California Decides Franchisor's Forum Selection Invalid, Despite Supreme Court Ruling

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SANTA ANA, California – A California federal court handed down a significant ruling last week denying a franchisor's motion to dismiss and allowing the franchise owner to proceed with its lawsuit in the state.

Pepe's Grilled Chicken's franchise agreement contained a "choice of forum" clause that required any lawsuit between franchisee and franchisor to be fought in the courts of London, England, where Pepe's is located. California law, however, states that any contract provision requiring a franchisee to bring a lawsuit outside of California is void.

The U.S. Supreme Court issued a decision last December that stated any valid forum selection clause should be enforced. Represented by Gray Plant Mooty, Pepe's argued that under the high court's decision, the case had to be dismissed or transferred to London.

But District Judge Dale S. Fischer rejected Pepe's position that the Supreme Court's decision in ***Atlantic Marine Construction Co., Inc. v. U.S. District Court for the Western District of Texas*** controlled, and that California law did not apply. The court invoked California statute to rule that the franchisor's contract provision was invalid and unenforceable. As a result, franchisee Frango Grille USA, Inc. was allowed to litigate its case against Pepe's in California instead of London, England.

W. Michael Garner, representing Frango Grille, declared that the California court's decision is straightforward and correct. He said it begins with *Atlantic Marine's* admonition that the holding in that case applies only to "valid forum selection clauses." It then proceeds to find that the California Franchise Relations Act's provision that holds forum selection clauses to be void and unenforceable rendered in contractual forum-selection clause in *Frango* to be "invalid." The Minneapolis attorney said under governing Ninth Circuit law, the court found the contractual forum selection clause unenforceable and denied the motion to dismiss or transfer.

Garner said there are two other cases that are arguably at odds with *Frango v. Pepe's.* In *Saladworks, LLC v. Sotosano Salads, LLC,* Pennsylvania federal court rejected the argument that California franchise law, CFRL, invalidated the contractual forum selection clause choosing Pennsylvania. In the second case, *Caribbean Restaurants, LLC v. Burger King Corp.*, the court rejected the argument that a portion of Puerto Rico's law that voided forum selection clauses required denial of a motion to transfer pursuant to a contractual provision requiring suit to be brought in Florida, where Burger King is located. The court held, citing prior precedent, that freely-negotiated contractual provision would take precedence over Puerto Rico law.

Garner said his case can be distinguished from the two cases on the ground that it relied on the fact that Pepe's had come into California and registered with the state to offer and sell franchises. "Thus, it deliberately subjected itself to California's regulation; the California Franchise Regulation Act's ban on forum selection clauses was incorporated as part of the franchise agreement," he explained.

The franchisee attorney said ultimately, his *Frango* case, and *Saladworks* and *Caribbean Restaurants* may be on a collision course. He explained that *Saladworks* and *Caribbean Restaurants* point to the *Atlantic Marine* case and its predecessor *Ricoh,* as standing for the proposition that venue is strictly a matter of federal procedural law, and that federal law should govern in all instances. "Frango, however, recognizes that a choice of venue clause is a matter of contract law, and that states have a role in governing the contracts of their citizens," Garner said.

"In that respect, then, the CFRA's ban on forum selection clauses is no different from state usury laws or California's refusal to enforce post-termination non-competes. And substantive state contract law is not the same as *federal venue law,"* he continue.

Garner said failure to make that distinction would result in state and federal courts giving different results on the same choice-of-venue question. "More ominously, failure to make the distinction would result in federal procedural law dictating state substantive law. The distinction is critical, and one that the Supreme Court has not yet made," he said.

"What is certain," Garner concluded, "is that we can look forward to conflicting decisions and further confusion until the higher courts squarely address the issue."

Other attorneys weigh in

Senior attorney Jesse C. Ehnert of Paris Ackerman & Schmierer in New Jersey said federal courts in his state view a forum-selection clause as an important consideration in determining whether to transfer a case. With the 2013 Supreme Court decision, other "private interest" factors, including convenience of the parties and witnesses based on location and financial conditions, which used to apply no long do.

"The result is that there is now a very heavy burden on a party seeking to avoid the preselected forum. In the franchise context, that is good news for franchisors who will be more able to keep litigation in their preferred courts, and bad news for franchisees who may prefer to litigate elsewhere," Ehnert said. He stressed that this should serve as a warning to prospective franchisees that they should have a franchise attorney looking out for their best interest in these contract issues.

Attorney David Gurnick of Lewitt Hackman in Encino, California said this issue on forum selection is not simple, and it is a very timely issue. He agrees that there are two conflicting rules in place today. "The U.S. Supreme Court saying that an agreed venue shall be pretty much enforced. Then you have California and a few other states saying any venue agreement that sets venue outside the state is void. So those two issues conflict with each other," he explained.

Gurnick said if franchisees or franchisors want to have the best chance to be in their preferred venue in a legal action, they have to sue first. "If you are a franchisor with a franchisee in California and you don't want to litigate in California, you have to sue first in the venue stated in the franchise agreement. More than likely, that state will apply the rules and find that *Atlantic Marine* applies.

"If you are a California franchisee and your franchisor is out of state, and you have an out-of-state venue clause in your franchise agreement, you have to sue first in California. You have to make the argument that Judge Fischer ascribed to, that the agreed venue clause in your agreement and the *Atlantic Marine* decision only applies to valid venue. Of course, you then invoke the section of California's law that voids a venue clause setting venue outside of California.

Gurnick said he is currently litigating this very "forum selection" issue. "I currently have three cases with three different franchise companies in three states outside of California." He said the reason he is involved is that all of them have touched California. "We are fighting this issue of what state the litigation should take place. With my three cases and the *Pepe's* lawsuit, you can interpret this issue of forum selection as being widespread."

Attachment	Size
Pepe's U.S. District Court Decision.pdf	22.46 KB

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