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Stretching the PMPA

Attorneys for independent dealers repeatedly have attempted to stretch the reach of the Petroleum Marketing Practice Act beyond its normal context of formal franchise terminations and nonrenewals. They argue that the Act is intended to prohibit supplier misconduct that is equivalent to wrongful termination or nonrenewal, specifically supplier misconduct that leaves a dealer little choice but to surrender his or her location.

Dealer attorneys contend that, in situations where abusive pricing and rent policies render the continuation of franchise relationship impossible or nearly so, courts should recognize the doctrines of "constructive termination" and "constructive nonrenewal," even though the franchise relationship has not been formally severed. In sum, they argue that supplier should not be permitted to circumvent the Act's protection of the dealer's franchise rights by using its superior economic power to the dealer's disadvantage.

A very recent decision by the First Circuit Court of Appeals, which has jurisdiction over federal courts situated throughout most of New England, considered the subject in depth. That decision, *Marcoux v. Shell Oil Products,* drew a sharp distinction between the concepts of "constructive termination" and "constructive nonrenewal."

This lengthy and hotly contested litigation grew out of Motiva's termination of Shell's long-continued rent subsidy program, following Shell's transfer of its franchise relationships to the Motiva joint venture in 1998. Also at issue were Motiva's subsequent lease renewals and product pricing practices.

Following years of pretrial wrangling, a group Massachusetts dealers convinced a jury that Shell violated the PMPA by reneging on its promises of continued rent support, and thereby constructively terminated their franchises by rendering them financially unviable.

In addition, the jury determined that Motiva violated the PMPA by compelling the dealers to accept a new rent formula when their franchises came up for renewal, and breached the open price term provision of the dealers' supply agreements by failing to set prices for gasoline in good faith.

Not surprisingly, the defendants appealed.

Affirming the dealers' constructive termination claim, the First Circuit Court of Appeals held that the PMPA addresses situations where a franchisor has breached one of the three statutory components of the franchise agreement -- the contract to use the refiner's trademark, the contract for the supply of motor fuel and the lease of the service station premises -- or where the franchisor has assigned its obligations under the franchise agreement to a third party in violation of state law. Here, the evidence supported the jury's finding that Shell's repudiation of the promised rent subsidy program violated the lease component of the franchise agreement.

Shell argued that constructive termination would only occur if there were a *total* breach of the lease component of the franchise agreement, which deprived the dealer of actual occupancy of the service station. Shell argued that, because the dealers remained in their service stations, no total breach of the lease had occurred.

Rejecting Shell's argument, the First Circuit held that the PMPA would be violated absent a total breach if the franchisor's misconduct constituted "such a material change that it effectively ended the lease, even though the plaintiffs continue to operate the business."

The court explained:

> To require an actual abandonment of years of work and investment before we recognize a right of action under the PMPA would be unreasonable.

Clearly, the appeals court was correct. Had Shell's argument been accepted, the entire concept of constructive termination would have been rendered meaningless because, under Shell's definition, a total breach would only exist if actual termination had occurred. To the contrary, the concept of constructive termination properly embraces circumstances where the franchisor has employed means short of a total breach in order to render the franchise financially unviable.

Next the appeals court considered the dealers' constructive nonrenewal claim. The dealers argued that the new leases presented to them by Motiva failed to satisfy the PMPA's good faith requirement because the new rent formula was unreasonable. So as not to lose their stations, however, the dealers signed the new lease agreements "under protest" and included a claim for constructive nonrenewal in their law suit.

Reversing the jury's verdict for the dealers on that claim, the court of appeals rejected entirely the concept of constructive nonrenewal. It held that a dealer's exclusive remedy under the PMPA when faced with odious contract terms as part of a renewal proposal is to reject the agreement in its entirety and to seek injunctive relief in court during the 90 day notice period.

Though the First Circuit's rejection of the constructive nonrenewal concept can be criticized for the policy reasons set forth in the Ninth Circuit's contrary decision in *Pro Sales, Inc. v. Texaco, USA*, its position is consistent with the majority of cases in the area.

In most jurisdictions today, signing a franchise agreement "under protest" likely will not suffice protect a dealer's right to pursue a PMPA claim. The dealer's dilemma, therefore, is as set forth in the First Circuit's opinion:

> The franchisee therefore risks the end of the franchise if the claim fails and so must carefully weigh the decision to sign or sue. This is the balance Congress has struck, and should we prefer another,

> we would not be free to impose it.

Finally, the appeals court considered the unreasonable gasoline pricing claim, with happier results for the dealers. Affirming the jury's verdict, the appellate court rejected Motiva's argument that its pricing was reasonable as a matter of law because it did not discriminate in price between competing dealers that it supplied.

Motiva also argued on appeal that the dealers' evidence of unfair pricing was insufficient because they had relied almost exclusively on their competitors' lower retail prices, and presented little if any evidence of the dealer tankwagon prices charged to those competitive service stations.

Rejecting Motiva's contention, the court observed that because Motiva itself used a "street-back" pricing model in setting its dealer tankwagon price, it should not be heard to complain because the dealers relied upon street pricing to demonstrate Motiva's bad faith.

In sum, the *Marcoux* decision is of considerable significance. It does much to clarify the law of constructive termination and, unfortunately, constructive nonrenewal. It also provides helpful support for dealer complaints about unfair pricing practices. It will likely be cited and relied upon in many subsequent court decisions.

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