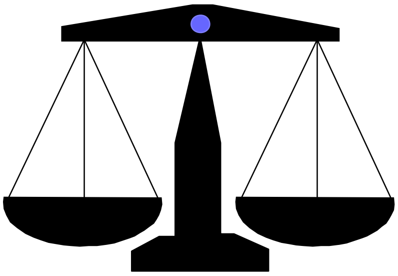

General Counsel Corner

By Peter H. Gunst, Esquire

Latest Development in Open Price Litigation

Probably the most perplexing legal issue faced by dealers and their attorneys is determining whether they have a basis for challenging a supplier's excessive pricing for motor fuel under the terms of an open price contract, which gives the supplier the discretion to change its dealer tankwagon price at will. Three recent federal court decisions give guidance as to how the law is evolving in this difficult area.

The underlying legal principles governing what is permissible in an open pricing relationship are found in § 2-305 of the Uniform Commercial Code, which has been enacted by state legislatures across the country. That provision requires a party setting prices pursuant to an open price contract do so "in good faith." The problem is in figuring out what "good faith" entails and what it does not.

Two lines of judicial decisions have emerged. Under one line – typified by decisions like that of the New Jersey Supreme Court in *Wilson v. Amerada Hess Corp.*, 168 N.J. 236, 773 A.2d 1121 (N.J. 2001), and the federal Fifth Circuit Court of Appeals in *Mathis v. Exxon Corp.*, 302 F.3d 448 (5th Cir. 2002) – dealers have been permitted to charge that their suppliers acted with "subjective" bad faith by pricing them out of the market in order to seize their locations.

The other line of cases – epitomized by *Shell Oil Co. v. HRN, Inc.*, 141 S.W.3d 429 (Tex. 2004) – holds that the whole notion of subjective bad faith is irrelevant because the supplier's only obligation is to charge a posted price that falls somewhere within the range of prices charged by all suppliers in the marketplace. This almost always gives the supplier a free pass because it can usually point to others in the marketplace who were charging similarly high prices.

This past year, three district courts examined the split of authority and came down on the side of permitting dealers to assert claims charging subjective bad faith, but with important evidentiary limitations.

In *Bob's Shell, Inc. v. O'Connell Oil Assoc., Inc.*, 2005 WL 2365324 (D.Mass. 2005), a group of lessee dealers charged the distributor who supplied them with bad faith pricing because the distributor's dealer tankwagon prices made it difficult if not impossible for them to compete with nearby distributor-operated stations and open locations supplied by the distributor.

Rejecting the distributor's motion for summary judgment and sending the dealers' case to a jury, the court held that the dealers were free to argue that the distributor had "made it impossible for [the dealers] to survive and that it set prices in an attempt to drive them out of business."

The court continued:

> [W]hile there may not be a fiduciary duty to protect one's dealer-lessees, wielding

> contractual leverage to eliminate competitors surely could violate good faith pricing.

In *Yonaty v. Amerada Hess Corp.*, 2005 WL 1460411 (N.D.N.Y. 2005), a lessee-dealer complained that Hess had priced its gasoline at "unreasonable levels that did not allow him to earn a profit upon market prices in the Binghamton market."

Although the court concluded that the dealer might be able to assert a bad faith claim if he could prove "his contention that [Hess] has a broad plan to force its franchisees out of business in order to increase the percentage of its operations that occur through company stations," it granted summary judgment to Hess because the dealer had failed to proffer any proof to back up his contention.

The court concluded:

> Without some evidence about Defendant's profit margins, Defendant's company station prices, the DTW prices of other franchises operating in the Binghamton area, the retail prices that other station in the Binghamton area and/or the relative percentage that the DTW prices constituted of Plaintiff's expenses, the Court has no means of assessing the propriety of Defendant's pricing policies.

Of interest, although the dealer lost on his pricing claim, he succeeded in defeating Hess' summary judgment motion directed against his claim under the Petroleum marketing Practices Act.

The dealer contended that Hess' failure to maintain the station and to deliver gasoline in a timely manner constituted a "constructive termination" of his franchise in violation of the PMPA. Given the hostility that some courts have shown to a constructive termination theory, the dealer's ability to survive summary judgment was a notable victory.

Finally, in *Callahan v. Sunoco, Inc.*, 2005 WL 994615 (E.D.Pa. 2005), the court adopted the "persuasive reasoning" of the New Jersey Supreme Court's *Wilson* opinion that "a party exercising its right to use discretion in setting price under a contract breaches the duty of good faith and fair dealing if that party exercises its discretionary authority arbitrarily, unreasonably, or capriciously, with the objective of preventing the other party from receiving its reasonably expected fruits under the contract."

As in the *Yonaty* decision, the court's decision in *Callahan* to recognize a bad faith pricing claim did not carry the day for the dealers who had sued their supplier. The court found that they had failed to present any specific evidence that Sunoco's pricing was in bad faith, and merely had argued abstractly that Sunoco's use of price zones was "fundamentally flawed." That, the court said, would not suffice.

Thus, these recent cases indicate that the glass is half empty and half full. Courts now generally appear to be willing to accept a subjective bad faith argument – despite *HRN*'s contrary holding – but demand considerable objective proof establishing bad faith pricing and its direct impact on the complaining dealer.

A bad faith pricing claim remains a tough fight, but a winnable fight under the proper circumstances.

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