The GPMemorandum

TO: OUR FRANCHISE AND DISTRIBUTION CLIENTS AND FRIENDS

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

Quentin R. Wittrock, Editor of *The GPMemorandum*

Maisa Jean Frank, Assistant Editor

DATE: May 1, 2014—No. 180

Below are summaries of recent case decisions of interest to franchisors.

TRADEMARKS

FRANCHISOR USES UNIFORM DOMAIN-NAME DISPUTE-RESOLUTION POLICY TO OBTAIN CONTROL OVER INFRINGING DOMAIN

A franchisor whose trademark was being infringed in a domain name recently obtained transfer of the domain to its control through a Uniform Domain-Name Dispute-Resolution Policy ("UDRP") arbitration action. *U.S. Structures, Inc. v. Ginger Storm*, FA1401001540563 (NAF Mar. 5, 2014). Gray Plant Mooty represented the franchisor in the matter. In this case, U.S. Structures' trademark ARCHADECK® was infringed by the domain name archadeck-chicagoland.com. Chicagoland is a common reference to the Chicago metropolitan area, where U.S. Structures has an Archadeck franchisee. The offending domain pointed to a website that was simply a "link farm" from which the infringing registrant profited when users clicked on links to other sites, some of which were directly competitive with U.S. Structures' ARCHADECK® franchise system and services.

U.S. Structures began an action in the UDRP, a streamlined arbitration procedure established by the Internet Corporation for Assigned Names and Numbers for the resolution of trademark disputes concerning internet domain names. The UDRP governs generic top level domains ("gTLDs") including .com, .net, and .org, and the hundreds of new gTLDs that are currently in the process of being launched. To prevail, U.S. Structures had to show that the domain name at issue was confusingly similar to its trademark, that the registrant did not have any rights or legitimate interest in the domain name, and that the registrant registered and was using the domain name in bad faith. The domain name registrant did not respond to the complaint but, under UDRP rules, the single-arbitrator panel was still required to consider whether the complaining party satisfied the requirements for transfer or cancellation of the domain name and issue a written opinion. The panel found in favor of U.S. Structures on all of the elements. It ordered transfer of the domain name to U.S. Structures, which was then able to redirect the domain name to its Chicago-area franchisee's subpage.

COURT HOLDS FORMER FRANCHISEE IN CONTEMPT FOR FAILING TO COMPLY WITH TEMPORARY RESTRAINING ORDER

In *Ledo Pizza System, Inc. v. Singh*, 2014 U.S. Dist. LEXIS 46906 (D. Md. Apr. 3, 2014), a federal court in Maryland granted a franchisor's motion for contempt against a former franchisee who failed to comply with a temporary restraining order prohibiting his continued operation of a pizza franchise following termination. The franchisor, Ledo Pizza, terminated Singh's franchise agreement after he defaulted on several of his obligations under the contract. Ledo also filed suit for breach of contract and various violations of the Lanham Act. The court granted Ledo's request for a temporary restraining order ("TRO") requiring the defendant to immediately cease operations as a Ledo franchisee and cease and desist from the use of Ledo's trademarks and trade secrets. When Singh continued to operate his franchise and use Ledo's proprietary software after entry of the TRO, Ledo moved for sanctions and a contempt order based on Singh's refusal to comply with the court's directive.

The court held that a contempt order was warranted given that (1) the TRO constituted a valid decree of which Singh had constructive notice; (2) Singh's conduct violated the TRO; (3) Singh had sufficient knowledge of his violations of the TRO; and (4) Ledo suffered harm as a result of Singh's continued trademark infringement. The court also granted Ledo's request that Singh disgorge the profits he made from the operation of the franchise following the entry of the TRO and awarded Ledo some of the litigation expenses it incurred in bringing its motion. The court, however, denied Ledo's request for a permanent injunction against Singh because such a sanction would not directly remedy his contumacious conduct and Ledo had not shown that monetary damages would be inadequate to compensate it for the injury caused by violation of the TRO.

CLASS ACTIONS

CLASS CERTIFICATION DENIED IN CUSTOMER'S FEDERAL LAWSUIT REGARDING UNSOLICITED TEXT MESSAGES

A federal court in California denied class certification to a customer who received an unwanted text message from a promotional campaign by a franchisee. *Ryan v. Jersey Mike's Franchise Sys.*, 2014 U.S. Dist. LEXIS 42677 (S.D. Cal. Mar. 28, 2014). The plaintiff, Ryan, was one of 7,659 of the franchisee's customers who received a promotional text message relating to a loyalty card each obtained from the store. Ryan claimed that he had not given consent for such a text message, and he brought suit against both the franchisor and franchisee under the Telephone Consumer Protection Act and the California Business & Professions Code. The defendants argued that the customers who provided their telephone numbers when receiving the loyalty card consented to receiving the promotional text messages. In a sworn deposition, however, Ryan repeatedly testified that he had not provided his phone number, although he also testified that he did not remember other details of the conversation with the cashier.

The defendants filed a motion to deny class certification, arguing that because Ryan testified he had not volunteered his phone number, he could not represent a class of customers who had provided them. Ryan then filed a new affidavit attesting that he did not actually deny providing his phone number, but he simply was unable to remember either way. He argued that his inability to remember details of his encounter with the cashier made him more typical of the average customer, not less so. The court rejected Ryan's arguments and concluded that his inconsistent and uncertain testimony was insufficient to meet the "typicality" requirement for class certification. One could not conclude that his interest aligned with the interests of either class of customer, and no amount of discovery would change that. Based on this finding and the credibility concerns raised by the named plaintiff's inconsistent testimony, the court granted the defendants' motion.

INTERNET

COURT HOLDS THAT FRANCHISOR MAY BE LIABLE FOR DATA BREACH AT FRANCHISED LOCATION

A federal court recently denied the motion of Wyndham Hotels & Resorts to dismiss a complaint brought by the Federal Trade Commission for unfair or deceptive acts or practices based on breaches of the property management computer system used by Wyndham and its franchisees. *FTC v. Wyndham Worldwide Corp.*, 2014 U.S. Dist. LEXIS 47622 (D.N.J. Apr. 7, 2014). The FTC alleged that franchisor Wyndham Hotels &

Resorts, along with its affiliates, engaged in (1) deceptive practices by misrepresenting that it used "industry standard practices" and "commercially reasonable efforts" to secure the data it collected from guests, and (2) unfair practices by failing to protect customer data. Between 2008 and 2010, a criminal organization had hacked into the property management computer system multiple times—first through a franchisee's local computer network and then through an administrator account at one of the Wyndham entity's data centers. The hackers accessed credit card information from several hundred thousand guests of company-owned and franchised hotels, which allegedly resulted in $10.6 million in fraud losses. Wyndham moved to dismiss the complaint on the grounds that, among other things, the FTC did not sufficiently plead allegations to support its unfairness or deception claims, in part because the hotel businesses operated by franchisees are separate entities for which Wyndham is not legally responsible.

The court disagreed and rejected Wyndham's contention that "as a matter of law, it is necessarily a separate entity from Wyndham-branded hotels," such that each maintains its own computer networks and engages in separate data collection practices. The FTC alleged that Wyndham failed to provide reasonable security for the personal information collected by it and its franchisees, and the court found that allegation sufficient to withstand a motion to dismiss. The court also rejected Wyndham's argument that its privacy policy expressly disclaimed responsibility for the security of customer data collected by its franchisees. The court focused on other language in the same privacy policy that emphasized the "importance of protecting the privacy of individual-specific (personally identifiable) information collected about guests" and stated that it "applies to residents of the United States, ***hotels of our Brands located in the United States***, and Loyalty Program activities." The court found that a reasonable customer might have understood the policy to cover data security practices at both company-owned and franchised hotels.

EMPLOYMENT

GEORGIA FEDERAL DISTRICT COURT RULES THAT FRANCHISOR AND A RELATED ENTITY MAY BE A "JOINT ENTERPRISE" UNDER FEDERAL WAGE AND HOUR LAW

A federal district court in Georgia has conditionally certified a class of plaintiffs in a collective Fair Labor Standards Act wage and hour action brought against GoWaiter Franchise Holdings, LLC ("GFH"). *Wilson v. GoWaiter Franchise Holdings, LLC,* 2014 U.S. Dist. LEXIS 34837 (D. Ga. Mar. 18, 2014). In permitting the collective action to proceed, the court also granted the plaintiffs' motion to amend their complaint to assert that defendant GFH is a "joint enterprise" with the franchisor of the GoWaiter system, GoWaiter Business Holdings, LLC ("GBH"), for purposes of the FLSA. GBH, which is not named as a defendant in the lawsuit, franchises the GoWaiter franchise

GRAY PLANT MOOTY

system. GFH is a distinct entity from franchisor GBH, and its purpose is to take over GoWaiter franchises temporarily until they can be sold or transferred to a new owner to avoid a lapse in ownership, provide continuity of service, and preserve goodwill in a service area. The plaintiffs are food-service delivery drivers who worked at two franchise locations temporarily owned by GFH. They claim to have been improperly classified as independent contractors and paid a flat fee for each food delivery that amounted to less than federal minimum wage.

GFH sought dismissal of the drivers' action on the grounds that it does not generate sufficient annual revenue to be covered by the FLSA. In response, the drivers sought to amend their complaint to assert that GFH and GBH are a "joint enterprise," and that their collective revenue brought GFH within the purview of the FLSA. The district court granted the amendment. The court explained that, while independently owned franchises are typically not a "joint enterprise," the FLSA regulations provide that "*some* franchise . . . arrangements have the effect of creating a larger enterprise and whether they do or do not depends on the facts." The key inquiry is whether plaintiffs can show: (1) related activities, (2) unified operation or common control, and (3) a common business purpose. Applying this test, the district court found that the plaintiffs had alleged sufficient facts to potentially prove a "joint enterprise." The court found that GFH and GBH had a common business purpose and related activities because the purpose of GFH is to help GBH sell franchises. The court also noted that the two entities had mostly common ownership, had the same founder and president, had the same principal place of business, and operated with many of the same personnel. These facts were sufficient for the court even though GFH and GBH followed other corporate formalities, such as having separate bank accounts, insurance, payroll, taxes, and franchise disclosure statements. The court did note, however, that GFH was free to renew its arguments that no "joint enterprise" existed in a summary judgment motion at a later phase of the case.

ARBITRATIONS

CALIFORNIA FEDERAL COURT DENIES FRANCHISEE'S PRELIMINARY INJUNCTION MOTION TO PREVENT FRANCHISOR'S ARBITRATION OF DISPUTE

A federal district court in California recently denied a franchisee's motion for a preliminary injunction to prevent a franchisor from proceeding with arbitration, finding that the arbitration provision was neither procedurally nor substantially unconscionable. The dispute in *Moody v. Metal Supermarket Franchising America Inc.*, 2014 WL 988811 (N.D. Cal. Mar. 10, 2014), involved Metal Supermarket's exercise of its option to purchase Moody's assets upon termination and the proper purchase price for those assets. After Moody filed a state court action seeking a declaration with regard to the purchase price issue, Metal Supermarket removed the action to federal court and filed a

GRAY PLANT MOOTY

demand for arbitration. Moody moved unsuccessfully for a temporary restraining order to prevent the arbitration from moving forward and then sought the same relief through a preliminary injunction.

The court found that Moody had not established a likelihood of success on his challenge to the enforcement of the arbitration clause or irreparable injury. In particular, the court rejected Moody's argument that the arbitration clause was procedurally and substantively unconscionable under California law. First, the court noted that Moody had been represented by counsel in the process of signing the franchise agreements and had been able to negotiate some contract terms, and found little evidence of procedural unconscionability. Next, although the court agreed that Metal Supermarket's right to injunctive relief and the agreements' damages limitations might have been one-sided, it had no problem with the lack of mutuality in forum selection or attorneys' fees provisions. The district court noted that under California law, lack of mutuality in a one-sided contract did not necessarily render a contract invalid because it could provide a "margin of safety that provides the party with superior bargaining strength a type of extra protection for which it has a commercial need." Finally, the court rejected Moody's assertion that he would suffer irreparable harm, since he was only seeking monetary damages.

POST-TERMINATION INJUNCTIONS: NONCOMPETE COVENANTS

COURT ENFORCES NONCOMPETE AFTER EXPIRATION

In *Anytime Fitness, LLC v. Edinburgh Fitness, LLC*, 2014 U.S. Dist. LEXIS 50337 (D. Minn. Apr. 11, 2014), a federal court in Minnesota enjoined a former Anytime Fitness franchisee from violating a franchise agreements' post-expiration covenant against competition and from using the franchisor's proprietary customer data. After electing not to renew its franchise agreement, the franchisee had opened a new fitness club at the same location as its former Anytime franchise and used confidential customer data to solicit former Anytime clients. Anytime brought suit for breach of contract and trademark infringement, and it moved for a preliminary injunction.

In granting Anytime's motion, the court concluded that Anytime was likely to succeed on the merits of its claims. It held that the post-expiration covenant prohibiting competition within the former franchisee's exclusive area, or within twenty miles of any other Anytime club (or within five miles in cities with populations of 50,000 or more) for a period of two years was reasonable and enforceable. The court further held that Anytime was likely to succeed on its claim concerning the franchisees' use of customer data because the franchise agreement contained a provision stating that any customer data obtained while operating the franchise belonged to Anytime. Next, the court held that the franchisees' continued operation of the competing club and use of customer data caused irreparable harm to Anytime's goodwill and the franchise system as a whole. According to the court, the balance of harms weighed in favor of Anytime, as any harm suffered by the former franchisee was self-inflicted. Finally, the court noted that the public has an interest in the enforcement of bargained-for contract terms. The court also enjoined the former franchisee from using Anytime's trademarks.

PROCEDURE

FEDERAL COURT IN CALIFORNIA DENIES MOTION OF FRANCHISEE'S SUPPLIER TO INTERVENE IN FRANCHISOR'S ACTION AGAINST THE FRANCHISEE

A federal district court in California this month denied a restaurant foodservice supplier's motion to intervene in a franchisor's action to collect amounts owed by a former franchisee. *Jack In The Box, Inc. v. Mehta,* 2014 U.S. Dist. LEXIS 50575 (N.D. Cal. Apr. 9, 2014). Jack In The Box ("JIB") sued Mehta, its former franchisee, for failure to pay amounts owed, and JIB took over Mehta's restaurants pursuant to a court order in lieu of receivership that authorized JIB to operate the restaurants, collect all revenues, and pay reasonable and necessary bills for the protection of the restaurants. At the time of the takeover, Mehta owed McLane Foodservice, Inc., one of its suppliers, over $500,000. JIB voluntarily paid McLane $127,000 owed for food and supplies in the restaurants at the time of takeover, but denied further payment because JIB had no agreement with McLane. McLane sought to intervene in the action to recover the remaining amounts due.

The court analyzed whether McLane could intervene in the case as a matter of right or with the court's permission. It first considered the four elements necessary to create a right to intervene: (1) the motion must be timely; (2) the applicant must claim a significantly protectable interest relating to the property or transaction that is the subject of the action; (3) the applicant must be so situated that the disposition of the action may, as a practical matter, impair or impede its ability to protect that interest; and (4) the applicant's interest must be inadequately represented by the parties to the action. The court determined that McLane satisfied the timeliness element, and that its interest was not represented by the parties in the action. The court, however, found intervention as a right inappropriate because McLane could not establish a significantly protectable interest relating to the subject of the action. McLane's interest was in its contracts with Mehta, and the relationship between that interest and JIB's action was "too attenuated to justify intervention." The court also denied permissive intervention because the determination that McLane's interest was distinct from the claims in the franchise action meant that McLane had not established the common question of law or fact necessary for permissive intervention.

GRAY PLANT MOOTY

Minneapolis, MN Office

* **John W. Fitzgerald, cochair (612.632.3064)**
* Megan L. Anderson (612.632.3004)
* Sandy Y. Bodeau (612.632.3211)

Phillip W. Bohl (612.632.3019)
Jennifer C. Debrow (612.632.3357)
Danell Olson Caron (612.632.3383)
Elizabeth S. Dillon (612.632.3284)
* Ashley Bennett Ewald (612.632.3449)
* Michael R. Gray (612.632.3078)

Kelly W. Hoversten (612.632.3203)
Franklin C. Jesse, Jr. (612.632.3205)
Jeremy L. Johnson (612.632.3035)
* Richard C. Landon (612.632.3429)

Gaylen L. Knack (612.632.3217)
Kirk W. Reilly, cochair (612.632.3305)
Craig P. Miller (612.632.3258)
Bruce W. Mooty (612.632.3333)
John W. Mooty (612.632.3200)
Kevin J. Moran (612.632.3269)
Kate G. Nilan (612.632.3419)
Karli B. Peterson (612.632.3278)
* Matthew G. Plowman (612.632.3425)

Max J. Schott II (612.632.3327)
Michael P. Sullivan, Jr. (612.632.3350)
Michael P. Sullivan, Sr. (612.632.3351)
Henry T. Wang (612.632.3370)
Lori L. Wiese-Parks (612.632.3375)
* Quentin R. Wittrock (612.632.3382)

Washington, DC Office

Robert L. Zisk, cochair (202.295.2202)
* Julia C. Colarusso (202.295.2217)
* Maisa Jean Frank (202.295.2209)

Jan S. Gilbert (202.295.2230)
* Jeffrey L. Karlin (202.295.2207)
* Mark A. Kirsch (202.295.2229)
* Peter J. Klarfeld (202.295.2226)
* Sheldon H. Klein (202.295.2215)

Janaki J. Parmar (202.295.2235)
Iris F. Rosario (202.295.2204)
* Justin L. Sallis (202.295.2223)
* Stephen J. Vaughan (202.295.2208)
* David E. Worthen (202.295.2203)

Eric L. Yaffe (202.295.2222)
* Carl E. Zwisler (202.295.2225)

**** Wrote or edited articles for this issue.***

For more information on our Franchise and Distribution practice and for recent back issues of this publication, visit the **Franchise and Distribution** practice group at www.gpmlaw.com/practices/franchise-and-distribution.aspx.

GRAY PLANT MOOTY

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

Suite 700, The Watergate
600 New Hampshire Avenue, N.W.
Washington, DC 20037-1905
Phone: 202.295.2200

franchise@gpmlaw.com