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PERSPECTIVE

For California franchises, there's no place like home

By Barry Kurtz and David Gurnick

Competitors of all kinds know home court advantage helps them win. Home court advantage refers to the psychological, procedural and logistical edge gained by competing in a familiar setting, where one has better knowledge of the rules and conditions, and where spectators and possibly referees, judges and juries tend to be more supportive. Sports teams, business negotiators, entertainers and litigators all want the home court advantage.

In litigation, jockeying over home court occurs in a battle over "venue." Extensive rules and decisional law have developed addressing how the question of venue will be decided.

In late 2013 the U.S. Supreme Court issued an important decision on venue in business litigation. *Atlantic Marine Construction Co. v. U.S. Dist. Court*, 134 S.Ct. 568 (2013). The decision's impact is already being felt in litigation between franchisors and franchisees. The current U.S. Supreme Court decides many important cases by a 5-4 vote. Four justices (John Roberts, Clarence Thomas, Antonin Scalia and Samuel Alito) lean conservative. Four justices (Ruth Bader Ginsburg, Stephen Breyer, Sonia Sotomayor and Elena Kagin) tilt liberal. Frequently, the majority is whichever group centrist Justice Anthony Kennedy joins. But the *Atlantic Marine* decision was *unanimous*. This means despite the political schism on the court, all nine justices agreed.

Franchise agreements often specify the state, county or city where disputes will be litigated. Because franchisors write the agreements, many of them specify that venue will be where the franchisor is headquartered. A smaller number of franchise agreements allow venue where the franchisee is located. Some specify a neutral venue. A few are silent.

Atlantic Marine was not a franchisor-franchisee dispute, but concerned an agreed venue clause. A construction company, Atlantic Marine, entered into a contract with the U.S. Army to build a structure at the Fort Hood Army Base in Texas. Atlantic Marine also entered into a subcontract for a management company to work on the project. The subcontract said all disputes would be litigated in Virginia. But when a dispute arose, the management company sued Atlantic Marine in Texas.

It's common for lawyers, after conferring with clients, to start lawsuits locally, or in a court of choice, despite what the parties' agreement says about venue. Courts have applied a variety of legal theories to avoid contractually agreed locations. Doctrines such as giving weight to the plaintiff's choice of forum, or changing venue due to significant inconvenience to the defendant (forum non conveniens) are examples.

In *Atlantic Marine*, the Supreme Court said a mutual agreement on where disputes will be resolved "represents the parties' agreement as to the most proper forum"; and "enforcement of valid forum-selection clauses, bargained for by the parties, protects their legitimate expectations and furthers vital interests of the justice system." Therefore, the court ruled, "a valid forum-selection clause should be given controlling weight in all but the most exceptional cases."

Within just eight months, *Atlantic Marine* has dramatically affected many franchising cases. In recent published decisions Burger King was able to get a franchisee lawsuit moved to its home court in Florida, *Caribbean Restaurants, LLC v. Burger King Corp.*, 2014 WL 2465133 (D.P.R. June 03, 2014), and other franchisors such as Country Inn & Suites, Hawthorne Suites, Salad Works and Allegra Network were able to defeat franchisee efforts to move cases away from franchisor home courts. *Country Inns & Suites v. Praestans One LLC*, 2014 WL 3420800 (D.Minn., July 14, 2014); *Hawthorn Suites Franchising Inc. v. Meriden One Lodging LLC*, 2014 WL 2926533 (D.N.J., June 27, 2014); *Saladworks LLC v. Sottosanto Salads LLC*, 2014 WL 2862241 (E.D. Pa., June 24, 2014); *Allegra Holdings LLC v. Davis*, 2014 WL 1652221 (E.D. Mich. 2014).

In July, the U.S. District Court for the Central District of California, considered *Atlantic Marine* in a franchise case, *Frango Grille USA Inc. v. Pepe's Franchising Ltd.* (CV 14-2086 DSF). Pepe's, based in England, franchises quick service restaurants featuring chicken. Frangos is a Los Angeles-based master franchisee of Pepe's which sued in Los Angeles, on state law claims, despite an agreement setting venue in London. Citing *Atlantic Marine*, Pepe's asked the court to enforce the venue agreement. The court declined, noting that California law, Business and Professions Code Section 20040.5, voids any agreement in a franchise relationship that restricts venue to a forum outside California. The court noted the *Atlantic Marine* precedent enforces valid agreements on venue, but the application of Section 20040.5 rendered the contractual provision invalid.

In contrast, when franchisors sued California franchisees outside California, several courts refused franchisee requests to apply Section 20040.5 to void forum selection agreements. In *TGI Friday's Inc. v. Great Nw. Rests.* Inc., 652 F.Supp.2d 750, 760 (N.D.Tx. 2009), a U.S. district court enforced an agreement setting venue in Texas over a California franchisee's Section 20040.5 objection, noting "Defendants do not explain ... why this court should apply California law to void a franchise agreement that provides that Texas law applies to all matters relating to the agreement, and that Texas is the forum for any disputes relating to the agreement." In *Maaco Franchising Inc. v. O. Tainter*, 2013 WL 2475566 at *4 (E.D.Pa. 2013), a district court noted that among courts outside California, "the majority have not invalidated forum selection clauses or opted to transfer cases to California pursuant to Section 20040.5."

Out-of-state courts apply home state law to the parties' relationship, and when home state law applies, California Section 20040.5 does not. As another example, a U.S. district court in Michigan noted: "it would appear that Defendants have waived their right to contest venue. Defendants attempt to avoid this conclusion by asserting that the ... forum selection clause is invalid under ... [Section]20040.5 ... This argument is unpersuasive for a number of reasons ... The relevant contracts expressly state that they should be interpreted under Michigan law ... and such choice-of-law clauses are not facially invalid under the [California Franchise Relations Act]." *Hoodz Int'l. LLC v. Toschiaddi*, 2012 WL 883912 at *4 (E.D. Mich. 2012).

The import for franchisors and franchisees of *Atlantic Marine*, and the analysis applied within and outside California, is that the best way to obtain one's desired forum in litigation is to be the first to sue in one's preferred venue. A franchisor who sues in an agreed venue outside California can invoke *Atlantic Marine* to insist the venue agreement should be enforced, and a franchisee's claim under Section 20040.5 should be rejected. In contrast, a franchisee who brings litigation in California, despite an agreement setting venue elsewhere, can argue that Section 20040.5 voids the venue clause, and therefore, as in *Pepe's*, *Atlantic Marine* should not apply.

Atlantic Marine was decided under the federal venue statute, 28 U.S.C. Section 1404. Venue is considered to be procedural rather than substantive law. While *Atlantic Marine* is therefore binding as to procedure in federal court, under the well-known *Erie* doctrine, *Erie v. Tomkins*, 304 U.S. 64 (1938), it is influential, but not necessarily binding in state courts. Regardless, there will no doubt be multiple court decisions in the future on the consequences of *Atlantic Marine* in franchisor/franchisee and other business litigation matters.

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