The GPMemorandum

TO: OUR FRANCHISE CLIENTS AND FRIENDS

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

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This issue of *The GPMemorandum* focuses on topics primarily of interest to companies that use distributors and dealers rather than manage a business format franchise system. The distribution-related topics this quarter include dealer termination, antitrust, application of state statutes, and more.

ANTITRUST

FEDERAL APPEALS COURT AFFIRMS DISMISSAL OF VERTICAL PRICE FIXING ALLEGATIONS

In one of the first post-*Leegin* appellate decisions in the vertical pricing context, the Eleventh Circuit this month rejected on the pleadings the antitrust claims brought by consumers against a manufacturer in *Jacobs v. Tempur-Pedic North Am., Inc.*, 2010 U.S. App. LEXIS 24638 (11th Cir. Dec. 2, 2010). The complaint alleged, and was taken as true, that the manufacturer and its distributors agreed as to minimum resale prices for the manufacturer's mattresses. The appeals court agreed with the trial court that the pleading of "visco-elastic foam mattresses" as a relevant product market cannot stand without more facts than the plaintiffs had set forth. Under today's heightened pleading standards in federal cases, the court held that a plaintiff must plead more compelling facts regarding the relevant market and other required elements. The same result was true as to the plaintiffs' claim of horizontal price fixing. The theory underlying that claim was that the manufacturer was a competing distributor through its own Web site, which also adhered to the established minimum pricing. But the Eleventh Circuit noted that dual distribution practices are typically viewed as vertical, and also held that the plaintiffs had not made the required "plausible" showing of an unlawful agreement.

The court denied the plaintiffs' request to conduct further discovery, as well as their request to replead the case. This decision will be frequently cited by manufacturers and suppliers in defending against claims that they are engaged in price fixing with distributors.

FIFTH CIRCUIT UPHOLDS DISMISSAL OF PLAINTIFF'S AMENDED COMPLAINT IN *PSKS v. LEEGIN*

In affirming the dismissal of the plaintiff's second amended complaint, the Fifth Circuit appears to have put an end to the parties' long-running legal battle in a case that resulted in the United States Supreme Court's 2007 reversal of the century-old *per se* ban on minimum resale price agreements. *PSKS, Inc. v. Leegin Creative Leather Prod., Inc.*, No. 09-40506 (5th Cir. Aug. 17, 2010). Plaintiff PSKS had been a retailer of the high-end Brighton® brand of women's accessories manufactured by Leegin. Leegin had instituted a minimum resale price maintenance policy through which it induced retailers to agree to follow Leegin's suggested pricing policy at all times, and it threatened and ultimately refused to deal with any retailer that violated its pricing policy by offering discounts. Following the Supreme Court's reversal and remand, PSKS filed a second amended complaint alleging the same violations but adding relevant market allegations, as it was required to do under the rule of reason. Both of PSKS's two alternative product markets were rejected by the district court, which accordingly dismissed the second amended complaint for failure to state a claim.

In affirming the district court's decision, the Fifth Circuit held that the district court properly rejected the two alternative product markets alleged: (1) the "retail market for Brighton's women's accessories"; and (2) the "wholesale sale of brand-name women's accessories to independent retailers." The court agreed that Brighton products do not constitute their own market and only in rare "lock-in" situations will a single brand of product or service constitute a relevant market for antitrust purposes. The court further agreed that "wholesale sale" does not adequately define a relevant market, "because the relevant market definition must focus on the product rather than the distribution level." Also, the court held that "women's accessories" is too broad and vague a definition to constitute a market. As for alleged discussions about discounts between Leegin and its dealers, the court declared: "A manufacturer's discussion of pricing policy with retailers and its subsequent decision to adjust pricing to enhance its competitive position do not create an antitrust violation or give rise to an antitrust claim."

STATE FRANCHISE LAWS

MINNESOTA COURT FINDS THAT MINIMUM SALES REQUIREMENT AND PURCHASE OF EXCESS INVENTORY CAN CONSTITUTE FRANCHISE FEES

A Minnesota federal court in *Coyne's & Co. v. Enesco, LLC*, 2010 U.S. Dist. LEXIS 83630 (D. Minn. Aug, 16, 2010), issued a lengthy opinion addressing cross motions for summary judgment filed by a Minnesota distributor and the assignee of its original supplier, Enesco, LLC. While the court addressed several issues, most notably it held that Enesco could not succeed on its motion for summary judgment on the plaintiff's claim under the Minnesota Franchise Act (MFA), finding that both sides had put forth viable arguments as to whether their relationship included an indirect franchise fee.

Coyne's & Co. entered an exclusive North American distributorship agreement with Country Artist, Ltd. (CA) for a product line manufactured in England. Years later, CA was placed into receivership and its business and assets were sold to Enesco, and the receivers terminated Coyne's distributorship agreement. Coyne sued Enesco claiming, among other things, that Enesco's termination of the distributorship agreement violated the MFA. Although Enesco pointed out that the distributorship agreement expressly stated it created no franchise relationship, the court held that Coyne could not waive its protections under the MFA even with "explicit written language." In considering the MFA claims, the court focused on whether Coyne had paid a "franchise fee." The court noted that "reasonableness" is the standard for determining whether a franchise fee exists. A 35-50 percent markup paid by Coyne to CA could reflect CA's profits on its products, the court wrote, indicating that it could reflect a bona fide wholesale price, rather than a franchise fee. The court also found that a minimum sales requirement could be a franchise fee "if the prices exceeded bona fide wholesale prices or if the distributors were required to purchase amounts or items that they would not purchase otherwise." A requirement to purchase excess inventory could also be a franchise fee if the inventory was not liquid. In the end, the court decided that there was at least a genuine issue of fact as to whether an indirect franchise fee existed, and denied summary judgment accordingly.

WISCONSIN APPEALS COURT REJECTS SEVENTH CIRCUIT'S COMMUNITY OF INTEREST TEST

The Wisconsin Court of Appeals has rejected Seventh Circuit jurisprudence concerning the "community of interest" test as applied to the Wisconsin Fair Dealership Law (WFDL). In *The Water Quality Store v. Dynasts Spas, Inc.,* 2010 Wisc. App. Lexis 550 (Wisc. Ct. App. Jul. 15 2010), a Wisconsin retailer had been selling the defendant manufacturer's line of spa and spa equipment, on a nearly exclusive basis, for approximately seven years. The manufacturer terminated the relationship without good cause and without observing the notice and opportunity to cure requirements of the WFDL. On summary judgment, the manufacturer argued that the WFDL did not apply to the parties' relationship because the retailer could not establish that there was a "community of interest" between the parties, as required under the WFDL. Wisconsin Supreme Court cases interpreting the WFDL have set forth a multi-pronged test for the community of interest requirement, looking at ten different facets of the manufacturer's relationship with the dealer. For WFDL cases arising in federal court, the Seventh Circuit has articulated a slightly different test for community of interest, looking to whether the manufacturer has a bargaining power advantage so as to have the dealer "over a barrel" in the relationship. More recent Seventh Circuit cases have interpreted the "over a barrel" test such that if the dealer has been able to replace the manufacturer's line of products with a substitute brand, the manufacturer is deemed not to have the dealer "over a barrel," negating the existence of a community of interest and, as a result, application of the WFDL.

The Wisconsin Court of Appeals rejected the Seventh Circuit approach and reaffirmed the Wisconsin Supreme Court's ten-facet test. Evidence that the plaintiff had successfully mitigated its damages by replacing the manufacturer's line of spas with a competitor's products was deemed irrelevant. Denial of the defendant's summary judgment motion was therefore upheld. The decision underscores the significant differences in the way community of interest will be analyzed in Wisconsin state court versus in the federal court system. This provides manufacturers with greater incentive to secure federal court jurisdiction whenever possible in WFDL cases.

COURT ENJOINS TERMINATION OF DEALER AGREEMENT, FINDING NEW JERSEY FRANCHISE PRACTICES ACT LIKELY WILL APPLY

In *Engines, Inc. v. MAN Engines & Components, Inc.*, 2010 U.S. Dist. LEXIS 76541 (D.N.J., July 29, 2010), a New Jersey federal court granted a preliminary injunction prohibiting MAN Engines & Components, Inc. from terminating its dealer agreement with Engines, Inc. because the relationship is likely a franchise under the New Jersey Franchise Practices Act (NJFPA). Engines was an authorized provider of repair, conditioning, and replacement services for MAN for many years. During that time, Engines made certain investments in its business in connection with its activities under the dealer agreement, including purchasing tools and equipment and sending technicians to training. After becoming dissatisfied with the quality of Engines' repair work, MAN sought to terminate the dealer agreement pursuant to the agreement's termination "without cause" provision. In response, Engines sued to enjoin MAN from terminating, alleging that the NJFPA applied to the relationship and provided that an agreement cannot be terminated without cause.

The court granted Engines' request for injunctive relief, determining that the relationship constituted a "franchise" under the NJFPA. As part of its analysis, the court concluded that a "community of interest in the marketing of goods and services" existed between MAN and Engines because Engines was required "to make a substantial investment in goods or skills that will be of minimal utility outside the franchise." Engines had made significant franchise-related investments by purchasing MAN parts and specialty tools, promoting its relationship with MAN, and sending its employees to MAN training seminars. The court rejected MAN's argument that there was no community of interest because Engines' investments were made voluntarily and were not required under the terms of the dealer agreement. In doing so, the court looked beyond the terms of the dealer agreement and held that the nature of the relationship contemplated the investments by Engines.

TERMINATIONS

COURT FINDS NO JUST CAUSE FOR TERMINATION IN OHIO ABSENT BREACH OF DISTRIBUTORSHIP AGREEMENT

In September, an Ohio federal court granted the motion for preliminary injunction brought by a group of alcohol beverage distributors, enjoining their supplier from enforcing the terminations of their distributorships. The case is *Tri-County Whole Distrib., Inc. v. The Wine Group, Inc.*, 2010 U.S. Dist. LEXIS 92598 (D. Ohio Sep. 2, 2010). In granting the motion, the court held that the supplier did not demonstrate that it had "just cause" to terminate the distributorships under the Ohio Alcoholic Beverages Franchise Act because the distributors had not breached their agreements. Rather, the supplier simply wanted to move distribution of its wine products in Ohio to a single statewide distributor. The court found that, although the Franchise Act does not define "just cause," it does provide that just cause does not include the unilateral decision to alter a franchise for reasons unrelated to a breach, and that a rational business purpose is not enough to permit termination.

COURT REJECTS DEALER'S CLAIMS FOR WRONGFUL TERMINATION

An Illinois federal court recently issued two decisions in a case rejecting a dealer's claims that it was improperly terminated. In *Scholl's 4 Seasons Sports, Inc. v. Arctic Cat Sales, Inc.*, 2010 U.S. Dist. LEXIS 110360 (N.D. Ill. Oct. 18, 2010), the court denied the plaintiff's motion for leave to amend its complaint to allege a violation of the Illinois Equipment Fair Dealership Law (IEFDL). The court found that dealers like the plaintiff who sold only ATVs and snowmobiles were not covered by the law. Although the IEFDL was amended in July 2010 to specifically include ATV dealers, the plaintiff's dealership was terminated a year earlier, and the law did not apply retroactively.

Just one month later, the court granted defendant Arctic Cat's motion for summary judgment on all of the plaintiff's claims. 2010 U.S. Dist. LEXIS 121235 (N.D. Ill. Nov. 16, 2010). Without deciding that plaintiff qualified as a franchisee, the court held that Arctic Cat's termination did not violate the Illinois Franchise Disclosure Act (IFDA) because the plaintiff's failure to pay for inventory constituted good cause to terminate. The court also ruled that Arctic Cat did not violate the IFDA by failing to specify in the default notice that the plaintiff would be terminated if it did not cure its breach. "Given that [Arctic Cat] attempted to collect plaintiff's debt for months," the ten day notice given by Arctic Cat was reasonable, and therefore it complied with the IFDA.

CHANGE IN IDENTITY OF DISTRIBUTOR NEGATES CLAIM BY DEALER UNDER NORTH CAROLINA WINE ACT

In *The Country Vintner of North Carolina v. Gallo Winery, Inc.,* 2010 U.S. Dist. Lexis 110615 (E.D.N.C. Oct. 18, 2010), a wine retailer sued for wrongful termination under the North Carolina Wine Distribution Agreements Act. The plaintiff, Country Vintner, had previously been a wholesaler of the Alamos brand of Argentinean wine for the entire state of North Carolina. In 2009, the manufacturer of Alamos replaced its original U.S. distributor (Billington) with a new distributor, Gallo. Gallo, upon taking over U.S. distribution of Alamos wine, began supplying its own wholesalers, effectively preventing Country Vintner from continuing to wholesale Alamos in North Carolina.

Country Vintner sued, claiming that Gallo had terminated its distribution agreement without providing the statutory notice required under the Wine Act. However, Country Vintner had no written agreement with Gallo, Billington, or the wine's manufacturer. Further, Country Vintner did not claim that the new distributor, Gallo, had ever orally agreed to continue supplying it with wine. Instead, Country Vintner asserted that an "agreement" exists under the Wine Act whenever a dealer has been given distribution rights. The court rejected this interpretation and looked to the plain meaning of the statute. Because Gallo, the new distributor of Alamos, had never entered into an agreement with Country Vintner, Gallo was not bound by the Wine Act's notice requirements and was free to distribute through wholesalers of its own choosing.

CONTRACTS

COURT GRANTS SUMMARY JUDGMENT TO AUTOMOBILE MANUFACTURER ON DEALER'S BREACH OF CONTRACT CLAIM

In *Landreth, Inc. v. Mazda Motors of Am., Inc.*, 2010 U.S. Dist. LEXIS 108080 (S.D. Ind. Oct. 7, 2010), the plaintiff Mazda dealer sued Mazda Motors of America alleging that the manufacturer had broken its promise to award plaintiff an additional dealership. The plaintiff admitted that Mazda had not entered into a written agreement to grant it an additional dealership, but contended that Mazda's representatives had told the plaintiff that it would receive a new dealership when the opportunity arose. Mazda moved for summary judgment on that claim, arguing that no contract could exist in the absence of a writing.

The court agreed and granted Mazda's motion. The court found that the plaintiff had not presented any proof that the parties entered into an enforceable contract concerning the dealership. While the plaintiff presented evidence of numerous discussions about the possibility of the plaintiff taking over a dealership, it failed to present any proof that those discussions led to a final agreement. The court concluded that the evidence did not show a binding promise had been made or that the parties had agreed on any material terms.

TORTIOUS INTERFERENCE

COURT RULES THAT COMPETITOR PRIVILEGE DEFENSE TRUMPS TORTIOUS INTERFERENCE CLAIM

In *Utility Trailer Sales of Kansas City, Inc. v. MAC Trailer Mfg., Inc., et al.,* 2010 LEXIS 83142 (D. Ka. Aug. 16, 2010), a Kansas federal court held that the "wrongful means" element needed to defeat the competitor privilege on a tortious interference claim is a higher standard than "malice." The case arose out of a 2000 dealer agreement that granted Utility Trailer (UT) a nonexclusive license to sell trailers manufactured by MAC Trailer Manufacturing. Within a specified territory, however, UT was to be the sole authorized dealer. Importantly, the dealer agreement did not restrict MAC or any MAC dealer outside of UT's territory from selling MAC products in the territory. MAC attempted to terminate the dealership agreement in April 2008 and again in 2009. In 2008, Summit, a competitor of UT located outside the territory, began selling MAC trailers within the territory. UT sued MAC and Summit in 2008 alleging, among other things, tortious interference with a prospective business expectancy or relationship. The jury returned a verdict in UT's favor on the claim of tortious interference with a competitive business advantage. MAC and Summit argued that judgment as a matter of law should be entered because there was no evidence of malice and they were protected by the "competitor privilege."

The court granted the motion and determined that, while the evidence did not clearly indicate that MAC's behavior was not malicious, UT failed to produce sufficient evidence that MAC's and Summit's actions were not protected under the competitor privilege. The court noted that under the competitor privilege a plaintiff cannot be held liable for tortious interference with a prospective business relationship if: (a) the relationship concerns a matter involved in the competition between the actor and the plaintiff; (b) the actor does not employ wrongful means; (c) its action does not create or

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continue an unlawful restraint of trade; and (d) its purpose is at least in part to advance its interest in competing with the plaintiff. The court focused on the "wrongful means" element of the competitor privilege test and determined that the standard for establishing wrongful means requires a showing that the defendant acted with "independently actionable conduct," a more difficult standard to meet than malice. Because the acts alleged by UT did not constitute independently actionable conduct, there was no legally sufficient basis on which the jury could have concluded that the competitor privilege did not apply.

INTERNET ISSUES

FIRST CIRCUIT AFFIRMS HONDA'S DECISION CONCERNING INTERNET SALES OF EXTENDED WARRANTIES

In *Saccucci Auto Group v. American Honda Motor Co.,* 617 F.3d 14 (1st Cir. Aug. 4, 2010), the court held that a car manufacturer's decision to suspend temporarily the sale by its dealers of extended warranty plans over the Internet did not violate the Rhode Island "Dealer Act." Although Honda had allowed its dealers to sell extended warranties online since 1997, the practice had come under criticism by some dealers, including its Dealer Advisory Board, which complained that the lower prices offered for the plans over the Internet damaged goodwill with customers who were sold higher-priced plans at dealerships. As a result, Honda formed a committee that studied the issue for several months and considered alternatives to allowing the extended warranties to be sold online. In the end, Honda announced a temporary prohibition on the sale of the extended warranties over the Internet and established a range of graduated penalties for noncompliant dealers. In response, a Honda dealer in Rhode Island sued the company for, among other things, violation of the Dealer Act, claiming that the prohibition was coercive, arbitrary in nature, and predatory in practice. A federal district court granted Honda's motion for summary judgment, holding that the Dealer Act did not apply and, even if it did, the prohibition on Internet sales did not violate the statute.

The First Circuit affirmed the lower court's decision on the ground that Honda's decision did not violate the Dealer Act, sidestepping the question of whether the statute applied at all. The court concluded that Honda's decision was not arbitrary because the company had studied the question thoroughly and taken alternative measures into account. Further, the court held that the prohibition on Internet sales did not constitute a "wrongful demand" on the dealer because the decision was "at bottom, a commercial judgment" based on its concern that the sales were "harming brand image and loyalty" and leading some dealers to offer competing warranty plans. Similarly, the court found that Honda's action was not a predatory practice because there was nothing in the record that suggested that it was taken solely for its own benefit. "To the contrary," the court found, "the evidence indicates that Honda enacted the policy to protect brand loyalty and image, something in the best interest of Honda's dealers."

CHOICE OF FORUM/VENUE

COURT APPLIES FEDERAL LAW TO UPHOLD FORUM SELECTION CLAUSE

A federal magistrate judge in Oklahoma recently upheld a forum selection clause found in a dealer agreement in *Sundowner Trailers, Inc. v. Snyder Serv., Inc.*, 2010 U.S. Dist. LEXIS 105183 (E.D. Okla. Sept. 30, 2010). The dispute arose when Synder, a horse trailer dealership, ceased operation and requested that Sundowner, the manufacturer, repurchase all of its unsold equipment and parts at 90-100% of net cost. A Tennessee law requires suppliers to repurchase inventory, at the retailer's option, in certain situations when the retailer's contract is terminated. Sundowner sought a declaratory judgment that it need not repurchase such items, claiming the Tennessee law did not apply because the products did not fall within the definition of "inventory," and the dealership chose to cancel the dealer agreement.

Pursuant to a forum selection clause in the dealer agreement, Sundowner brought the case in the Eastern District of Oklahoma. Dealer Snyder, which is located in Tennessee, moved to transfer venue to a federal court in Tennessee, citing a Tennessee statute that voids contractual terms restricting choice of forum. The judge denied the dealer's motion. The court found that since the jurisdictional basis for the action was diversity, federal procedural law applied rather than the Tennessee statute. Thus, the court upheld the forum selection clause in the dealer agreement and found the case could properly be brought in Oklahoma. However, the court noted that the ruling would not preclude application of Tennessee substantive law to the underlying issues in the case.

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