rejected Clark and Pagnozzi's argument that because a successful suit would result in the contracts being ruled void, the forum-selection clauses should not be enforced.¹²⁹ Since Texas law presumes contracts to be valid, the court of appeals held that it would not "inquire into the enforceability of the contract in which that clause was found," and upheld enforcement of the forum-selection clause.¹³⁰

D. ARBITRATION

As discussed earlier, in *Hanson Pipe*, the Fifth Circuit dismissed a licensee's suit against its licensor and ordered the licensee and the licensor's subsidiary to arbitration.¹³¹ The Fifth Circuit held that, "[a]lthough the contract containing the arbitration claim was between Con/Span (the licensor) and Hanson Pipe, Hanson Pipe did not challenge in the district court its obligation to arbitrate its claim on grounds that Bridge Tek (the subsidiary) was not a signator to the agreement."¹³² The Fifth Circuit refused to consider any argument made for the first time on appeal.¹³³

In addition, the Fifth Circuit held that, although the contract containing the arbitration clause expired before the dispute arose that was the sub-

122. *Id.*

123. *Id.* at 799-800.

124. 62 S.W.3d 795 (Tex. 2001).

125. *Clark*, 192 S.W.3d at 799 (quoting *id.* at 798 (noting that fraudulent inducement "is a particular species of fraud that arises only in the context of a contract and requires the existence of a contract as a part of its proof.")).

126. *Clark*, 192 S.W.3d at 799 (citing *My Café-CCC, Ltd. v. Lunchstop, Inc.*, 107 S.W.3d 860, 867 (Tex. App.—Dallas 2003, no pet. h.) *abrogated on other grounds by In re AIU Ins. Co.*, 148 S.W.3d 109 (Tex. 2004)); *see also* *Tex. Source Group, Inc. v. CCH, Inc.*, 967 F. Supp. 234, 237-38 (S.D. Tex. 1997); *Hoffman v. Burroughs Corp.*, 571 F. Supp. 545, 547 (N.D. Tex. 1982).

127. *Clark*, 192 S.W.3d at 800.

128. *Id.*

129. *Id.*

130. *Id.*

131. *Hanson Pipe & Products, Inc. v. Bridge Tech., LLC*, 160 F. App'x 380, 382 (5th Cir. 2005).

132. *Id.*

133. *Id.*

ject of the suit, the Supreme Court has made it clear that an arbitration clause applies to a grievance arising after the expiration of the agreement when “under normal principles of contract interpretation, the disputed contractual right survives expiration of the remainder of the agreement.”¹³⁴ The Fifth Circuit agreed with the district court that defendants were entitled to demand arbitration because plaintiff sought a ruling regarding the scope and legitimacy of the intellectual property rights defendants claimed to possess in their bridge system that survived the expiration of the contract.¹³⁵ As such, the district court properly submitted this dispute to arbitration.¹³⁶

When parties agree to arbitrate and the arbitrator’s decision is confirmed, appellate review is very limited, since decisions are meant to be final in all but exceptional cases. In *Universal Computer Systems, Inc. v. Dealer Solutions, LLC*,¹³⁷ the Houston Court of Appeals held that the facts presented were not exceptional under the applicable case law, and, therefore, confirmation of the arbitrator’s decision was confirmed.¹³⁸ In this case, Universal Computer Systems, among others, sued its competitor Dealer Solutions, among others, for misappropriation of trade secrets and breach of the licensing agreement. Dealer Solutions counterclaimed for misappropriation of trade secrets.¹³⁹

In the trial court, Dealer Solutions and Universal were engaged in a highly contested discovery dispute. Dealer Solutions propounded interrogatories to Universal requesting the identity of each trade secret that Dealer Solutions allegedly misappropriated, and Dealer Solutions alleged Universal provided inadequate responses on more than five occasions. Dealer Solutions repeatedly moved to compel the identity of each trade secret. After three sets of supplemental responses to the interrogatories, which Dealer Solutions still contended were inadequate, Universal filed a proposed order, which was agreed to by Dealer Solutions, referring the case to arbitration. The trial court, nevertheless, entertained the discovery dispute by entering an order granting Dealer Solutions’ motion to dismiss for discovery abuse. Pursuant to the order, the trial court “established a presumption of the non-existence of any trade secret . . . claimed by [Universal]. . . .”¹⁴⁰ Although Universal again supplemented its discovery responses, Dealer Solutions filed a second motion to dismiss for discovery abuse. Although the trial court denied the second motion to dismiss, it limited Universal’s evidence in support of its claim that a certain software system was a trade secret. Following this order, Universal again moved to compel arbitration, the trial court held a hearing to clarify the evidentiary limitation, and the trial court granted, in part, Universal’s

134. *Id.* (quoting *Litton Fin. Printing Div. v. N.L.R.B.*, 501 U.S. 190, 205-06 (1991)).

135. *Hanson Pipe*, 160 F. App’x at 382.

136. *Id.*

137. 183 S.W.3d 741 (Tex. App.—Houston [1st Dist.] 2005, pet. denied).

138. *Id.* at 744.

139. *Id.*

140. *Id.* at 746.

motion to compel arbitration. Universal filed a mandamus petition, challenging the trial court's partial denial of its motion to compel arbitration.¹⁴¹

In the arbitration, despite the trial court's "discovery-limitation" ruling, the panel of three arbitrators declined to limit Universal's testimony and evidence on trade secrets. As such, the panel allowed Universal to introduce evidence for two weeks. After hearing all the evidence, the panel held that Universal had failed to prove its trade secret misappropriation claim.¹⁴²

The court of appeals held that the trial court erred by not sending the case immediately to arbitration and in making the "discovery-limitation" ruling.¹⁴³ "Once a party seeking to compel arbitration establishes that an agreement [to arbitrate] exists . . . , and that the claims raised are within the agreement's scope, the trial court has no discretion but to compel arbitration and stay its proceedings pending arbitration."¹⁴⁴ However, notwithstanding the trial court's order, the arbitrators ultimately considered all of Universal's evidence, not just the matters set forth in Universal's interrogatory responses. The court of appeals, therefore, held that the trial court's discovery order did not cause the rendition of an improper judgment.¹⁴⁵

After reviewing the circumstances of the arbitration award, the court of appeals held that Universal did not establish sufficient grounds to set aside the award, namely, that the decision was tainted with fraud, misconduct, or gross mistake.¹⁴⁶ Along with other arguments that Universal made, Universal asserted that the panel made a gross mistake by failing to address three leading Texas cases and making legal conclusions that were a "gross distortion of well-settled law."¹⁴⁷ The court of appeals concluded that "these alleged errors in the application of substantive law by the arbitrators during the proceedings were not reviewable by the court on a motion to vacate an award."¹⁴⁸ The court of appeals emphasized that it "could not review alleged errors in the application of substantive law by the arbitrators."¹⁴⁹ Rather, its review was confined to whether the record indicated the arbitrators acted in bad faith or failed to exercise honest judgment—not whether it agreed or disagreed with the panel's application of the law.¹⁵⁰ Accordingly, the court of appeals concluded that the arbitrators did not commit a gross mistake in finding that Universal failed to prove its trade secret misappropriation and breach of con-

141. *Id.* at 747.

142. *Id.* at 748.

143. *Id.* at 749-50.

144. *Id.* at 749.

145. *Id.* at 750.

146. *Id.* at 753-54.

147. *Id.* at 751.

148. *Id.* at 753.

149. *Id.* at 754.

150. *Id.*

tract claims.¹⁵¹

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

A. THE FRANCHISE RELATIONSHIP

In *Douglas v. Petroleum Wholesale, Inc.*,¹⁵² the Houston Court of Appeals heard an appeal from the trial court's ruling that an operator of a Diamond Shamrock gas station was not a franchisee/retailer under the PMPA¹⁵³ and, therefore, could not avail itself of the protections afforded by the PMPA.¹⁵⁴ Defendant Petroleum Wholesale, Inc., ("PWI") was a wholesale distributor of motor fuel, who had contracted with the owner of a gas station and convenience store to supply Diamond Shamrock branded motor fuel on assignment in connection with related Diamond Shamrock signage and materials. The gas station owner leased, and then ultimately sold, the assets related to the gas station and convenience store to Douglas in 1997, and Douglas continued to operate under the Diamond Shamrock name. PWI continued to perform under the existing agreement after Douglas took ownership of the assets. However, in 2000, PWI informed Douglas that his station was being "de-branded" and that he could no longer sell Diamond Shamrock branded motor fuel.¹⁵⁵

Douglas sued PWI for wrongful termination of their alleged franchise relationship on grounds that the termination violated the PMPA. Douglas argued that he was a retailer under the PMPA who purchased motor fuel for sale to the general public. However, the trial court found that Douglas obtained gas from PWI on consignment and therefore never purchased fuel for sale to the general public, which was a requirement for application of the PMPA. Therefore, the trial court found that Douglas could not avail himself of the protections of the PMPA.¹⁵⁶

On appeal, Douglas argued that he met the definition of a retailer because he satisfied a test that analyzes whether the party has a "significant indicia of entrepreneurial responsibility or economic risk in the operation of the motor fuel sales at his store."¹⁵⁷ The significant-indicia-of-entrepreneurial-responsibility test has been used in a number of cases. It instructs courts to first look to the statutory definition of a retailer and then to the totality of the circumstances to see whether the operator effectively undertakes the risks associated with the resale of fuel.¹⁵⁸ However, the court of appeals declined to go beyond the clear language of the PMPA and instead stated that it believed the "the indicia of en-

151. *Id.*

152. 190 S.W.3d 97 (Tex. App.—Houston [1st Dist.] 2005, no pet. h.).

153. 15 U.S.C. §2801-06.

154. *Douglas*, 190 S.W.3d at 98.

155. *Id.* at 97.

156. *Id.*

157. *Id.* at 100-01.

158. *Id.* at 101.

trepreneurial responsibility to be relevant only to the extent that it establishes that a gas station operator purchases motor fuel for resale to the public."¹⁵⁹ Thus, the court of appeals affirmed the trial court's decision that Douglas was not a retailer under the PMPA.¹⁶⁰

B. TERMINATION AND NON-RENEWAL

In *Kothari v. Motiva Enterprises, L.L.C.*,¹⁶¹ Kothari brought an action against Motiva stemming from the termination of a franchise agreement to operate a Shell service station. Kothari operated a Shell branded service station in Houston, Texas, pursuant to two contracts: a Retail Facility Lease and a Retail Sales Agreement. After protesting the real estate value of his station pursuant to the Retail Facility Lease (for purposes of calculating rent), Kothari received notice that his station failed an image inspection conducted pursuant to the Retail Sales Agreement. Thereafter, Motiva issued a formal notice of termination to take effect on February 21, 2005. Before the termination was effective, Kothari filed suit alleging that Motiva's Notice of Termination violated the PMPA and also asserting causes of action under the DTPA, common law fraud, breach of contract, and a cause of action for declaratory judgment. The court entered an Agreed Temporary Restraining Order preserving the status quo pending resolution on the merits. In the interim period, Motiva developed and promoted a rescission program for former franchisees that had previously been terminated due to imaging defaults. The rescission program required the terminated franchisee to attend image training and pass two additional inspections by a third party in order to be eligible for rescission. Motiva offered rescission to Kothari, and Kothari accepted.¹⁶²

Since Kothari's termination was rescinded and Kothari had never actually ceased operating, Motiva moved to dismiss Kothari's PMPA claims as moot, moved for summary judgment on Kothari's remaining fraud, DTPA, and part of its breach of contract claims, and moved for dismissal of Kothari's declaratory relief action. As to the PMPA claims, the district court held that the Temporary Restraining Order and the damages claims were indeed moot.¹⁶³ The district court also found that the declaratory relief claims were not justiciable.¹⁶⁴ However, the district court declined to grant the motion for summary judgment as it pertained to the state law fraud, DTPA, and breach of contract claims, finding that the factors weighed against exercise of supplemental jurisdiction.¹⁶⁵ Instead, the district court dismissed the claims without prejudice such that Kothari could bring the claims in state court if desired.¹⁶⁶

159. *Id.* at 102.

160. *Id.*

161. No. H-05-0499, 2006 U.S. Dist. LEXIS 55800 (S.D. Tex. 2006).

162. *Id.* at *2.

163. *Id.* at *12-13.

164. *Id.* at *20.

165. *Id.* at *18-19.

166. *Id.* at *19, 21.

V. COMMON-LAW CLAIMS

A. CONTRACT ISSUES

In *Performance Dealerships, L.P. v. Mitsubishi Motors North America, Inc.*,¹⁶⁷ the United States District Court for the Southern District of Texas addressed an automobile-dealership franchisee's claims of fraud, economic duress, and unconscionability against its franchisor. In 2003, the automobile dealership entered into a sales and services agreement with Mitsubishi. In 2004, after suffering financial loss, the dealership sought permission from Mitsubishi to house its Saab service and parts department, which was precluded by the terms of the 2003 agreement. Mitsubishi, however, agreed to enter into a new sales and service agreement in 2004 that would allow the dealership to combine its Saab and Mitsubishi operations for a period of twenty-four months. As in the 2003 agreement, the 2004 agreement contained a general release and a waiver of the application of Section 1542 of the California Civil Code, which provides certain protections to parties executing releases, thus allowing the dealership to release unknown claims. Two months after entering into the new agreement, the dealership resigned as an authorized Mitsubishi dealer and sued Mitsubishi alleging fraud, economic duress, and unconscionability.¹⁶⁸

To establish fraud under California law,¹⁶⁹ a plaintiff must show (1) a misrepresentation; (2) knowledge that the misrepresentation was false; (3) intent to defraud; (4) justifiable reliance; and (5) resulting damage.¹⁷⁰ The principal of the automobile dealership alleged that a Mitsubishi employee told him that the terms of the 2004 agreement were the same as the terms of the 2003 agreement. A comparison of the two agreements revealed that the agreements were in fact identical other than the addition of an exhibit that allowed the plaintiff to operate the Saab dealership on the premises. Therefore, the district court held that the dealership failed to present evidence that Mitsubishi made any misrepresentations regarding the release.¹⁷¹ Further, the district court held that the principal of the automobile dealership was not justified in relying on the alleged misrepresentation under the circumstances.¹⁷² Where a party on one side of the transaction is represented by counsel, he cannot justifiably rely on the alleged misrepresentations made by an individual on the other side of the transaction.¹⁷³ The district court granted Mitsubishi's motion for summary judgment with regard to the fraud claim.¹⁷⁴

167. No. Civ.A. H-05-4211, 2006 WL 964730 (S.D. Tex. Apr. 12, 2006).

168. *Id.* at *1.

169. The 2004 Sales and Service Agreement provided that it "shall be governed by, and construed in accordance with, the laws of the State of California." *Id.* at *3.

170. *Id.* at *4 (citing *Gil v. Bank of Am.*, 39 Cal. Rptr. 3d 114 (Cal. Ct. App. 2006)).

171. *Mitsubishi Motors*, 2006 WL 964730, at *4.

172. *Id.*

173. *Id.*

174. *Id.*

The district court also granted Mitsubishi's summary judgment motion on the economic duress claim. A release may be held invalid on the basis of economic duress if a party is subject to a wrongful act and succumbs to the wrongdoer to avoid financial ruin.¹⁷⁵ The district court held that plaintiff failed to present evidence that Mitsubishi had threatened or engaged in any related misconduct, particularly where Mitsubishi had agreed to renegotiate the 2003 agreement to allow the dealership to house portions of its Saab operation with portions of the Mitsubishi business.¹⁷⁶ Additionally, the district court recognized that there was no evidence that plaintiff would have faced economic ruin.¹⁷⁷

Finally, the district court granted summary judgment on the unconscionability claim. Under California law, a court may invalidate a release if it is unconscionable both procedurally, where the circumstances show oppression and surprise, and substantively, where the terms of the release are overly-harsh and one-sided.¹⁷⁸ Because the principal of the automobile dealership was a well-educated businessman with years of experience in the automobile industry, was represented by counsel at all relevant times, and the release language was not hidden in the 2004 agreement, the district court held that there was no evidence that the release was procedurally unconscionable.¹⁷⁹ Further, the release language was straight-forward, clear and not overly harsh, and, therefore, the district court held that it was not substantively unconscionable.¹⁸⁰

In *Murat Holdings*,¹⁸¹ the breach of contract claim was tried to a jury and the trial court rendered judgment on the jury verdict in the amount of \$5,806,000 in favor of Murat. The question of whether the parties modified the franchise agreement was not submitted to the jury even though the jury received an instruction on contract modification. The court of appeals held that Murat had to establish modification of the franchise agreement first in order to prove that Murat satisfied its obligations and to support a breach by Red Roof.¹⁸² The court of appeals concluded that it was likely that the oral modification instruction formed the basis for the jury's findings that Murat met its obligations under the franchise agreement and Red Roof breached the agreement.¹⁸³ However, because the court of appeals could not conclusively determine the effect of the instruction, the court of appeals held that the trial court's error in including the instruction without an accompanying question was

175. *Id.* (citing *Navellier v. Sletten*, 262 F.3d 923, 940 (9th Cir. 2001)).

176. *Mitsubishi Motors*, 2006 WL 964730, at *4.

177. *Id.*

178. *Id.* at *5 (citing *A&M Produce Co. v. FMC Corp.*, 186 Cal. Rptr. 114 (Cal. Ct. App. 1982)).

179. *Mitsubishi Motors*, 2006 WL 764730, at *5.

180. *Id.*

181. *Murat Holdings*, 223 S.W.3d at 681.

182. *Id.* at 682.

183. *Id.* at 683.

reversible error that prevented Red Roof from presenting its case on appeal.¹⁸⁴

B. VICARIOUS LIABILITY

In *Wallace v. Wymer*,¹⁸⁵ four boys left Astroworld Amusement Park through the front gate. Somewhere between Astroworld and a nearby McDonald's parking lot, they were assaulted by a gang of fifty or more unknown people. After the assault, the boys continued towards the McDonald's restaurant where they were picked up by one of the boys' parents. After they left the McDonald's parking lot in the parent's car, they were struck by another car fleeing an attack by people in the McDonald's parking lot. Plaintiffs sued McDonald's, Six Flags Theme Parks, Inc., in its capacity as owner of Astroworld, and others, claiming that the defendants were liable for plaintiffs' personal injuries.¹⁸⁶

The district court entered summary judgment in favor of Six Flags and the Houston Court of Appeals affirmed, holding that Six Flags did not have a duty to protect plaintiffs from the assault.¹⁸⁷ The general rule is that "no person has a legal duty to protect another from the criminal acts of a third person."¹⁸⁸ An exception to this rule, however, exists when a person controls the premises.¹⁸⁹ Under these circumstances, a person "has a duty to use ordinary care to protect invitees from criminal acts of third parties if he knows or has reason to know of an unreasonable and foreseeable risk of harm to the invitee."¹⁹⁰ Because the acts occurred outside Astroworld, the court of appeals held that Six Flags could not have had "knowledge of an unreasonable and foreseeable risk," and therefore, the exception did not apply.¹⁹¹

The district court also granted McDonald's motion for summary judgment. McDonald's produced summary judgment evidence, including an affidavit from a McDonald's corporate representative, stating that McDonald's did not own or control the restaurant where the alleged assault took place, and the restaurant was instead owned by Wymer Enterprises.¹⁹² Because plaintiffs failed to mention Wymer in their response to the summary judgment motion and because there was no evidence to create an issue of fact regarding McDonald's ownership or control of the restaurant, the court of appeals found no error in the district court's grant of summary judgment to McDonald's.¹⁹³

184. *Id.*

185. No. 01-04-00735-CV, 2005 WL 3214689 (Tex. App.—Houston [1st Dist] Dec. 1, 2005, no pet.).

186. *Id.* at *1.

187. *Id.* at *3.

188. *Id.* at *2.

189. *Id.*

190. *Id.*

191. *Id.*

192. *Id.* at *3.

193. *Id.* at *3-4.

VI. STATUTORY CLAIMS

A. COVENANTS NOT TO COMPETE

Under the Texas Non-Compete Act,¹⁹⁴ a covenant is enforceable if it (a) is ancillary to or part of an otherwise enforceable agreement, and (b) contains reasonable limitations on the time, geographical area, and scope of the activity to be restrained, which do not impose a greater restraint than necessary to protect the employer's goodwill or business interest. To be "ancillary" to an "otherwise enforceable agreement," the consideration typically consists of an employer's promise to provide an employee confidential information, which makes the non-compete covenant necessary to enforce the employee's return promise not to disclose the confidential documents or materials.¹⁹⁵

Although not a franchise case, and slightly outside the survey period, on October 20, 2006, the Texas Supreme Court revisited and revised its landmark ruling in *Light v. Centel Cellular Company of Texas*,¹⁹⁶ the seminal case concerning covenants not to compete in Texas. Thus, we felt it necessary to include the case in this Survey, since it could have a bearing on franchises in Texas.

In *Alex Sheshunoff Management Services, L.P. v. Johnson*,¹⁹⁷ the Texas Supreme Court held that an at-will employee's promise not to disclose confidential information became an enforceable agreement to support a non-compete covenant when his employer later performed its corresponding promise to provide training and access to confidential information.¹⁹⁸ By reaching this decision, the Texas Supreme Court removed its *Light*-imposed requirement that the agreement containing the covenant had to be enforceable the *instant* the agreement was made.¹⁹⁹

In *Sheshunoff*, an employer required a four-year, at-will employee, several months after being promoted, to sign an employment agreement containing a covenant not to compete. In the covenant, the employee agreed that, for one year after his termination, he would not: (1) provide services to any of the employer's clients to whom the employee had provided services or conducted significant sales activity within the last year of his employment (without geographical limitation); or (2) solicit or aid any other party in soliciting the employer's clients or prospective clients. The covenant was ancillary to a confidentiality/non-disclosure agreement in which the employer agreed to provide the employee with confidential information and special training regarding its business methods, and, in turn, the employee agreed not to disclose the confidential information. After the employee signed the agreement, the employer *later* provided the employee with the confidential information and training on an on-going

194. TEX. BUS. & COM. CODE ANN. § 15.50 (Vernon 2002).

195. *Sheshunoff*, 209 S.W.3d at 648-49.

196. 883 S.W.2d 642 (Tex. 1994).

197. 209 S.W.3d 644 (Tex. 2004).

198. *Id.* at 646.

199. *Id.*

basis.²⁰⁰

Subsequently, the employee resigned and went to work for a competitor, and the employer sued the employee to enforce the restrictive covenant. The trial and appellate courts determined, relying on *Light*, that the confidentiality/non-disclosure provision was not “an otherwise enforceable” agreement because the employer did not make a promise that was enforceable *at the time* the parties entered into the agreement. The employer appealed the ruling to the Supreme Court of Texas.²⁰¹

Based on *Light*, a split among the Texas appellate courts developed concerning what promises between the employer and employee are sufficient to create an “otherwise enforceable agreement.” The majority viewpoint has been that the “otherwise enforceable agreement” cannot be dependent on any future performance. Instead, the agreement must be enforceable “at the time the agreement is made.”²⁰² The *Sheshunoff* case resolved this post-*Light* confusion.

Initially, the Texas Supreme Court agreed that, under *Light*, the employer’s promise to provide confidential information and training was not enforceable at the time the confidentiality/non-disclosure agreement was made.²⁰³ Rather, the employer could have terminated Johnson’s at-will employment *before* it provided the confidential information and training, which made the employer’s promise illusory at that point in time.²⁰⁴ Under the reasoning in *Light*, the non-compete was unenforceable because the promise giving rise to the employer’s interest in restraining the employee from competing (providing confidential information) was not enforceable at the time the agreement was made.²⁰⁵ In *Sheshunoff*, however, the supreme court departed from this view of Texas non-compete law.

The supreme court observed that the Covenant Not to Compete Act’s “core inquiry is whether [a] covenant ‘contains limitations as to time, geographical area, and the scope of activity to be restrained that are reasonable and do not impose a greater restraint than is necessary to protect the goodwill or other business interest of the promisee.’”²⁰⁶ Therefore, the supreme court explained that “overly technical disputes” regarding whether a covenant is ancillary to an otherwise enforceable agreement have obscured this “core inquiry.”²⁰⁷ One such “technical dispute” was the prevailing viewpoint that the “otherwise enforceable agreement” had to be binding and enforceable at the moment the agreement was made. In rejecting this viewpoint, the supreme court concluded that a covenant not to compete is enforceable if: (1) it is part of, or ancillary to, an agree-

200. *Id.* at 646-47.

201. *Id.* at 647-48.

202. *See id.* at 648-50.

203. *Id.* at 649.

204. *Id.* at 650.

205. *Id.*

206. *Id.* at 655 (quoting TEX. BUS. & COM. CODE § 15.50(a)).

207. *See id.*

ment that contains a promise giving rise to the employer's interest in restraining the employee from competing; (2) the employer then makes good on its promise and delivers the confidential information or specialized training; and (3) the covenant not to compete contains reasonable limitations as to time, geographical area, and scope of activity to be restrained.²⁰⁸ Based on this test, the supreme court reversed and remanded, explaining that Sheshunoff's agreement became enforceable when the employer later performed its promise by providing him with confidential information and training.²⁰⁹

The Texas Supreme Court further rejected the employee's arguments that the covenant was overbroad because, among other things, the restriction on solicitation of certain clients and prospective clients was unrelated to any training or confidential information he received after he entered into the employment agreement.²¹⁰ In Sheshunoff's position, the employee continued to develop clients after he executed the agreement and was privy to on-going confidential information relevant to competing with his employer.²¹¹

Based on *Sheshunoff*, employers are no longer required to contemporaneously provide an employee confidential information and training when the employee signs an agreement containing a covenant not to compete. The *Sheshunoff* case, however, is not expected to end litigation over such restraints. Rather, the supreme court shifted the focus to analyzing disputes over whether a covenant is ancillary to an otherwise enforceable agreement within the broader context of "whether and to what extent a restraint on competition is justified."²¹²

VII. REMEDIES: DAMAGES AND INJUNCTIVE RELIEF

A. COMPENSATORY DAMAGES²¹³

In *Kothari*, discussed *supra*, despite the franchisor Motiva's argument that Kothari's PMPA claim was moot, Kothari argued that he was still entitled to actual damages in the form of a \$65-per-gas-load-delivered fee as a result of the pending termination. Kothari argued that Motiva revoked his use of the electronic fund transfer system and that he was charged \$65.00 per delivery during the pendency of the action. Motiva countered that Kothari did not actually pay this charge. Although four loads of fuel were delivered to Kothari during the time of the lawsuit, Motiva adduced evidence that Kothari was never invoiced for or paid the

208. *Id.* at 651, 656.

209. *Id.* at 657.

210. *Id.*

211. *Id.*

212. *Id.* at 655-56.

213. The authors comment that a notable, franchise case discussing compensatory and punitive damages, *Springs Window Fashions Division, Inc. v. Blind Maker, Inc.*, 184 S.W.3d 840 (Tex. App.—Austin 2006, pet. granted) was analyzed in Deborah S. Coldwell, et al., *Franchise Law*, 59 SMU L. REV. 1349, 1375-78 (Summer 2006).

\$65.00 charge.²¹⁴

In addition to actual damages, Kothari sought punitive damages and attorneys' fees. Motiva argued that the district court should enter summary judgment on the punitive damages and attorneys' fees claim because no termination ever took effect and because Kothari was not a "prevailing party." Kothari argued that the Agreed Preliminary Injunction entered by the district court afforded it "prevailing party" status. The district court held that a "prevailing party is one who has been awarded some relief by the court. Relief includes judgments on the merits as well as settlement agreements enforced through a consent decree that create the 'material alteration of the legal relationship of the parties.'"²¹⁵ The district court concluded that the preliminary injunction did not dispose of Kothari's claims on the merits or affect the underlying dispute but was "instead a temporary measure to preserve the status quo pending trial on the merits."²¹⁶ The district court further held that "Kothari was not a prevailing party because of Motiva's voluntary decision to rescind the notice of termination. 'A defendant's voluntary change in conduct, although perhaps accomplishing what the plaintiff sought to achieve by the lawsuit, lacks the necessary judicial imprimatur on the change.'"²¹⁷ The district court, therefore, found that Kothari had not achieved any relief in this lawsuit that qualified him as a "prevailing party."²¹⁸

B. PUNITIVE DAMAGES

Exemplary damages must be adequately pleaded. In *In re Schlotzsky's, Inc.*,²¹⁹ the Official Committee of Unsecured Creditors of Schlotzsky's, Inc. (the "Committee") sued Grant Thornton, an audit firm, for alleged failures to properly perform fiscal year audits. The Committee asserted that Thornton did not abide by Generally Accepted Accounting Standards ("GAAS"), which caused Schlotzsky's to become more insolvent. The Committee asserted claims for professional negligence, breach of contract, equitable subordination, and avoidance of preferential transfers. The Committee also sought exemplary damages. Grant Thornton, however, argued that the Committee failed to adequately plead gross negligence pursuant to Texas Civil Practice and Remedies Code section 41.003.²²⁰

214. *Kothari*, 2006 WL 2129097, at *4.

215. *Id.* (quoting *Buckhannon Bd. and Care Home, Inc. v. W. Va. Dept. of Health & Human Res.*, 121 S. Ct. 1835, 1839-40 (2001)).

216. *Kothari*, 2006 WL 2129097, at *4.

217. *Id.* at *5 (citing *Buckhannon*, 121 S. Ct. at 1841).

218. *Kothari*, 2006 WL 2127097, at *5.

219. 351 B.R. 430 (W.D. Tex. 2006). Co-author Robert A. Lauer served as Corporate Counsel for Schlotzsky's, Inc., during the bankruptcy. Haynes and Boone, LLP, served as lead bankruptcy counsel for Schlotzsky's, Inc. during the bankruptcy.

220. *Id.* at 440.

The Committee claimed that Grant Thornton's argument was flawed, since it tracked the language of the statute: ". . . when viewed objectively from Grant Thornton's viewpoint. . . . Grant Thornton's conduct involved an extreme degree of risk, considering the probability and magnitude of the potential harm. . . . Further, Grant Thornton was subjectively aware of the risks involved, but proceeded with conscious indifference to their duties and to the rights and welfare of the debtors."²²¹ The bankruptcy court concluded that this language satisfied the "short and plain statement" requirement of Rule 8 of the Federal Rules of Civil Procedure and, therefore, withstood the motion to dismiss.²²²

C. INJUNCTIVE RELIEF

In *Schlotsky's, Ltd. v. Sterling Purchasing & National Distribution Co.*,²²³ the United States District Court for the Western District of Texas analyzed whether Sterling was entitled to injunctive relief, so that it could distribute Schlotsky's products until a final trial on the merits. In December 2004, Bobby Cox Companies, Inc., purchased the assets of Schlotsky's, Inc., ("SI")²²⁴ for \$28.5 million following an auction of SI's bankruptcy estate. Bobby Cox assigned its rights to Schlotsky's Ltd. ("SL"). Pursuant to the sale order from the bankruptcy court, the asset sale conveyed title to all of SI's trademarks and rights as franchisor, without transferring any of SI's liabilities.²²⁵

SL, as franchisor, had the right to approve all suppliers and distributors of its branded and proprietary products. Effective June 2005, SL designated SYGMA and COI as the only sources for Schlotsky's products. During the bankruptcy proceeding, SI had previously approved Sterling as a "non-exclusive supply chain manager," which authorized Sterling as a distributor of Schlotsky's products. Sterling's approval, however, was revocable at any time. Despite Sterling's non-exclusive, revocable status, Sterling made representations that it was an exclusive distributor. SL asserted that Sterling's misrepresentations threatened Schlotsky's trademarks. As such, SL sought to have most, if not all, of its franchisees sign participation agreements with SYGMA and COI. Sterling moved for a preliminary injunction to prevent SL from excluding Sterling from participating in SL's distribution chain. In addition to injunctive relief, Sterling asserted claims for tortious interference with existing and prospective contracts and relations, promissory estoppel, and negligent misrepresentation.²²⁶

The district court held that Sterling failed to prove that it was likely to

221. *Id.*

222. *Id.*

223. No. A-05-CA-195SS, 2006 WL 2265527 (W.D. Tex. May 24, 2006).

224. Co-author Robert A. Lauer served as Corporate Counsel for Schlotsky's, Inc., up to the date of the sale to Bobby Cox Companies, Inc., and testified at the trial in this case.

225. *Schlotsky's*, 2006 WL 2265527, at *1.

226. *Id.* at *1-2.

succeed on the merits of any of its claims.²²⁷ In particular, the district court held that SL did not tortiously interfere with Sterling's contracts or relations; SL merely asserted its legitimate authority as franchisor and trademark owner and exercised its own legal rights.²²⁸ In addition, the district court held that Sterling could not succeed on its promissory estoppel or negligent misrepresentation claims, since these claims were based on SI's alleged promises.²²⁹ The district court emphasized that SL did not succeed to any of SI's liabilities, under which such promissory estoppel and misrepresentation claims would fail.²³⁰ Moreover, the district court held that Sterling could not reasonably have relief on any of SI's alleged promises, given the franchise system's state under the bankruptcy.²³¹ Therefore, the district court found that Sterling had not demonstrated there was a substantial likelihood that it would succeed on the merits of its counterclaims.²³²

In *ICEE Distributors, Inc. v. J&J Snack Foods Corp.*,²³³ the Fifth Circuit discussed grounds for modification of a permanent injunction. ICEE Distributors, a regional distributor, sued ICEE of America ("IOA"), the trademark owner of ICEE, for breach of their licensing agreement as well as J&J Snack Food Corp. and Wal-Mart Stores, Inc., for trademark infringement and dilution. Distributors owned a right to distribute ICEE products in their distribution territory, including Louisiana, Arkansas, Texas, Missouri, Alabama, and Georgia. Despite Distributors' refusal to allow J&J to distribute its ICEE product—squeeze-up tubes—J&J sold the tubes in Distributors' territory; Wal-Mart sold these tubes in its Sam's Club stores.²³⁴

After a trial, the jury found J&J and Wal-Mart liable for willful trademark dilution and IOA liable for breach of contract. Based on the verdict, the district court entered a permanent injunction against J&J and Wal-Mart, prohibiting the sale of squeeze tubes within Distributor's territory.²³⁵ J&J, Wal-Mart, and IOA appealed the injunction, and the court affirmed the injunction, but solely on the basis of the breach of contract claim.²³⁶ On remand, the district court entered a final judgment, keeping the permanent injunction.²³⁷ The defendants then moved to vacate and modify the judgment and moved for a new trial on the contract claim. Although the district court denied the motion for a new trial, the court narrowed the permanent injunction to only prohibit J&J from selling the

227. *Id.* at *3-5.

228. *Id.* at *3.

229. *Id.* at *3-4.

230. *Id.* at *3.

231. *Id.*

232. *Id.*

233. 445 F.3d 841 (5th Cir. 2006).

234. *Id.* at 843.

235. *Id.*

236. *Id.*

237. *Id.*

tubes in Distributors' territory.²³⁸ Among other things, Distributors' appealed the modification of the injunction.²³⁹

The Fifth Circuit held that the district court improperly modified the injunction.²⁴⁰ The Fifth Circuit observed that modification of an injunction is appropriate when the legal or factual circumstances justified the injunction have changed.²⁴¹ Although the defendants argued to the Fifth Circuit that the circumstances had changed, the Fifth Circuit held that the defendants waived their right to challenge the scope of the injunction since they did not assert this challenge to the district court.²⁴² The Fifth Circuit concluded that the district court abused its discretion in modifying the injunction and remanded to allow the district court to reinstate the original injunction.²⁴³

238. *Id.*

239. *Id.* at 844.

240. *Id.* at 850.

241. *Id.*

242. *Id.*

243. *Id.*