General Counsel Corner

By Peter H. Gunst, Esquire

Back to the Bar Examination

Part of the agony of sitting through a bar examination is being faced with unbelievably complex hypothetical situations, which the aspiring attorney must sort through in order to give a hypothetical client advice or to pursue a hypothetical lawsuit.

Veteran dealer-attorney Arnold Azarow may be forgiven a sense of bar examination *déjà vu* when he was confronted with the complicated factual scenario that was to become the *Koylum, Inc. v. Paksen Realty Corp.* litigation in the Second Circuit Court of Appeals.

In 1994, the previous dealer at a service station in Ridge, New York entered into a supply agreement with a jobber, Ocean Petroleum, and a lease agreement with a real estate entity that was closely affiliated with the jobber. Both agreements were to expire on December 31, 2011.

The supply agreement contained an unusual provision. It permitted the dealer to purchase gasoline from "any other open market supplier" if the jobber's quoted prices exceeded those specified by a formula. The dealer was required, however, to document his calculations justifying his purchase of gasoline on the open market, and was further required to utilize a specified transporter for the delivery of any open-market gasoline.

In 1996, the lease and supply agreements were assigned to the present dealer, who flew the flag of the jobber's supplier, Coastal Refinement Corporation.

By 1997, the dealer's relationship with the jobber was deteriorating. Because of his dissatisfaction with the jobber's pricing policies, the dealer turned to other suppliers for fuel, including non-Coastal brand suppliers. The dealer and the supplier exchanged nasty letters, but nothing else occurred at that point.

In July 1998, the jobber encountered difficulties in obtaining gasoline from the Coastal refinery, and supplied the dealer with non-Coastal gasoline obtained from other suppliers. The dealer also continued to purchase non-Coastal gasoline in the open market because of his dissatisfaction with the jobber's prices.

Upset with the dealer's open-market purchases, the jobber and its affiliated real estate company sent the dealer written notices on October 2, 1998 of their intention to terminate the supply agreement and the lease effective midnight October 6, 1998.

The notices of termination accused the dealer of violating both the supply agreement and the lease by (1) purchasing unbranded gasoline from unauthorized suppliers for resale under the Coastal brand name; (2) mixing unbranded gasoline with gasoline supplied by the jobber; and (3) selling gasoline not approved by the jobber or its real estate affiliate. For good measure, the termination notices also charged the dealer with trademark infringement, unfair competition and trademark dilution for his sale of unbranded gasoline under the Coastal brand name.

On October 7, 1998, the real estate company filed an action for ejectment in state court to oust the dealer from the premises, and the dealer counterclaimed for a judgment allowing him to continue to occupy the premises. Nothing further happened in the ejection action, and the dealer continued to occupy the station under a stipulation entered into with his landlord.

In late October 1998, Coastal canceled the jobber's right to use the Coastal trademark, and terminated its supply agreement effective February 1999. The jobber filed for bankruptcy protection in late November 1998.

Under bankruptcy law, a petitioner like the jobber normally is permitted to reject executory contracts, like the dealer's ongoing supply agreement. The jobber did so in late February 1999.

Approximately a month earlier, the dealer had removed all Coastal identification at the station. He had done so on the advice of his previous attorney in order to avoid further charges that he was violating Coastal's trademark.

In late January 1999, the real estate affiliate, which apparently was not in bankruptcy, again notified the dealer that he was being terminated for selling non-Coastal gasoline purchased in the open market.

Thereafter, in May 1999, the real estate company sold the station, without notice to the dealer, to another Coastal marketer. The dealer, however, refused to surrender possession.

Such was the complex situation presented to attorney Azarow when he filed suit for the dealer in July 1999. The complaint charged the landlord with violating the Petroleum Marketing Practices Act, 15 U.S.C. §§2801 *et seq.*, claiming that the real estate company had wrongfully terminated the lease and failed to give the dealer a right of first refusal before selling the station.

After the dealer succeeded in obtaining a preliminary injunction prohibiting termination until after a full trial, the real estate entity appealed to the influential Second Circuit Court of Appeals.

Ruling for the dealer, the Second Circuit in *Koylum, Inc. v. Peksen Realty Corp.*, 272 F.3d 138 (2nd Cir. 2001), affirmed the grant of the preliminary injunction, and sent the case back to the district court for trial on the merits. In so doing, the court rejected a number of interesting arguments presented by the landlord.

First, the landlord argued that no PMPA franchise had ever existed with the dealer because the supply agreement had given the jobber the right to designate "any brand names and trademarks (or none at all) for fuel sold at the station." Without reference to a definite refiner trademark, the landlord argued, a necessary element of a PMPA franchise was lacking.

The Second Circuit disagreed, holding that a franchise existed because the jobber had orally authorized the dealer to use Coastal's marks. Whether the jobber had the power to designate the use of its own marks, in place of a refiner's marks, was irrelevant because that was never done. The court said, "Whether the parties were in a franchise relationship, however, turns on the relationship that existed, not on the fact the parties might have constructed a different relationship."

Second, the landlord argued that, even if a franchise relationship had existed at one time, it did not exist at the time suit was filed because the jobber had by then rejected the supply agreement during the bankruptcy proceedings.

The court responded that the issue was whether or not a franchise agreement existed on the date that the alleged violation of the PMPA occurred. Here, the dealer was complaining about a notice of termination that it received months before the bankruptcy rejection, in October 1998, when the franchise relationship remained in effect.

Most significantly, the landlord also argued that it had an absolute right to terminate the dealer because of his sale of misbranded gasoline, relying upon the Second Circuit's earlier decision in *Wisser v. Mobil Oil*, 730 F.2d 54 (2nd Cir. 1984).

The Second Circuit stepped back from the seemingly absolute position that it had been taken in *Wisser*, finding that the sale of unbranded gasoline under the Coastal mark might not be a violation of the PMPA because (1) the supply agreement arguably contemplated that the dealer might purchase unbranded gasoline; (2) the jobber had itself delivered unbranded gasoline to the dealer for sale under the Coastal mark; and (3) the jobber's failure to perform adequately under the supply agreement might have justified the dealer's acquisition of gasoline on the open market.

The answer to the bar examination riddle that is the *Kolyum* case is not, however, complete. The puzzle remains as to what relief the dealer will ultimately be entitled to if he succeeds in proving a violation of the PMPA at trial.

Obviously, the dealer wants a right of first refusal to purchase the premises. The problem, however, is that his former supplier has lost the right to grant use of the Coastal mark, and the dealer has removed all Coastal signage.

Of course, the dealer had little choice given the threatened claim of trademark infringement. But the issue remains as to whether enough of a franchise relationship remains to justify the imposition of a right of first refusal under the PMPA.

Even the august Second Circuit appeared uncertain as the answer to this part of the bar examination question. It would merely "express no view on the question, leaving it entirely to the district court in the first instance."

We do not venture a guess as to the outcome, but await further developments.

pgunst@aggt.com

astrachan gunst thomas

attorneys at law
a professional corporation