



Franchise Law Alert

Recent developments in franchise law

A publication of Nixon Peabody LLP

MARCH 9, 2010

U.S. Supreme Court raises threshold for constructive termination and constructive non-renewal

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On March 2, 2010, the United States Supreme Court unanimously held that a franchisee that stays in business cannot sue for constructive eviction under the Petroleum Marketing Practices Act (the “Act”). In *Mac’s Shell Service, Inc. v. Shell Oil Products Co. LLC*, service station franchisees sued their franchisor, Motiva Enterprises LLC (a joint venture of Shell Oil and two other companies) for withdrawing a volume-based rent subsidy, thereby effectively raising the franchisees’ rent when they were up for renewal. As each franchise agreement expired, Motiva offered new agreements that contained a new rent formula for calculating rent, which resulted in higher rent. The franchisees sued both for constructive termination and for constructive non-renewal while continuing in operation.

The United States Supreme Court held that a franchisee cannot recover for constructive termination under the Act if the allegedly wrongful conduct by the franchisor did not compel the franchisee to abandon the franchise. The decision was based on the plain reading of the Act, bolstered by the analogous legal contexts of constructive termination in employment cases and constructive eviction in landlord-tenant law cases. An alternative construct, which would allow a “termination” while the franchisee continues in business, would be indeterminate and unworkable; courts would be unable to discern whether a simple breach of franchise agreement case would be so threatening as to constitute constructive termination, and trigger federal jurisdiction under the Act. The Court determined that the franchisees had adequate state law remedies to redress wrongful acts that did not put an end to their business and did not need to resort to federal jurisdiction under the Act.

The Court did not decide whether a cause of action exists under the Act for constructive termination at all. The Court merely decided that constructive termination did not exist in this case. For this reason, the decision will be very persuasive in evaluating whether franchisees are constructively terminated under state law.

The Court was also asked “to decide whether a franchisee who is offered and signs a renewal agreement can nonetheless maintain a claim for ‘constructive nonrenewal’ under the Act.” For similar reasons, the Court decided that such a claim could not be maintained because the Act only covers the termination or cancellation of a franchise. A renewal, even under protest, defeats that argument. The Court suggested that where a franchisor would renew only under “unlawful and coercive terms” prohibited by the Act, the relaxed preliminary injunction standard under the Act

would be available to resume the continuation of the franchise relationship during the litigation.

The Court's decision suggests that franchisors will have greater flexibility to modify the terms of their franchise agreements at the time of renewal. Because of the significance of this case, we attended the oral argument at the Supreme Court and have access to the briefs. Please contact us if you would like further information on this case or its potential implications.

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