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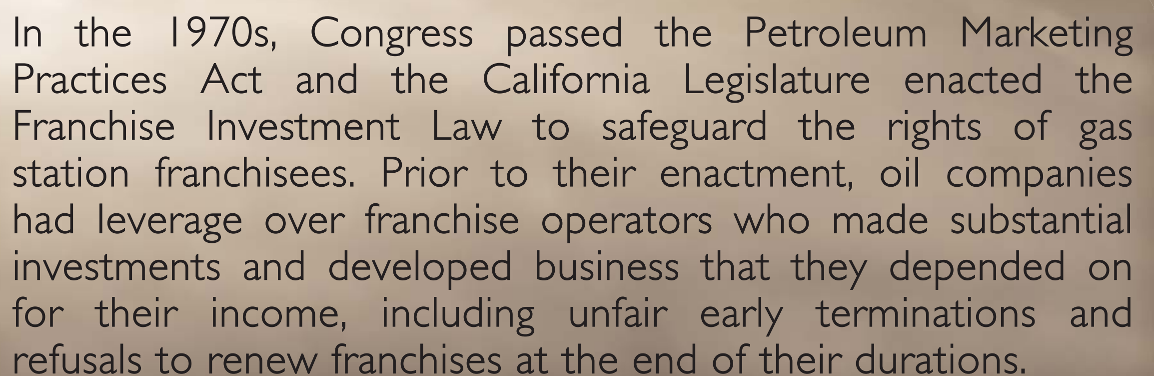
Gas Station Franchises:
Federal and California State Regulations

By David Gurnick and Matthew J. Soroky



In the 1970s, Congress passed the Petroleum Marketing Practices Act and the California Legislature enacted the Franchise Investment Law to safeguard the rights of gas station franchisees. Prior to their enactment, oil companies had leverage over franchise operators who made substantial investments and developed business that they depended on for their income, including unfair early terminations and refusals to renew franchises at the end of their durations.

IN 2013, MOTOR FUEL WAS AVAILABLE AT ABOUT 150,000 locations across the United States. This was a 25 percent decline from two decades earlier when the number of gas stations exceeded 202,000.[1] The number of gas stations is expected to continue to fall and there are many reasons why.[2]

A scarcity of real estate and rising property values, particularly in metropolitan areas, increasing fuel economy standards, rising fuel prices, alternative fuels, concern for the environment, more hybrid and all-electric vehicles, the growing use of mass-transit, and even motorized scooters,[3] all encourage people to drive less and use less fossil fuel. An increasing number of gas stations at large retail stores like Walmart and Costco mean higher volumes of gas can be pumped at fewer stations, while a new app-based business provides delivery of fuel and fill-up at the customer's own location.[4]

For decades, motor fuel has been distributed largely by franchisees. ARCO, Chevron, Exxon, Mobil, Shell, Texaco and Union 76[5] are readily recognizable franchise brands in California. Suppliers—typically oil refiners like Exxon, Shell and Standard Oil—grant franchises to retailers to operate and supply fuel to branded service stations. This model emerged in the early 1900s[6] due to the many benefits of franchising the distribution of gasoline. As summarized by a Court of Appeals:

> Every pumping station is an advertisement; each bears the name of the oil producer whose gasoline is supplied therefrom, if the retailer honestly observes his bargain. The system is a great convenience to the public; it has increased enormously the ease with which motor drivers may obtain "gas" even in remote and thinly settled districts. It is the only method known or suggested, of keeping before the consuming public the oil manufacturers' trade-mark, and it has largely succeeded the system of distributing oil in barrels, which barrels bore the maker's trade-mark and were practically loaned to the vendees, to be returned empty.[7]

In the 1970s, Congress and state legislators found that relationships between massive oil refiners and individual mom and pop franchise operators were unbalanced.[8] Refiners had leverage they could use to take unfair advantage of franchisees who may have made substantial investments and developed business that they depended on for their income—including unfair early terminations and refusals to renew franchises at the end of their durations. To address that imbalance and achieve uniform treatment of petroleum franchisees, in 1978 Congress passed the Petroleum Marketing Practices Act (PMPA).[9] Eight years earlier, in 1970 California enacted the Franchise Investment Law to regulate offers and sales of franchises generally. This law was amended to apply to agreements between petroleum corporations and gasoline dealers starting in 1975.[10] The state also enacted restrictions on the termination and nonrenewal of petroleum franchises, which took effect in 1976.[11]

Petroleum Marketing Practices Act

PMPA's "overriding purpose" is to protect petroleum franchisees "from arbitrary and discriminatory terminations or nonrenewals."[12] The PMPA restricts oil industry franchisors in terminating a franchisee before the end of the term, or choosing to not renew a franchise at the end of its term. A franchisor may terminate or not renew a franchise only if there is good cause, prior notice, and opportunity to cure if the good cause is breach of the franchise agreement.

The PMPA creates a cause of action for termination or nonrenewal in violation of the restrictions. The action may be brought in federal court, though there is an unresolved split whether federal courts have exclusive jurisdiction over PMPA claims or whether state courts have concurrent jurisdiction. A federal district court in California has ruled that jurisdiction is exclusive to federal courts,[13] while the state courts of appeal split on this question.[14] The split of authority also exists in decisions outside California.[15]

The Act's remedies include actual and punitive damages, attorney's fees, the costs of expert witnesses and equitable relief.[16] A court can grant a preliminary injunction to protect a franchisee from a wrongful termination or nonrenewal. The standard for granting an injunction is relaxed as a franchisee need only show that they have been terminated or non renewed, serious questions on the merits to make the questions fair ground for litigation (a lower standard than the usual probability of success on the merits), and that the hardship on the franchisor from issuing an injunction would be less than the hardship on the franchisee if the injunction were denied (which often can be shown in demonstrating that the franchisee faces loss of its business).[17] The PMPA also preempts state petroleum marketing franchise law, unless the state law replicates the PMPA.[18]

Under the PMPA, a franchise is a contract between a "refiner and a distributor," a "refiner and retailer," a "distributor

David Gurnick and **Matthew J. Soroky** are attorneys with the firm of Lewitt Hackman in Encino. They can be reached, respectively, at dgurnick@lewitthackman.com and msoroky@lewitthackman.com.

and another distributor," or a "distributor and retailer," where the refiner or distributor permits the retailer or distributor to use a trademark "in connection with the sale, consignment, or distribution of motor fuel."[19]

A franchise also includes any contract under which a retailer or distributor is allowed to occupy leased marketing premises that are used to sell or distribute motor fuel.[20] A franchise also includes a contract pertaining to the supply of motor fuel and the unexpired portion of a franchise, which is transferred or assigned."[21]

Though many gas stations include convenience stores, the PMPA does not cover "secondary arrangements" or other agreements between the franchisor and franchisee, such as a mini-market or convenience store operations.

The PMPA is structured such that a lawful termination is the exception rather than the rule. It generally prohibits a franchisor from acting to terminate or not renew a gas station franchise.[22] The PMPA then provides exceptions under which termination or nonrenewal is permitted.

A franchisor may terminate a franchisee before the end of the agreement's term in these circumstances:

- A franchisee is not complying with a reasonable, material term of the franchise. In this case, the franchisor must act on the non-compliance within specified time limits (60 – 120 days). Belatedly raising stale grievances is not permitted.[23]

- The franchisee is not implementing good faith efforts to carry out the terms of the franchise after being notified and given an opportunity to cure. The issue must also be recent (within the prior 180 days).[24]

- An event occurs that is relevant to the operation of the franchise, making termination or nonrenewal reasonable. Examples stated in the PMPA include fraud or criminal conduct by the franchisee relevant to the business; felony of moral turpitude or knowingly breaking law relevant to the business; franchisee bankruptcy, insolvency or not staying current on amounts due to the franchisor; franchisee severe physical or mental disability (at least 3 months); franchisor loss of its underlying lease for the premises, if the franchisee was notified before the term started of the underlying lease term and that it might end and the franchisor offers to transfer to the franchisee any renewal, extension or purchase option (the franchisor is allowed to require a release from the franchisee); the government taking of the premises by eminent domain; the franchisor's loss of the right to use the brand involved; the destruction of premises; the franchisee's failure to operate for seven straight days (or shorter time that is unreasonable for the franchisee to have not operated); or if the franchisee adulterates or mislabels the product. The event must occur during the franchise term and the franchisor must act within specified time limits (60 –120 days) after learning of the event.[25]

- The parties mutually agree to terminate the franchise. The agreement must be for termination within 180 days and the franchisee must be given seven days to repudiate the agreement.[26]

- The franchisor decides in good faith to withdraw from marketing through outlets in the area provided the decision was not made before the franchise was granted, was based on changes in circumstances after such date, and is not for the purpose of converting the station to a company location. The franchisor must offer to sell its interest in the premises or offer a right of first refusal to buy the franchisor's interest, or for a sale of the premises, the buyer must offer a franchise to the franchisee.[27]

A franchisor may elect to not renew a franchise at the end of its term in any of the above circumstances or these additional circumstances:

- The parties do not agree to modifications of the franchise at renewal if the changes are set by the franchisor in good faith. The failure to agree cannot be due to a desire

by the franchisor to convert the premises to a company location.[28]

- There have been numerous customer complaints to the franchisor about the franchisee's operation of the business. The franchisee had to be promptly informed of the complaints and did not promptly cure or address the basis of the complaints.[29]

- The franchisee, has been notified of two failures to operate in a clean, safe, healthful way and fails a third time.[30]

- The franchisor decides in good faith to change the premises to a business other than motor fuel, or to change or sell the premises, or decides renewal won't be economical despite any reasonable changes or additions that would be acceptable to the franchisee. Again, the determination cannot be for the purpose of converting premises to a company location. Within 90 days after notifying the franchisee, the franchisor must offer to sell to the franchisee the franchisor's interest in the premises or, if applicable, offer the right of first refusal of at least 45-days of an offer, made by another, to buy the franchisor's interest in the premises.[31]

A franchisor that makes the decision to terminate or not renew a petroleum franchise must offer to sell, transfer or assign its interest in the premises to the franchisee or offer the franchisee an opportunity to buy the premises on the same terms as the franchisor is selling to someone else.[32]

Transferring a California Service Station

The PMPA applies when a franchise is terminated or not renewed. But it does not cover a situation where a franchise continues, such as when a franchisor sells, transfers or assigns ownership of a service station to a franchised service station operator.[33]

This is addressed in California's Business & Professions Code §20999.25(a), which "facilitates the purchase of retail service stations by their independent lessee-franchisees in contexts outside franchise termination and nonrenewal."[34]

Under §20999.25(a), an oil company that wants to sell a service station premises that it owns and leases to a franchised service station operator may make a bona fide offer to sell its interest in the premises to the franchisee; or give the franchisee "a right of first refusal (ROFR) of any bona fide offer acceptable to the franchisor made by another to purchase the franchisor's interest in the premises."[35]

Section 20999.25(b) sets forth a similar duty when a franchisor leases the service station premises but owns improvements thereon and is selling those improvements. These disjunctive requirements are "minimal standards" to limit the government's foray into a franchisor's property rights.[36]

The purpose of §20999.25(a) is to ensure the public greater access to service stations and further a more dynamic and full-service oriented retail environment.[37] Like its PMPA-counterpart, the statute seeks to protect the franchisee's reasonable expectation of continuing its business, while at the same time, allowing the franchisor adequate flexibility to respond to changing market conditions.[38] Both the bona fide offer and the ROFR options "fully reserve the price determining function to market actors."[39]

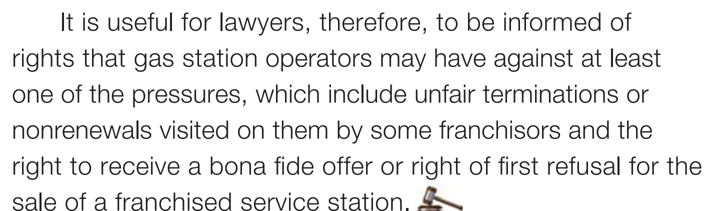
The price term of an offer to purchase the franchisor's interest in the premises is considered bona fide if it approaches fair market value under an objectively reasonable analysis.[40] The standard assumes that all non-price conditions of the sale are likewise reasonable.[41] As a result of the reasonableness standard, the guiding principles to determine whether an offer is bona fide provide fertile ground for a service station franchisee to challenge the franchisor's terms and conditions as unreasonable.

Several unpublished decisions reveal the kinds of price and non-price terms that pass muster under §20999.25(a). For instance, a group of service stations survived summary judgment on a claim that the oil company's offers and ROFRs were "commercially unreasonable" by requiring completion of environmental due diligence during the same 45-day window required to evaluate the ROFR, accept the title commitment and title survey, secure financing and pay a non-refundable deposit to accept the ROFR—all of which raised a triable issue of fact whether the oil company's terms set the transaction for failure.[42]

By contrast, where an oil company can show that other franchisees already accepted the same or similar offers, or there is mere disagreement between the parties' appraised values of the transaction, a court is unlikely to find that an offer or ROFR is not bona fide.[43]

Enactment of the PMPA was important at the time and continues to be critically important in the automotive capital of Southern California,[44] as well as the rest of the state and the nation. Gas station operators serve their communities, providing the fuel that keeps people's cars operating, all while facing pressures generated by trends in transportation, energy and economics.

It is useful for lawyers, therefore, to be informed of rights that gas station operators may have against at least one of the pressures, which include unfair terminations or nonrenewals visited on them by some franchisors and the right to receive a bona fide offer or right of first refusal for the sale of a franchised service station.



[1] Data from Nat. Assoc. of Convenience Stores (www.convenience.org/YourBusiness/FuelsCenter/Pages/default.aspx).
[2] See e.g., Michael Buhr, *Gas Stations Will Disappear Sooner Than You Think* (Oct 1, 2017) (available at http://thehill.com/opinion/technology/352884-gas-stations-will-disappear-sooner-than-you-think).
[3] See e.g., *Bird is flying high with new funding*, L.A. Times (June 29, 2018)

(discussing business start-up that places electric scooters in neighborhoods for anyone to use for $1 plus 15 cents per minute, and when finished "abandon them wherever they choose.").
[4] See www.trybooster.com.
[5] Exxon and Mobil merged in 1998 to form ExxonMobil. Chevron and Texaco merged in 2000 to form ChevronTexaco.
[6] See David Gurnick & Steve Vieux, *Case History of the American Business Franchise*, 24 Okla. City U. L. Rev. 37, 45-46 (1999).
[7] *Standard Oil Co. v. FTC* 273 F. 478, 480 (2d Cir. 1921).
[8] *DuFresne's Auto Serv., Inc. v. Shell Oil Co.*, 992 F.2d 920, 925 (9th Cir. 1993).
[9] 15 U.S.C. Secs. 2801 – 2807; *see also Atlantic Richfield Co. v. Herbert* (In re Herbert), 806 F.2d 889, 892 (9th Cir.1986) ("In enacting the PMPA, Congress attempted to provide national uniformity of petroleum franchise termination law.")
[10] Cal. Corps. Code §31005(b); *Davis v. Gulf Oil Corp.* 572 F.Supp. 1393, 1396 (C.D.Cal. 1983).
[11] Bus. & Profs. Code §20999.1; *Davis v. Gulf Oil Corp.* 572 F.Supp. 1393, 1398 (C.D.Cal. 1983).
[12] *Darling v. Mobil Oil Corp.*, 864 F.2d 981, 983 (2d Cir.1989)
[13] *Rustom v. Atlantic Richfield Co.* 618 F.Supp. 210, 214 (1985) ("Congress intended to vest the federal courts with exclusive jurisdiction over actions brought under the PMPA").
[14] Compare *Niakan v. Samaan* (1988) 199 Cal.App.3d 716, 720 (finding exclusive federal jurisdiction over PMPA claims) with *Union Oil Co. v. O'Riley* (1990) 226 Cal.App.3d 199, 204 (holding "state courts have concurrent jurisdiction with federal courts over claims made pursuant to the PMPA").
[15] Compare, *Johnson v Mobil Oil Corp.* (Pa. 1990) 560 A.2d 124, 126 ("Congress intended to give the federal courts exclusive jurisdiction over PMPA actions") with *Grotemyer v. Lake Shore Petro Corp.* (Ill. App. 1992) 602 N.E.2d 51 (finding concurrent jurisdiction).
[16] In one case, the First Circuit Court of Appeals affirmed a $2.5 million damages award against an oil refinery that stopped selling product to its dealer on credit and demand the dealer to cease using its trademark, finding that the refinery's acts failed to comply with the termination notice requirements of the PMPA. *See Seahorse Marine Supplies, Inc. v. Puerto Rico Sun Oil Co.,* 295 F.3d 68 (1st Cir. 2002)
[17] 15 U.S.C. §2805(b)(2).
[18] 15 U.S.C. §2806; see also, *Exxon Corp. v. Miro* 555 F.Supp. 234, 237 (C.D. Cal. 1983) (noting PMPA "preempts all state laws on the subject of terminating a franchise or nonrenewing a franchise in the petroleum industry, including . . . the California Franchise Investment Law.")
[19] 15 U.S.C. §2801(1)(A).
[20] 15 U.S.C. §2801(1)(B).
[21] *Id.*
[22] 15 U.S.C. §2802(a)(1).
[23] 15 U.S.C. §2802(b)(2)(A).
[24] 15 U.S.C. §2802(b)(2)(B).
[25] 15 U.S.C. §2802(b)(2)(C).
[26] 15 U.S.C. §2802(b)(2)(D).
[27] 15 U.S.C. §2802(b)(2)(E).
[28] 15 U.S.C. §2802(b)(3)(A).
[29] 15 U.S.C. §2802(b)(3)(B).
[30] 15 U.S.C. §2802(b)(3)(C).
[31] 15 U.S.C. §2802(b)(3)(D).
[32] *Id.*
[33] 15 U.S.C. §2806(b)(1); *Forty-Niner Truck Plaza, Inc. v. Union Oil Co. of Cal.*, 58 Cal. App. 4th 1261, 1275 (1997).
[34] *Forty-Niner*, 58 Cal. App. 4th at 1273.
[35] Cal. Bus. & Prof. Code §20999.25(a).
[36] *Light Petroleum, Inc. v. Exxonmobil Corp.*, 632 F. App'x 328, 329 (9th Cir. 2015).
[37] *Forty-Niner, supra,* 58 Cal. App. 4th at 1273.
[38] *Id.*
[39] *Id.*at 1274.
[40] *Id.*at 1281.
[41] *Id.*(citing *Slatky v. Amoco Oil Co.* 830 F.2d 476, 830 F.2d at p. 485, fn. 7 (3d Cir.1987)).
[42] *See Almasi v. Equilon Enterprises, LLC*, No. 10-cv-03458 EJD, 2012 WL 3945528, at *7 (Sept. 10, 2012).
[43] *See Light Petroleum, Inc. v. Exxonmobil Corp.*, 632 F. App'x 328, 329 (9th Cir. 2015).
[44] See e.g., Dennis Romero, *L.A. Is Still Car Crazy, and We Shouldn't Apologize For That,* L.A. Weekly June 2, 2014 ("This city is a world capital of car culture, and even in the age of global warming, we should never apologize for our four-wheeled lust.") (www.laweekly.com/news/la-is-still-car-crazy-and-we-shouldnt-apologize-for-that-4759210).

Test No. 118

This self-study activity has been approved for Minimum Continuing Legal Education (MCLE) credit by the San Fernando Valley Bar Association (SFVBA) in the amount of 1 hour. SFVBA certifies that this activity conforms to the standards for approved education activities prescribed by the rules and regulations of the State Bar of California governing minimum continuing legal education.

1. Over the past two decades the growing population and growing number of cars has paralleled an increase in the number of retail gas stations in the United States.
❑ True ❑ False

2. The franchised model for distribution of motor fuel developed with the growing economy boom years of the 1950s and 1960s.
❑ True ❑ False

3. The Petroleum Marketing Practices Act, or PMPA, was passed to address an imbalance between franchisors and franchisees and help achieve uniform treatment of petroleum franchises nationwide.
❑ True ❑ False

4. The PMPA was a response from Congress to refiners engaging in unfair early terminations and refusals to renew gas station franchises.
❑ True ❑ False

5. When the California Franchise Investment Law was enacted in 1969, it included regulation of the offer and sale of petroleum franchises.
❑ True ❑ False

6. The PMPA's overriding purpose is to protect franchisees from arbitrary and discriminatory terminations or non-renewals.
❑ True ❑ False

7. The general rule of the PMPA is to restrict oil industry franchisors from terminating a franchisee before the end of its term, or choosing to not renew a franchise relationship at the end of its term.
❑ True ❑ False

8. A franchisor may not terminate or non-renew a petroleum franchise unless the franchisor has good cause and provides prior written notice to the franchisee.
❑ True ❑ False

9. An action for violation of the PMPA may be brought only in state court.
❑ True ❑ False

10. Actual damages are recoverable for violation of the PMPA but not punitive damages.
❑ True ❑ False

11. Injunctive relief is available under the PMPA to protect a franchisee from a wrongful termination or nonrenewal.
❑ True ❑ False

12. State law restricting termination or nonrenewal of petroleum franchises operates concurrently with the PMPA.
❑ True ❑ False

13. The PMPA regulates a franchise between a refiner and a distributor, between a refiner and a retailer, between a distributor and another distributor, or between a distributor and retailer.
❑ True ❑ False

14. The PMPA also covers convenience stores and mini-markets that are part of the gas station property.
❑ True ❑ False

15. Under the PMPA, a franchisor may terminate a franchisee before the end of the agreement's term if the franchisee is not using good faith to carry out the terms of the franchise, but the franchisee must be notified and given an opportunity to cure and the issue must be within the past 180 days.
❑ True ❑ False

16. Under the PMPA, an event that is relevant to the franchise, making termination or nonrenewal reasonable, is a lawful ground for termination.
❑ True ❑ False

17. Under the PMPA, the parties can mutually agree to terminate the franchise but the agreement must be for termination to take place within 180 days and the franchisee must be given seven days to repudiate the agreement.
❑ True ❑ False

18. A franchisor may refuse to renew a petroleum franchise if the purpose is a good faith intent to convert it to a company owned location.
❑ True ❑ False

19. The PMPA regulates and preempts state law on sales and transfers of gasoline franchises.
❑ True ❑ False

20. California law seeks to ensure greater public access to service stations and a more dynamic and full-service retailing atmosphere, complete with tires, batteries, tune-ups, etc. and to protect the franchisee's expectation of continuing its business.
❑ True ❑ False

MCLE Answer Sheet No. 118

INSTRUCTIONS:

1. **Accurately complete this form.**
2. **Study the MCLE article in this issue.**
3. **Answer the test questions by marking the appropriate boxes below.**
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ANSWERS:
Mark your answers by checking the appropriate box. Each question only has one answer.

1.	❑ **True**	❑ **False**
2.	❑ **True**	❑ **False**
3.	❑ **True**	❑ **False**
4.	❑ **True**	❑ **False**
5.	❑ **True**	❑ **False**
6.	❑ **True**	❑ **False**
7.	❑ **True**	❑ **False**
8.	❑ **True**	❑ **False**
9.	❑ **True**	❑ **False**
10.	❑ **True**	❑ **False**
11.	❑ **True**	❑ **False**
12.	❑ **True**	❑ **False**
13.	❑ **True**	❑ **False**
14.	❑ **True**	❑ **False**
15.	❑ **True**	❑ **False**
16.	❑ **True**	❑ **False**
17.	❑ **True**	❑ **False**
18.	❑ **True**	❑ **False**
19.	❑ **True**	❑ **False**
20.	❑ **True**	❑ **False**