STATE BAR OF MICHIGAN
ANTITRUST, FRANCHISING, AND TRADE REGULATION SECTION
E-NEWSLETTER
FEBRUARY, 2011

SECTION INFO:

MESSAGE FROM THE CHAIR

Occupational hazards are frequently the subject of litigation. As defenders of competition, one of our more dangerous hazards is the brief that is due between December 24 and January 3. As a recent victim of this occupational hazard, I found it ironic to recently read that antitrust and trade regulation lawsuit filings decreased over the past year.

Please let us know your views about the pulse of Michigan's antitrust, franchising, and trade regulation practices. Does your organization anticipate more litigation during 2011?

With the commencement of the New Year, we are ramping up our efforts to organize conference topics to focus on your interests. We are currently preparing conferences that will have particular interest to in-house counsel and students.

We are scheduled to have our Council meetings January 14, March 4, April 22, June 3, July 22, and September 16. Additionally, we will most likely have meetings during November and December. We are making arrangements to have these meetings in conjunction with educational presentations and networking events at our local law schools.

Happy New Year,
Andrew J. Morganti, J.D., LL.M.
SUTTS, STROSBERG LLP
T. 519.561.6251: F. 519.561.6203
M. 248.787.6078
andrew@strosbergco.com

SECTION NEWS

Upcoming Law School Presentations

We will be holding presentations at various Michigan law schools informing students interested in competition law about the work of the Antitrust, Franchising, and Trade Regulation Section and the benefits of membership. On March 11, we will be presenting on the topic of cross-border antitrust litigation at the University of Michigan. On April 6, we will be presenting at the University of Detroit. After each presentation we will be hosting a networking hour with an open-bar at a local pub. All law students are welcome to network.

Now Accepting Submissions

If you have an antitrust, franchising, or trade regulation article that you would like to submit to be considered for publication in an upcoming eNewsletter, please submit your work to the Section's Publications Editor, Justin Hakala.

Missed the Last E-Newsletter?

If you missed the last eNewsletter, be sure to check out the archives at the State Bar of Michigan's website, accessible here.

In This Issue:

MICHIGAN NEWS

Packaged Ice Antitrust Litigation, MDL No. 1952 (E.D. Mich.)
December 6, 2010
In July 2010, the court denied the defendants' motion to dismiss reminding the Bar that, "[e]ven if ultimate proof of the facts may seem improbable to a 'savvy judge,' *Twombly* did not purport to place on a plaintiff alleging an antitrust conspiracy claim a summary judgment standard at the pleading stage" and that *Twombly* does not require the who, what, when, and where allegations. In November, Arctic Glacier, Inc.'s former Vice President of Sales and Marketing for North America was deposed resulting in a wave of motions to compel discovery. The former VP also provided testimony for the parallel Canadian class action suit. On December 6, 2010, in a related securities fraud class action, the Honorable Paul D. Borman issued a 58-page opinion and order denying Reddy Ice Holding, Inc.'s motion to dismiss securities fraud claims. This opinion may have a considerable impact on antitrust jurisprudence due to its thorough examination of the interrelationship between antitrust and securities fraud claims. The court also allocated a substantial portion of the analysis setting out the standard that is required for litigants to rely upon whistle-blowers and confidential witnesses' allegations. In conclusion, the court allocates significant analysis to the duty of a company to speak candidly and truthfully when choosing to speak on a subject. "Thus, where corporate officers choose to speak they are obligated to disclose the truth and to make any additional disclosures necessary to avoid making both present and prior statements misleading."

Auto Components Antitrust Investigations
December 23, 2010
On June 1, 2010, the United Kingdom's Office of Fair Trading arrested a British-based employee of Yazaki after receiving a tip-off from Sumitomo Electric Wiring Systems about possible antitrust violations within the electrical wiring industry. The FBI raided the U.S. offices of Denso Corp., Yazaki North America, Tokai Rika Group North America, and Tram Inc. It is reported that Lear Corp. was also a part of the raids. Lear's CEO, Robert Rossiter, has stressed that he is confident that Lear is not involved in any anticompetitive practices. The news wires and Securities and Exchange Commission filings about this investigation have been relatively light. On December 23, 2010, it was reported that the French competition authorities fined four suppliers of welding electrodes for having colluded over price. Documents confirmed that price schedules had been exchanged before the companies' bids were submitted. As a result of collusion, the firms artificially increased the price of their services and circumvented the open competition procedure initiated by the carmakers, the Autorité said. It is yet unknown whether there is a direct correlation between two cases.

Polyurethane Foam Antitrust Investigations, MDL No. 2196 (Consolidated – N.D. Ohio)
December 1, 2010
We previously reported that the European Commission's antitrust division carried out unannounced inspections (a/k/a, Dawn Raid) on the premises of companies active in the polyurethane foam sector in several Member States. The dawn raids relate to an alleged price-fixing cartel. Within the United States, including most of the Midwestern states, the FBI executed search warrants on the offices of leading polyurethane foam manufacturers.

DEAL LOG

Comcast Corp
&
NBC Universal Inc.
January 18, 2011

The DOJ, working closely with the FCC, proposed a settlement to the disputed Comcast and GE joint venture, which would have given Comcast control over NBCU and the use of its contents. The DOJ alleged that the original terms of the transaction would allow Comcast to limit competition and charge higher prices for NBC and raised concerns that it would stifle nascent online competitors. Among other things, the settlement requires that Comcast agrees to license NBC content to online distributers, that it gives up its management rights in Hulu, that it agrees to the Open Internet provisions enacted by the FCC, and it prohibits Comcast from imposing contract terms with content owners that unduly restrict their dealings with Comcast competitors. DOJ Press Release.

Simon Property Group, Inc.
&
Prime Outlets Acquisition Company, LLC
January 21, 2011

The FTC has issued a final Order requiring Simon Property Group to sell either its Cincinnati Premium Outlet center or its Prime-Outlets-Jeffersonville outlet center in Ohio. Simon will also lift radius restrictions for tenants that have stores in its Chicago and Orlando outlet malls. FTC Docket; Press Release.

Manufacturing plants in Ontario were also searched. Vitafoam Inc., with headquarters in North Carolina and Ontario, another polyurethane foam manufacturer, is reported as being accepted into the Corporate Leniency Program. On December 1, 2010, pursuant to 28 U.S.C. § 1407, the United States Judicial Panel on Multidistrict Litigation transferred all the U.S. civil antitrust class actions to the Federal District Court for the Northern District of Ohio. With the large concentration of automotive and building suppliers in Michigan, it is anticipated that the polyurethane foam antitrust litigation will be of particular interest to local companies and litigants.

***In re* Prandin Antitrust Litigation**, 2010-cv-12141 (E.D. Mich.)

The plaintiff direct-purchaser of pharmaceutical drugs alleges that Nova Nordisk, Inc. unlawfully monopolized the repaglinide market and prevented the introduction of lower-cost generic repaglinide. Repaglinide is typically used in one of three ways: (1) as a stand-alone treatment; (2) in combination with drugs called thiazolidinediones; and (3) in combination with a drug called metformin. The repaglinide compound itself is now off patent, but Novo has a patent on the combination with metformin, a so-called "method of use" patent. There is no patent protection for the other two primary uses. The patent holder may list method of use patents with the Food and Drug Administration (FDA) using a "use code narrative" that describes the method of use.

Prior to 2009, the use code narrative in place for Prandin stated as follows: "U-546: use of repaglinide in combination with metformin to lower blood glucose." Caraco, a Detroit-based generic pharmaceutical manufacturer, sought to market generic repaglinide with proposed labeling that did not induce infringement of Novo's patent, and the FDA preliminarily approved the labeling. Before the generic drug was approved for marketing, however, Novo changed the use code narrative with the FDA to: "U-968: A method for improving glycemic control in adults with Type 2 diabetes mellitus." With this change, the FDA deemed its previous approval of Caraco's labeling moot and required that Caraco proceed based upon presumed infringement of the patent. Consequently, Novo remains the exclusive producer of repaglinide. Plaintiffs are represented by Patrick Cafferty, Cafferty Faucher LLP (Ann Arbor), Berger & Montague, P.C., Cohen Milstein Sellers & Toll PLLC, Faruqi & Faruqi LLP, Taus Cebulash & Landau LLP, and Hagens Berman Sobol Shapiro LLP. Defendant is represented by David Ettinger and Herschel Fink, Honigman Miller Schwartz and Cohn LLP. Cobalt Pharmaceuticals Inc., a Canadian generic drug manufacturer, also lodged an antitrust claim against Novo Nordisk relating to repaglinide. *Novo Nordisk Canada Inc. v. Cobalt Pharmaceuticals Inc.*, T-1221-08, 2010 FC 746 (CanLII).

***In re* Detroit Association of Realtors**, 2010-cv-14046 (E.D. Mich.)
October 8, 2010

Purchasers of real estate brokerage services for real estate listed for sale by member brokers and agents of defendants, lodged a complaint against the Detroit Association of Realtors, Realcomp II, Ltd., et al., alleging that defendants entered into an illegal agreement that resulted in the restriction of Realcomp's Multi Listing Service ("MLS") and higher prices. The complaint follows the FTC's antitrust investigations of Realcomp II, Ltd. (Docket No. 9320) and pending Sixth Circuit appeal (Case No. 09-4596). An administrative judge previously found that Realcomp II held substantial market power in the relevant market of multiple listing services, including throughout the four Michigan counties of Wayne, Oakl-

Universal Health Services, Inc.
&
Psychiatric Solutions, Inc.
November 15, 2010

The FTC has proposed a settlement requiring Universal Health Services to sell 15 of its facilities before it can proceed with the $3.1 billion acquisition of Psychiatric Solutions. Universal Health and Psychiatric Solutions are the leading providers of inpatient psychiatric services and the acquisition would have "significantly increased Universal Health's market power" in Delaware, Puerto Rico and Las Vegas, Nevada. FTC Docket; Press Release.

Laboratory Corporation of America
&
Westcliff Medical Laboratories, Inc.
December 1, 2010

The FTC is challenging LabCorp's $57.5 million acquisition of Westclif Medical Laboratories, completed June 16, 2010, because the acquisition would leave only two significant competitors in the Southern California market for diagnostic lab services offered to physician groups. The remaining competitors, Universal Health and Quest Diagnostics Incorporated, would have 89 percent of the transactions in the market. Westcliff, "an upstart competitor," has priced some of its testing services lower than LabCorp and Quest, increasing its share of physician groups and in some cases, preventing LabCorp from raising prices for the service. FTC Docket; Press Release.

and, Livingston, and Macomb. The consumers are represented by Barris Sott Denn & Driker, PLLC, Goldman Scarlato & Karon (Cleveland, OH), Freed Kanner London & Millen LLC (Chicago, IL), and Reinhardt Wendorf & Blanchfield (St. Paul, MN).

GMA Cover Corp. v. Saab Barracuda, LLC, 2010-cv-12060 (E.D. Mich.)

This attempted monopolization claim was filed during mid-2010, but the defendant appears to be preparing to answer the complaint or motioning the court to dismiss. The plaintiff alleges that there are only two authorized manufacturers of specialized camouflage netting for the United States Army. The complaint alleges that the defendant engaged in predatory pricing in an attempt to monopolize the relevant market. Specifically, that over the past couple of years defendant has sold the relevant product below its average variable cost or, in the alternative, below defendant's average total cost. Plaintiff is represented by Fletcher Fealko Soudy & Francis, P.C. In November, Howard Iwrey, Dykema Gossett, PLLC, filed an appearance on behalf of Saab Barracuda LLC.

***In re* Blue Cross Blue Shield of Michigan**, (E.D. Mich.)
December 17, 2010

We previously reported that the US Department of Justice and the State of Michigan filed a civil antitrust lawsuit against Blue Cross Blue Shield of Michigan (BCBSM) alleging that provisions of its agreement with hospitals result in artificially high prices for various medical procedures and services as well as preventing other insurers from entering the marketplace. In particular, the DOJ has taken issue with the most favored nation (MFN) clauses incorporated into the contracts between BCBSM and certain Michigan healthcare facilities. On December 17, BCBSM, represented by Hunton & Williams LLP and Dickinson Wright PLLC, motioned the court to dismiss the action. BCBSM claims that the complaint should be dismissed pursuant to the state action doctrine and because it fails to allege the relevant product and geographic markets. The motion hearing is scheduled for March 2, 2011. Several civil antitrust class actions have also been filed against BCBSM. One of the more recent filings includes the matter of Abatement Workers National Health and Welfare Fund, Michigan Regional Council of Carpenters Employee Benefits Fund and Monroe Plumbers and Pipefitters Local 671 Welfare Fund, 2:2010cv14887 (Dec. 8, 2010). Plaintiffs in the various actions are represented by several firms, including Cohen Milstein Sellers & Toll, PLLC (Washington, D.C.), Berger Montague (Philadelphia, PA), The Miller Law Firm, and Fink + Associates.

Federal E-Rate Program Fraud Investigation
January 24, 2011

The president and part owner of an internet and technology services company in Grand Rapids, Michigan plead guilty to wire fraud charges related to the federal E-Rate program. The E-Rate program helps financially disadvantaged schools and libraries obtain internet access and telecommunications services by providing funding to cover up to 90 percent of the cost. To date, the investigation has led to the indictment of 7 companies and 20 individuals, 15 of whom have already been sentenced to jail time. The companies and individuals have paid, agreed to pay or have been ordered to pay more than $40 million in criminal fines and restitution. DOJ Press Release.

L.B. Foster Co. &
Portec Rail Products Inc.
December 14, 2010

The settlement agreement allowing the acquisition of Portec Rail Products by L.B. Foster will require the companies to divest Portec's West Virginia plant, responsible for the manufacture of all of its bonded insulated rail joints and polyurethane-coated insulated rail joints, to Koppers Inc. The acquisition as originally structured would have led to a significant decrease in competition in the already highly concentrated market for bonded insulated rail joints and polyurethane-coated insulated rail joints. DOJ Press Release.

ProMedica Health System, Inc.
&
St. Luke's Hospital
January 6, 2011

The FTC alleges that ProMedica's acquisition of St. Luke's Hospital would result in harm to competition in two relevant service markets in Lucas County, Ohio, the market for general acute-care inpatient hospital services and the market for inpatient obstetrical services. The acquisition would leave ProMedica facing only two other competitors in the acute-care services market and with a 60 percent market share. Post-acquisition ProMedica would have an 80 percent share of the inpatient obstetrical services market and would face only one other competitor. The evidentiary hearing before an Administrative Law Judge at the FTC, is scheduled for May 31, 2011. FTC Docket; Press Release.

NATIONAL NEWS

FTC Announces New Thresholds For Notice Requirement of Proposed M&As
January 21, 2011

The FTC has issued its new annually revised thresholds for requiring notification of proposed mergers and acquisitions. The threshold increased this year to $66.0 million from the previous $63.4 million. The FTC also announced new thresholds for when interlocking board membership is prohibited under Section 8 of the Clayton Act. This year's threshold is $26,867,000 under Section 8(a)(1) and $2,686,700 under Section 8(a)(2)(A). The new thresholds apply to transactions that close on or after the effective date of notice, which is 30 days after its publication in the Federal Register. Press Release.

European Commission Adopts Revised Guidelines On Horizontal Agreements
December 14, 2010

The most significant change to the revised Horizontal Guidelines is to the chapters on information exchange and standardization agreements. The new Guidelines provide more extensive and detailed criteria to help companies determine when information exchange and standard-setting agreements infringe EU competition law and when they do not. In addition, the Commission also adopted two new Block Exemption Regulations (BERs) on specialization agreements and R&D, considerably extending the scope of exempted R&D activities. Agreements are presumed to have no anticompetitive effects if they meet the conditions set forth in the BER. The new Regulations will go into effect on January 1, 2011 and will replace the current Regulations set to expire on December 31, 2010. EU Competition Rules on Horizontal Cooperation Agreements.

ENFORCEMENT ACTIONS

In re Minnesota Rural Health Cooperative
January 4, 2011

The FTC has approved a final Order requiring the Minnesota Rural Healthcare Cooperative to renegotiate all current contracts it has with insurance plans and prohibiting it from engaging in coercive tactics or refusals to deal in order to obtain favorable terms. The Minnesota Rural Healthcare Cooperative was charged with fixing contract prices between its doctor and hospital members and health insurance plans. It refused to deal with insurance plans that did not agree to its proposed reimbursement rates. FTC Docket; Press Release.

Ready-Mix Concrete Price Fixing Conspiracy
December 7, 2010

Federal and state authorities are investigating antitrust violations in the ready-mix concrete industry in Iowa and surrounding states. Thus far three individuals have pled guilty to participating in a conspiracy to fix sale prices of ready-mix concrete. Press Release.

Global Airline Price-Fixing Conspiracy
December 3, 2010

Florida West International Airways Inc., its former vice president of sales and marketing, and two executives from a Colombian air cargo carrier were indicted in U.S. District Court in Miami for participating in a conspiracy to eliminate discounts and fix price components and surcharges of air cargo shipments from Colombia to Miami. According to the DOJ

Keystone Holdings, LLC
&
Compagnie de Saint-Gobain
December 29, 2010

The FTC challenged Keystone's planned $245 million acquisition of Saint-Gobain's Advanced Ceramics business on the grounds that it would reduce competition in the North American alumina wear tile market. The deal would allow CoorsTek, the Keystone subsidiary that manufactures the tiles, to eliminate its most significant competitor in a concentrated market, substantially increasing CoorsTek's market share. The proposed settlement requires that the Saint-Gobain North American alumina tile business continue to operate and compete in the market. Additionally, the order requires that for a period of 10 years, Keystone obtain prior approval from the FTC before acquiring any asset of the Saint-Gobain's North American alumina wear tile business and that Saint-Gobain provide notice before selling any part of the North American tile business or stopping operations at its manufacturing facility. FTC Docket; Press Release.

Have We Missed Something?

Do you know of a recent case that you don't see in the newsletter? Please email the editor with recently resolved or newly pending cases that we have missed

press release, the price agreement was further expanded by an agreement not to compete for certain customers. A few days earlier, on November 30, Singapore Airlines Cargo Pte Ltd. had pled guilty and agreed to pay a $48 million criminal fine for its involvement in the conspiracy to fix components of cargo rates for air shipments on certain routes to and from the U.S.

So far, 21 airlines and 19 executives have been charged for their involvement in the price fixing scheme, resulting in the payment of criminal fines amounting to more than $1.7 billion. Four of the executives have already been sentenced to prison time. Other airlines that have pled guilty include All Nippon Airways Co. Ltd., Northwest Airlines, Asiana Airlines, Inc., British Airways Plc, Korean Air Lines Co. Ltd., Qantas Airways Limited, Japan Airlines International Co. Ltd., Martinair Holland N.V., Cathay Pacific Airways Limited, SAS Cargo Group A/S, Société Air France, Koninklijke Luchtvaart Maatschappij N.V. (KLM Royal Dutch Airlines), EL AL Israel Airlines Ltd., LAN Cargo S.A., Aerolinhas Brasileiras S.A., and Nippon Cargo Airlines Co. Ltd. Latest Press Release.

Global LCD Price-Fixing Conspiracy
January 13, 2011

The current president of HannStar Display Corporation was indicted by a federal grand jury in San Francisco for conspiring to fix LCD panel prices and eliminate competition. LCD panels are used in electronic devices such as computers, televisions and cell phones. According to the DOJ, companies adversely affected by the higher LCD prices include Apple, Dell and Hewlett Packard. A total of 8 companies and 22 executives have so far been indicted for participating in the price fixing conspiracy and more than $890 million has been obtained in criminal fines. DOJ Press Release.

High-Tech Employee No-Solicitation Agreements
December 21, 2010

Lucasfilm Ltd. and the Department of Justice reached a settlement that prohibits Lucasfilm from entering into agreements that restrain employee recruitment. Lucasfilm had entered into an agreement with Pixar to refrain from cold calling each other's employees, to provide notification when extending an offer to the other company's employee, and to not extend to such employee a counteroffer with a compensation higher than what was initially offered. The DOJ said the agreement interfered with the compensation price that would prevail in an unrestrained competitive market. Press Release.

Municipal Bonds Bid-Rigging Conspiracy
December 9, 2010

As a condition for admittance to the Antitrust Corporate Leniency Program, Bank of America agreed to pay $137.3 million in restitution fees for its involvement in the bid rigging conspiracy in the municipal bonds derivatives market. Bank of America was the first, and so far the only entity, to report the anticompetitive behavior of its employees to the DOJ.

On November 30, yet another guilty plea to bid-rigging and fraud conspiracy was entered by James L. Hertz, a former VP in the municipal derivatives group of an unnamed financial subsidiary based in Manhattan, New York. Indictments in the case still continue. On December 9, Peter Ghavami, Gary Heinz and Michael Welty were charged with participating

in various fraud conspiracies "that subverted competition in the market for municipal finance contracts," said Christine Varney, Assistant Attorney General. Ghavami, a Belgian national, was originally charged with wire fraud by criminal complaint and arrested at JFK International Airport in New York.

The indictment also alleges that Ghavami, Heinz and Welty conspired with Dunhill Insurance Services Inc. (CDR), among others, and obtained from CDR pricing information on competing bids, using this information to determine their employer's bid. In certain cases, intentionally loosing bids were submitted to give the appearance that the companies were engaged in actual competition. Latest Press Release.

Mount Sinai and New York Presbyterian Hospital Bid-Rigging Conspiracy
December 2, 2010
The New York Field Office's antitrust investigation into the bid rigging of construction, maintenance and service contracts by the Mount Sinai and NYPH Engineering Departments has led to another guilty plea. Mario Perciavalle, a former purchasing official at Mount Sinai is the tenth individual so far to plead guilty to the charges. Three companies have also entered guilty pleas and eight other individuals have been indicted and are awaiting trial. DOJ Press Release.

Polypore International and Microporous Products 2008 Merger Challenged
December 13, 2010
The FTC issued a final order requiring Polypore International, Inc. to divest Microporous Products, including technology and intellectual property that Microporous owned at the time of the acquisition in 2008, within six months. The Commission held that the merger reduced competition in three markets for different types of lead-acid battery separators, declining to find that there were anticompetitive effects in a fourth market for separators, as the administrative judge had found. Commissioner Rosch, who wrote a separate concurring opinion, pointed to pre-merger documents showing anticompetitive purposes and the post-merger price increases as essential facts for finding Polypore liable. Press Release; Commission Opinion; Concurring Opinion of Commissioner Rosch.

GrafTech International Ltd. and Seadrift Coke, L.P.
November 29, 2010
The DOJ is seeking an injunction against GrafTEch's April 2010 acquisition of Seadrift. GrafTech manufactures graphite electrodes and uses petroleum needle coke, the primary input in graphite electrodes, from Seadrift's competitor, ConocoPhillips Company, with whom it had a long term supply contract that included an MFN clause giving GrafTech the ability to audit Conoco's books to ensure compliance. The DOJ charges that GrafTech's acquisition of Seadrift would allow Seadrift access to information that GrafTech collects from Conoco, facilitating tacit coordination of prices or output. The DOJ is seeking to have GrafTech strike out the audit and MFN clauses from the Supply Agreement and prohibit any such clauses that would allow access to commercial information in contracts with Conoco in the future. DOJ Press Release

IMPLIED FRANCHISE: ANOTHER KIND OF FRANCHISE

By Howard Yale Lederman[†]

To gain the protection of state franchise investment laws, the proponent must prove that the business relation involved is a franchise. Most of the time, the proponent tries to prove an express franchise. When this is impossible or difficult, an often overlooked alternative is an implied franchise.

Many states' franchise laws, including Michigan's, recognize implied franchises. This recognition began with the first state franchise investment law, the 1971 California Franchise Investment Law ("CFIL"). In defining "franchise," the California Legislature included implied franchises:

> Franchise' means a contract or agreement, either expressed or *implied*, whether oral or written, between two or more persons, by which:
>
> (a) A franchisee is granted the right to engage in the business of offering, selling, or distributing goods or services under a marketing plan or system prescribed in substantial part by a franchisor.
> (b) A franchisee is granted the right to engage in the business of offering, selling, or distributing goods or services substantially associated with the franchisor's trademark, service mark, trade name, logotype, advertising, or other commercial symbol designating the franchisor or its affiliate.
> (c) The franchisee is required to pay, directly or indirectly, a franchise fee.[1]

In enacting the 1974 Michigan Franchise Investment Law ("MFIL"), the Michigan Legislature adopted and incorporated the CFIL's above franchise definition, including the above implied franchise alternative.[2] But MFIL legislative history is "sparse."[3] The only known available MFIL legislative history says nothing about why the Michigan Legislature adopted the CFIL franchise definition, let alone its expressed or implied language.[4] The Library of Michigan archives do not contain any MFIL legislative history.[5] Thus, resort to California law and sources on the definition's 'express or implied' language or the reason for the legislature's inclusion of 'implied' in the 'express or implied' language is essential.

Available CFIL legislative history on these subjects is not definitive. The CFIL's author, State Senator Stewart Bradley, stated: "We spent more time on [the section defining a franchise] than on any other single section of the bill. We decided that even though it may not be a perfect definition, that it is

---

[†] Howard Yale Lederman currently serves as the Secretary of the Antitrust, Franchising, and Trade Regulation Section of the State Bar of Michigan. He is an attorney at Norman Yatooma & Associates, P.C., where his practice focuses on franchising, commercial, employment, and other civil areas. He received a J.D. from Wayne State University and a B.A. from Oakland University.

[1] Cal. Corp. Code § 31005 (West 2010) (emphasis added).

[2] Mich. Comp. Laws § 445.1502(3).

[3] In Re Dynamic Enter., 32 B.R. 509, 516 (Bankr. Tenn. 1983) (applying Michigan law).

[4] Michigan House Legislative Analysis, HB 4203, August 2, 1974.

[5] On November 4, 2010, this author checked the Michigan Library archives and found no MFIL legislative history.

certainly adequate in light of the difficulty in defining 'franchise.'"[6] The California Department of Corporations "has taken the position that this statutory definition of 'franchise' is to be construed liberally so as to expand as much as possible the group of investors protected by the law and to carry out the intent of the Legislature."[7] This position parallels the statutory construction rule of construing remedial statutes liberally to further the legislative intent behind them.[8]

The California Court of Appeals has expanded this broad and liberal interpretation principle to a broad and liberal interpretation of each franchise definition element. The Court has concluded that each franchise definition element should be interpreted liberally "to broaden the group of investors protected by the law and to carry out the legislative intent."[9] Thus, the Court found that the implied franchise definition did not stand on its own but depended on the three franchise definition elements. Further, regarding the second franchise definition element, the Court recognized an implied marketing plan: "The marketing plan itself may be expressed or implied, oral or written."[10]

What is an implied marketing plan? The best example occurred in *Kline* involving Aunt Hilda's Pennsylvania Dutch Steamed Franks Enterprise. Kline deceived Shaul and Mushet into forming a partnership, investing in his business opportunity, and contracting with his National Food Service. The contract committed the partnership to a $50,000 investment in two Aunt Hilda's food service outlets and National Food Service to "total and continuing support" of the partnership.[11] This support included advertising support, food supply, menu planning, and related services. Despite "an ongoing relationship" between National Food Service and the partnership, National Food Service ran the outlets.[12] The food service outlets were "distinct and identifiable kiosks."[13] The contract specified sale of the above hot dogs.[14] Kline told several people "that he was organizing a national food franchise similar to other well-known and successful national franchises."[15] He planned it as an integrated operation. He did not register his business opportunity with the California Corporations Department, issue a Uniform Franchise Offering Circular before the contract, or otherwise follow CFIL.

When sales went south, the state prosecutor prosecuted Kline for selling an unregistered franchise, thus violating CFIL. Kline claimed that he was selling only a business opportunity. The trial court rejected his position and convicted him of selling an unregistered franchise.

Affirming, the California Court of Appeals held that the contract was an implied franchise. The Court cited and applied the statutory construction rule of broad and liberal construction of remedial statutes, like CFIL. Since the contract did not include a franchisor-prescribed marketing plan or system, it

---

[6] Gentis v. Safeguard Bus. Sys., 60 Cal. App. 4th 1294, 1300 (Cal. Ct. App. 1998) (quoting Senator Bradley's March 30, 1970 statement before the Small Business Subcommittee of the California Senate Committee on Urban and Rural Economic Development.)

[7] Harold J. Marsh & Robert H. Volk, California Securities Laws, (Matthew Bender 2010), sec40.04[1][a][i] (citing California Department of Corporations, Corporate Securities News Letter, No 9, p 1 (September 1972)).

[8] Kim v. Servosnax, 10 Cal. App. 4th 1346, 1356 (Cal. Ct. App. 1992); Gentis v. Safeguard Bus. Sys., 60 Cal. App. 4th 1294, 1298 (Cal. Ct. App. 1998).

[9] Kim v. Servosnax, 10 Cal. App. 4th 1346, 1355-6 (Cal. Ct. App. 1992).

[10] People v. Kline, 110 Cal. App. 3d 587, 594 (Cal. Ct. App. 1980).

[11] *Id.*

[12] *Id.*

[13] *Id.*

[14] *Id.*

[15] *Id.*

was not an express franchise. However, the Court found enough elements for an implied franchisor-prescribed marketing plan or system. The Court pointed to the distinctive and identifiable kiosks, Kline's "assistance," such as the advertising support, food supplies, and menu planning, and Kline's expressed intent to organize an integrated national food franchise. The Court found direct evidence of an express commercial symbol based on the Aunt Hilda's logo and direct evidence of an express franchise fee based on the required $50,000 investment. Finally, the Court saw Kline as the kind of financial investment predator that the California Legislature intended the CFIL to stop. In recognizing an implied franchisor-defined marketing plan or system, the Court recognized an implied franchise.

The Court could have cited other business opportunity-franchise differences. "Business opportunities generally require much smaller investments than [franchises]."[16] Unlike franchisors, business opportunity sellers furnish little assistance and training.[17] In contrast to franchisors, business opportunity sellers do not control business opportunity buyers.[18] The contracts are simpler and restrict buyers far less.[19] Lastly, business opportunity buyers do not operate under the sellers' trade name, trademark, or service mark.[20]

Another implied franchise arising from a more complex implied prescribed marketing system arose in *Hartford Electric Supply.*[21] There, Allen-Bradley manufactured "high-tech industrial automation products" and assigned each distributor a territory.[22] Hartford Electric Supply was a nonexclusive Allen-Bradley distributor. While over 50% of Hartford Electric Supply sales were of Allen-Bradley products or their accessories, Hartford Electric Supply could and did sell competing products.

Allen-Bradley and Hartford Electric Supply had a distributorship agreement. It compelled Hartford Electric Supply to prepare and forward a business plan, including "targeted accounts, a promotion program, a sales forecast, a training plan, an inventory plan, and demonstration equipment."[23] While Hartford Electric Supply retained "the ultimate authority over whom to employ," Allen-Bradley "exert[ed] enormous pressure'" on Hartford Electric Supply "to hire specialists for its products, and sales and operations managers."[24] Allen-Bradley also required Hartford Electric Supply to arrange and pay for its employees' extensive training to sell Allen-Bradley products. Moreover, Allen-Bradley required Hartford Electric Supply to maintain a specified inventory level, and in case of disagreement on the inventory level and mix, Hartford Electric Supply had to permit the local Allen-Bradley office to determine the exact level and mix of inventory required. Further, Allen-Bradley printed and sent Hartford Electric Supply a price catalog. Hartford Electric Supply used it to define sales prices of Allen-Bradley products.

Due to disputes over control and sales, Allen-Bradley terminated the distributorship agreement. Hartford Electric Supply sued to enjoin the termination and for damages under the Connecticut Franchise Act. The trial court found that Allen-Bradley had prescribed a marketing system and concluded

---

[16] Statement of Dennis E. Wieczorek on Behalf of the International Franchise Association to the Subcommittee on Commerce, Trade & Consumer Protection of the House Energy & Commerce Committee, U.S. House of Representatives, *"The FTC's Franchise Rule: Twenty-Three Years After Its Promulgation,"* June 25, 2002.

[17] *Id.*

[18] *Id.*

[19] *Id.*

[20] *Id.*

[21] Hartford Electric Supply v. Allen-Bradley, 250 Conn. 334; 736 A.2d 824 (1999).

[22] *Id.* at 337.

[23] *Id.* at 338.

[24] *Id.*

that the distributorship agreement was a franchise agreement. The trial court enjoined Allen-Bradley from terminating the distributorship agreement and awarded damages.

Affirming, the Connecticut Supreme Court found an implied Allen-Bradley-prescribed marketing system and held the parties' relationship a franchise. After noting the first franchise requirement's broad definition, the Court emphasized that the requirement means not a total franchisor-defined marketing plan or system, but only a substantial franchisor-defined marketing plan. Agreeing with an earlier Connecticut decision, the Court recognized that the franchisor's right to prescribe the marketing plan or system need not rest on express written contract provisions to meet the first franchise requirement.[25] The franchisor's right to substantially define the marketing plan or system need not rest on contract provisions. While their language may be relevant, it is not outcome-determinative. Rather, the franchisor's right can arise from the parties' actual relation, their actual course of dealing.[26] As a result, the Court created the following test: "Accordingly, the statutory test should be whether parties' conduct, in addition to their words, constitutes an agreement or arrangement," and the court must examine their conduct and words to determine whether substantial franchisor prescription of the marketing plan or system is present."[27]

Therefore, the Court recognized that an implied franchisor-defined marketing plan or system could exist, thus enabling the franchise proponent to meet the first franchise requirement.

Citing earlier decisions for factors in evaluating whether the franchise proponent meets this requirement, the Court evaluated these factors.[28] First, the Court recognized that Hartford Electric Supply's business plan was subject to Allen-Bradley's approval. After approval, the business plan "becomes the defendant's marketing plan to enforce upon the plaintiff."[29] Allen-Bradley "constantly monitor[ed]" Hartford Electric Supply's compliance with the business plan.[30] Moreover, Allen-Bradley recommended more sales promotions, suggested hiring of specialized employees, and participated in sales to Hartford Electric Supply's customers, whenever Allen-Bradley found Hartford Electric Supply's "adherence to its business plan inadequate."[31]

Second, the Court recognized Allen-Bradley's control over pricing and adopted the *Petereit* Court's conclusion that control over pricing is a crucial factor.[32] The Court rejected Allen-Bradley's arguments that the price catalog did not establish prices due to Hartford Electric Supply's option to ask Allen-Bradley for permission to sell products at below catalog prices and accept lower profit margins. Allen-Bradley retained control. Allen-Bradley could say yes or no. In addition, Allen-Bradley had "chastised" Hartford Electric Supply for selling products below catalog prices.[33]

Third, the Court pointed to Allen-Bradley's requirement that Hartford Electric Supply "maintain competent sales and marketing personnel," Allen-Bradley's "enormous pressure" on Hartford Electric

---

[25] *Id.* at 348 (citing Petereit v. S.B. Thomas, 854 F. Supp 55, 60 (D. Conn. 1993), 63 F.3d 1169, 11 (2d Cir. 1995), *cert. den.* 517 U.S. 1119; 116 S.Ct. 1351; 134 L.Ed.2d 520 (1996) and *Chem-Tek, Inc. v. GMC,* 816 F. Supp. 123, 125 (D. Conn. 1993)).

[26] *Id.*

[27] *Hartford Electric Supply Co.,* 250 Conn. at 348-349.

[28] *Id.* at 350 (citing *Consumers Petroleum of Connecticut, Inc. v. Duhan,* 38 Conn. Supp. 495, 498-499; 452 A.2d 123 (1982), *Chem-Tek v. GMC,* 816 F. Supp. 123, 125 (D Conn 1993)).

[29] *Hartford Electric Supply Co,* 250 Conn at 350.

[30] *Id.*

[31] *Id.*

[32] *Id.* at 351-352 (citing *Petereit,* 63 F.3d 1169, 1181).

[33] *Id.* at 352.

Supply "to hire specialists for its products, and sales and operations managers," and Allen-Bradley's pressure on Hartford Electric Supply "to terminate certain employees."[34] Fourth, the Court noted that Allen-Bradley had cited Hartford Electric Supply for failing "to maintain adequate sales personnel" and "failure to replace its operations manager."[35]

Fourth, Allen-Bradley had and enforced the right to require "extensive training" of Hartford Electric Supply's employees in Allen-Bradley's products.[36] The Court noted Allen-Bradley's contractual requirement for specific training "conducted locally at the factory and in regional locations."[37] Furthermore, the agreement compelled Hartford Electric Supply to assure that its employees attended "training at specific schools in cooperation with the defendant."[38] In addition, Allen-Bradley cited Hartford Electric Supply "for not sending personnel to training sessions."[39] Finally, Allen-Bradley required Hartford Electric Supply "to maintain and [use] a training center," at Hartford Electric Supply's expense, for its "staff and customers."[40]

Fifth, Allen-Bradley controlled Hartford Electric Supply's inventory. Allen-Bradley monitored Hartford Electric Supply's inventory and pressured it to buy and stock more Allen-Bradley products. Allen-Bradley dictated inventory levels, "minimum purchase amounts of certain products," and, absent inventory agreements between Allen-Bradley and Hartford Electric Supply, even permitted local Allen-Bradley offices to dictate "the exact level and mix of inventory."[41] Hartford Electric Supply had to provide Allen-Bradley with "inventory reports on the twentieth day of each month."[42]

The Court brushed aside Allen-Bradley's position that Hartford Electric Supply's rejection of its "assistance" negated Allen-Bradley's control. On receiving this news, Allen-Bradley terminated its distributorship agreement with Hartford Electric Supply. Accordingly, the Court had abundant evidence to find implicit and substantial Allen-Bradley prescription of Hartford Electric Supply's sales and marketing system. The Court sustained the lower Court's conclusions that Allen-Bradley substantially prescribed Hartford Electric Supply's marketing system, and that the parties' relationship met the first franchise requirement.

Therefore, an implied franchise based on an implied and substantial prescription of the dealer's or distributor's marketing plan or system is a viable option. The above two decisions illustrate many factors to use to advocate a marketing plan or system meeting the first franchise element. That state franchise investment laws are remedial statutes and that these laws often recognize implied franchises' possible existence facilitates court recognition of implied substantial franchisor-defined marketing plans or systems and implied franchises. That state franchise investment laws lack legislative histories on the implied statutory language and that state common law decisions on the implied statutory language are practically nonexistent are far from insurmountable barriers. Though few, certain state common law decisions have provided an analytical framework to overcome both barriers. Thus, when unable or less able to prove an express franchise or an express substantial franchisor-defined marketing plan or system, try to prove their implied counterparts.

---

[34] *Id.*
[35] *Id.*
[36] *Id.* at 354.
[37] *Id.*
[38] *Id.*
[39] *Id.*
[40] *Id.*
[41] *Id.* at 355.
[42] *Id.*