Radisson and the Potential Demise of the *Sealy-Barnes-Hinton* Rule

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During the past eleven years, there has been a lack of consensus in the courts as to the circumstances under which a franchisor is entitled to recover from a franchisee post-termination breach of contract damages for lost future profits, particularly lost future royalties. Nearly all courts have allowed such damages when the franchisee terminates, repudiates, or abandons its franchise. But there has been disagreement when the franchisor terminates after a default or breach by the franchisee. A number of courts, beginning most notably with the 1996 California appellate court decision in *Postal Instant Press, Inc. v. Sealy*[1] and followed by a 2002 Florida federal district court decision, *Burger King Corp., Inc. v. Hinton*,[2] have denied future damages in such situations, reasoning that the franchisor "proximately caused" its own future losses by its "election" to terminate the defaulting or breaching franchisee.[3] Meanwhile, other courts, essentially ignoring *Sealy*, have awarded franchisors future damages even when the franchisor terminates and the franchisee has not repudiated, terminated, or abandoned. In a recent decision on this subject, *Radisson Hotels International, Inc. v. Majestic Towers, Inc.*,[4] a California federal district court cast serious doubt on the continued vitality of the *Sealy* line of authority in the context of a liquidated damages clause in a hotel franchise agreement.

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We first summarize the history of this hotly debated issue. We then suggest that what we call the *Sealy/Barnes/Hinton* rule[5] does not make sense. That rule, which basically allows future damages if the franchisee, but not the franchisor, terminates (even if the franchisee has committed continuing uncured breaches), elevates form over substance by failing to properly analyze proximate causation and, in many cases, properly apply principles of mitigation to avoid excessive damages. We suggest instead an approach more consistent with basic contract principles under which future lost profit damages should be available if, at the time of contracting, the parties might reasonably have foreseen that such losses would be the probable result of the franchisee's breach. However, whether or not the agreement granted the franchisee an exclusive territory, a franchisor should not recover lost profits that the franchisee proves could have been either avoided by installing a replacement franchisee or otherwise mitigated.

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Case Law History

A substantial number of decisions have addressed the issue of post-termination lost future profits. These decisions can be categorized in a variety of ways. One distinction is between cases arising in the hotel industry and cases arising in all other areas. Perhaps due to the prevalence of liquidated damages clauses in hotel industry franchises, the *Sealy/Barnes/Hinton* rule has never been applied in hotel industry cases. Hotel franchisors generally have succeeded in obtaining future damages (provided they are reasonably certain and properly mitigated) even when they have terminated a franchisee for breach. It is only outside of the hotel industry that the *Sealy/Barnes/Hinton* rule has been applied. We separately review the history of non-hotel and hotel industry authorities because, until *Radisson*, these two lines of authority generally took little notice of each other despite having considerable in common.

THE NON-HOTEL CASES

Successful Breakaway Franchisees?

In *McAlpine v. AAMCO Automatic Transmissions*,[6] the first lost future profit decision of any consequence, the federal district court ruled in favor of the franchisor under Michigan law and explained in some detail the equities of that side's position on this controversial issue. In this case, a number of franchisees broke away to form a competing business, and also sued their franchisor alleging antitrust violations and contract breaches. The franchisor counterclaimed, seeking, among other things, $50,000 in past due royalties plus five times that amount ($250,000) for lost future royalties, as well as another $110,000 in expenses to refranchise in the market. After a bench trial, the court ruled against the franchisees on their claims, including allegations that the franchisor's wrongful conduct justified the franchisees' termination, and held that the franchisor could recover future damages for the franchisees' wrongful repudiation and termination of their agreement.[7]

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The court viewed the "major theme" of the case as "the problem of the successful franchisee who becomes dissatisfied in his franchise arrangement and desires to sever relations with the franchisor," an "emerging and increasing phenomenon in franchisee-franchisor relationships."[8] Sometimes, said the court, the franchise arrangement starts as mutually advantageous, both sides contributing to obtain benefits they could not obtain independently. The franchisor contributes its trademark, recognized product or service, experience, advertising, and management support. The franchisee contributes its capital, day-to-day management, and payment of fees. As the franchisee becomes successful, however, what seemed reasonable at inception may appear burdensome. The franchisee that has learned a system and reaped its benefits sometimes wonders if its new-found knowledge could enable it to prosper more on its own.[9]

The court spent little time addressing whether the franchisor was entitled to lost future profits from franchisees that broke away. Instead, the decision focused primarily on the method of calculating the damages and, of particular significance, mitigation. The court rejected as speculative the franchisor's "elaborate model" calculating royalties as a percentage of projected sales based on assumptions of a sustained future growth trend in the area.[10] The court similarly denied lost future profits pertaining to one franchisee that had never opened for business and thus had no track record. The court assumed that the ten other franchisees would have continued at the sales levels they experienced before leaving the system. By the time of trial, four years after the plaintiff franchisees left, new franchisees were already generating as much as the breakaway franchisees had. The court was therefore able to cap damages under mitigation principles as of the date when the new franchisees reached this threshold amount.[11]

More Than a License?

The next case of significance was *In re Mid-America Corp.*,[12] where a federal bankruptcy judge held that a franchisor was entitled to future damages for the full remaining term of the agreement with franchisees that abandoned their franchises by closing their doors. Ultimately, the court denied recovery because the franchisor's proof was too speculative. First, however, the court addressed the franchisee's argument that it owed no future damages because a franchise agreement is no more than a license, imposes no obligation on the franchisee to continue operating the restaurants, and thus does not entitle a franchisor to any expectation of future income or profits after termination. One form of the franchisor's agreement expressly stated, however, that the franchisee would operate for the entire term. Other forms granted the right to do so, and their default sections indicated an affirmative obligation to operate by making cessation of operation and voluntary abandonment without the franchisor's consent an event of default, entitling the franchisor to terminate and obtain lost future profits damages for breach. The court's rejection of the argument that the franchise was no more than a license is interesting in light of the fact, discussed below, that the subsequent *Sealy* decision turned in large part on an analogy to a patent license case, *Fageol & Tate v. Baird-Bailhache Co.*,[13] which denied future royalties after a patent licensor terminated a licensee's license.

Same but Different?

The final decision before *Sealy*, *In re Montcastle*,[14] concerned, like *Sealy*, the Postal Instant Press (PIP) franchise system, but it reached an opposite result from *Sealy* under California law. The franchisees in *Montcastle* "happily" paid royalty and advertising fees until PIP changed management and made operational changes with which the franchisees disagreed.[15] The franchisees then stopped making the required payments, believing they no longer derived benefit from the franchise relationship. As with *Mid-America*, earlier, the court interpreted the PIP franchise agreement to obligate the franchisees to pay not just past due fees of about $57,000 but also future fees of about $275,000 over the entire remaining period of eight and one-half years. The court credited PIP with making a "strong case" for its lost future profits because, in establishing a new franchisee, PIP incurred significant start-up costs. "[It] would be inequitable" (indeed, "perverse"), said the court, "to allow a franchisee to take advantage of PIP's training and assistance to establish a successful printing operation and as soon as the business becomes profitable, allow the franchisee to terminate the agreement, leaving the franchisor without the contracted for ability to recoup its initial expenditures" and the benefit of the parties' bargain.[16]

In sum, lessons from these three pre-*Sealy* decisions appear to include the following:

- franchise agreements will be interpreted to obligate payment of fees over their entire term; and
- franchisors may be entitled to receive such fees as lost future profit damages when franchisees abandon the system or cease paying their fees, provided that the franchisors can establish such future fees with reasonable certainty and that they take appropriate steps to mitigate their losses by attempting to refranchise.

Birth of the *Sealy/Barnes/Hinton Rule*

Sealy was decided three years later in 1996. In the late 1980s, after operating successfully for many years, a PIP franchisee failed to make several monthly payments of royalty and advertising fees. It then entered into a negotiated note for past due amounts. In 1991, the franchisee became delinquent on the note and also failed to make several regular payments. The franchisee testified that it gave other obligations a higher priority. The parties' agreement expressly made failure to cure non-payment a material breach, entitling the franchisor to terminate and recover its damages, including "the benefit of its bargain."[17] In early 1992, PIP terminated on this basis. Relying on past sales history, the trial court awarded lost profit expectation damages for the remaining seven-and-one-half-year term (approximately $300,000, the discounted value of future royalty and advertising fund contributions after deducting incremental costs of performance), in addition to past due amounts owed of approximately $77,000.

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The California Court of Appeal reversed the award of lost future profits on two grounds. First, characterizing the franchisee's breach as "a mere failure to pay,"[18] it held that future losses were proximately caused not by the franchisee's breach, but by the franchisor's election to terminate because of it. The franchisor could have, instead of terminating the relationship, simply sued the franchisees for the money owed, conceivably "again and again," to compel payment.[19] Second, even assuming the contract were construed to permit such damages, they would be impermissible as excessive, unconscionable, and oppressive under a California statute prohibiting award of such damages. They were also "disproportionate compensation" under the Restatement (Second) of Contracts.[20]

In addition, the court suggested in a lengthy dicta footnote[21] that there might have been a third basis for reversing the lower court, i.e., PIP's failure to establish lost future profits with requisite "certainty." The court noted that it would be difficult to estimate future profits in "a field as volatile as printing and reproduction." However, the "major imponderable," it said, was the ability of PIP, having terminated the Sealys, "to open a new outlet directly across the street" from the Sealys or to open up a "megastore" nearby. "In either event, the Sealys could lose most or all of their business" and "[t]o the extent [PIP] received royalty payments [from a new store,] PIP would not experience net 'lost profits.'" The court's note also stated that it would be unfair to award PIP damages because PIP would have little incentive to install a replacement franchisee until it received an award. PIP could thus collect a "double recovery": the award from the terminated franchisee and royalties from the replacement.

The *Sealy* court, in contrast to *McAlpine* and *Montcastle*, summarized additional equities from a franchisee's perspective to support its second holding. The court felt that franchise agreements, though commercial, "exhibit many of the attributes of consumer contracts," including a relationship characterized by a prevailing "inequality of economic resources" and "unequal bargaining power," as well as form "contracts of adhesion."[22] The court expressed concern that affirming the lost profits award would so unbalance the relationship as to make every franchise agreement unconscionable and oppressive. The court "imagine[d]" as a result of such a decision franchisors "crack[ing]" the "whip of a giant" "now and then to keep their" "enslaved" franchisees "in line" if they "fail [] to do everything exactly the way the franchisor demands. . . ."[23]

The *Sealy* opinion supported its first holding, i.e., proximate cause, in two ways. Noting the general similarities between franchises and license agreements, the court cited a 1931 California appellate decision, *Fageol & Tate v. Baird-Bailhache*,[24] holding that a licensor's decision to terminate a breached patent license agreement also terminated the licensee's duty to pay future royalties under the agreement.

In addition, the court distinguished cases that awarded lost future profits as involving "total failures to perform at all," "total" breaches, and situations where a defendant "stopped performing at all" and "directly prevented the plaintiff from earning [future royalties.]"[25] Whether a franchisor could ever recover lost profits would depend, said the court, on the nature of the breach and whether the breach itself prevented the franchisor from earning future royalties "independent of the franchisor's own termination."[26] Thus, the court seemed to suggest that whenever a franchisee committed any type of breach that could be cured, leaving a franchisor with an election to tolerate (albeit perhaps suing for specific performance or partial breach damages) or instead to terminate, the franchisor could not recover lost future profits if it chose to terminate. Consider, for example, situations where a franchisee fails to permit audits of revenue on which royalties are based; misreports those revenues; sells unauthorized products; has signage and facility deficiencies; or has other failures to comply with system standards, e.g., restaurant health and cleanliness. All can be cured. Apparently *Sealy* would permit no lost future profits for termination on any of these grounds because of the franchisor's election. Query what *Sealy* would do with franchisee breaches that cannot be cured, such as fraud or a felony conviction? Even in those situations, the franchisor generally has the election under the agreement of whether to terminate.

The *Sealy* decision, particularly its use of proximate causation in this manner, proved to be controversial and generated much critical commentary.[27]

Disagreement Since *Sealy*

In the eleven years since *Sealy*, there have been basically three types of decisions. First, most cases have allowed the franchisor to recover when the franchisee terminates, repudiates, or abandons.[28] Perhaps the most notable example of this is *Burger King Corp. v. Barnes.*[29] That case, for reasons discussed below, is also notable for rejecting, on the ground that the franchise agreement did not grant an exclusive territory, the franchisee's claim that the franchisor failed to mitigate its losses, reasoning that "[w]hen a non-exclusive contract is involved which would allow a plaintiff to enter into other similar contacts, an exception to the requirement of avoiding foreseeable consequences is created and there is no duty to mitigate or minimize losses."[30]

Second, five courts have, in fact, followed *Sealy*, or employed a similar rationale, by denying franchisors the right to future lost profits where the franchisee materially breached and the franchisor terminated, on the ground that the franchisor caused its own loss. A flagship case in this area is *Hinton*,[31] written by the same federal judge who decided *Barnes* four years earlier. As one commentator from the eastern United States observed, *Hinton* gave "credibility" to *Sealy*, a decision previously viewed by many as an "anomaly" from a "'Left Coast' court" "out of the mainstream," while Florida was apparently, by contrast, "considered very mainstream."[32] In *Hinton*, the franchisee failed to pay fees and other debts. Though the *Hinton* court said *Sealy* did not apply because Florida law governed, the court nonetheless denied the franchisor's future damage claims on the same proximate cause rationale.[33]

Third, some decisions have ignored *Sealy* and awarded the franchisor lost future profits even where it has terminated and the franchisee has neither repudiated nor done the equivalent. A good example is *American Speedy*

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Printing Center, Inc. v. AM Marketing, Inc.,[34] where the franchisee failed to report and pay royalties for various months over three years. The Sixth Circuit ignored *Sealy* and, applying Michigan law (as had *McAlpine*, discussed above, and *Kissinger, Inc. v. Singh*, *supra* note 33, reaching different results), awarded the franchisor its lost future royalties and profits.[35]

THE HOTEL CASES

A long line of cases from the hotel industry shows more consistent willingness to allow franchisors to recover lost future profits, even where a franchisor terminated for something less than repudiation or abandonment by the franchisee. Most,[36] though not all,[37] of these decisions involved liquidated damages clauses. Some of these decisions,[38] although not all of them,[39] involved, as in *Radisson*, liquidated damages provisions limited to two years, apparently predicated on the mitigation assumption that it takes about that long to find a replacement hotel franchisee. Until *Radisson*, only one of these hotel cases mentioned *Sealy*, and even then only in passing.[40]

The recent *Radisson* decision involved no more than, as *Sealy* stated, a franchisee's "mere failure to pay."[41] The franchisee was in business little more than six months when its payments became overdue. A series of notices to cure, partial payments, more notices, and, ultimately, a notice of termination ensued less than a year after opening. The agreement expressly gave the franchisor the election to take such a step, just as did the agreement in *Sealy*.[42] A liquidated damages provision provided for two years of lost future royalties. The franchisor sued for past due amounts of approximately $300,000 and liquidated damages of nearly $700,000. The franchisee did not meet its burden of proving the two-year provision unreasonable. It also argued that *Sealy*'s proximate cause holding precluded lost future royalties. *Radisson* granted summary judgment to the franchisor on its first two claims for past due amounts and liquidated damages for contract breach.

The court treated *Sealy* in two ways. First, it distinguished the case because the agreement there "only vaguely stated that the franchisor would be entitled to the 'benefit of the bargain'" if the franchisee materially breached.[43] "Given this contractual context," said the court, *Sealy* held that lost future royalties were not proximately caused by the franchisee's failure to pay past royalties, and "under the default contract principles governing the claim, these lost future royalties were not part of the 'bargain.'"[44] In *Radisson*, by contrast, an express contractual provision made the franchisee "liable for Radisson's lost future profits resulting from Radisson's decision to terminate" if "motivated" by the "mere failure to pay overdue royalties."[45]

The court then observed that the liquidated damages clause "functionally" required the franchisee to indemnify the franchisor's lost profits if the franchisee was terminated for failing to pay, noting perhaps somewhat rhetorically, "To this [c]ourt's knowledge, there is no rule that prevents a party from indemnifying (or insuring) losses that might otherwise not be recoverable under a contact law theory."[46] It then simply enforced the provision without saying specifically how the franchisor's election to invoke "functional indemnification" by terminating the franchisee and collecting liquidated damages did not run afoul of the *Sealy/Barnes/Hinton* rule in the sense that election to invoke the provision caused the loss of the franchisor's royalties.[47]

Interpreting Radisson Under *Sealy*

There are a number of ways to understand what might seem like *Radisson's* sleight of hand in dealing with the difficult *Sealy/Barnes/Hinton* rule.[48] One can view the court as essentially holding that proximate causation was satisfied by foreseeability: the clarity of the liquidated damages clause made termination and the subsequent loss of future profits a foreseeable result of breach by the franchisee. A somewhat different interpretation is to view the court as simply avoiding *Sealy* proximate causation through its indemnity provision analogy. The franchisor in *Radisson* needed to prove causation no more than a party invoking an indemnity provision needs to disprove that the decision to invoke the provision is the "cause" of the damage for which indemnity is sought. In all events, it is clear that the parties' expectations, as reflected in the contract, were somehow critical in either satisfying or avoiding *Sealy's* proximate causation analysis.

Clearly, though, the *Radisson* court had problems with the *Sealy* analysis. The court also stated in a dicta footnote,[49] as an alternative basis for its holding, that it believed the *Sealy* decision was "mistaken" and not binding (because it was not a California Supreme Court decision). The court noted that *Sealy* based its proximate cause analysis "on a single case involving a licensor-licensee relationship" decided by another intermediate court of appeal in 1931 (*Fageol*). The court's note also characterized *Sealy*'s holding that PIP should have to sue its franchisee "over and over again" as "simply untenable." The court noted by contrasting analogy that, though governed by statute, California law allows landlords to terminate tenancies and sue tenants for damages measured by the likely amount of lost future rent. Similarly, the *Radisson* court believed that when a franchisee is unable or unwilling to meet its obligations, lost future profits are a proximate result of the breach because "the franchisee's actions are a 'substantial factor in bringing about that loss or damage.'"[50] Thus, the court concluded that it did not find *Sealy* to be persuasive.

Problems with the *Sealy/Barnes/Hinton* Rule

Radisson points to an approach that should be used consistently in both the hotel and non-hotel context: application of traditional contract law principles, rather than facile reliance on the *Sealy/Barnes/Hinton* rule. We suggest below two principal analytical problems, with this rule. First, *Sealy* failed to properly analyze proximate causation. Second, *Barnes* improperly limited mitigation to cases involving exclusive franchises, while *Sealy* failed to consider mitigation because the defense was not raised. That failure improperly bolstered *Sealy's* conclusion that awarding future damages would be excessive.

Misanalysis of Proximate Causation

Sealy failed to properly analyze proximate causation in three ways. First, while citing hornbook law that the non-breaching party is entitled to recover only damages "proximately caused" by the breach and that lost profits must be its "natural and direct consequence,"[51] the court did not state fully, or discuss and properly

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apply, the test for causation in contract cases in California, nor did it adequately consider the related, critical issue of "foreseeability." Second, the court relied in large part on *Fageol*, an inapposite patent license decision. Third, the court ignored substantial authority that a non-breaching party's election to terminate a contract for material breach does not bar such a party from seeking expectation damages.

Proximate Causation and Foreseeability

As *Radisson* noted in criticizing *Sealy*, discussed above, the California test for determining proximate causation in contract cases is whether a breach was "a substantial factor in bringing about" a plaintiff's loss. *See Radisson* at 10 n.10, citing *U.S. Ecology*, which cited *Bruckman v. Parliament Escrow Corp.*,[52] which relied on 5 Corbin on Contracts § 999 (1964), whose discussion is essentially now found in 11 Corbin on Contracts § 55.9 (2005). "Substantial factor" is defined as "something which is more than a slight, trivial, negligible, or theoretical factor in producing a particular result." *U.S. Ecology*.[53]

Traditional analysis does not end with this causation test, however, as *Bruckman v. Parliament Escrow Corp.* illustrates by its reliance on Corbin and reference to *Hadley v. Baxendale*.[54] *Hadley*, of course, teaches that a contracting party is entitled only to damages that were a reasonably foreseeable result of the other party's breach.[55] Inquiry is not limited to what the parties *actually* foresaw and intended in their contract, but also includes what they *should have foreseen* under the circumstances at the time of contracting.[56]

General damages, for example, are those "that would naturally arise from the breach, or that might have been reasonably contemplated or foreseen by both parties at the time they made the contract, as the probable result of the breach."[57] Special or consequential damages, similarly, are those that, although not an invariable result of every breach of the type in question, "were reasonably foreseeable or contemplated by the parties at the time the contract was entered into as a probable result of a breach," based on special circumstances that were known or should have been known to the parties.[58] Some have suggested that in contract cases, foreseeability really is or should be the test for determining legally cognizable causation. Corbin, for example, states thus:

> Cases are very numerous in which damages have been refused on the supposed ground of remoteness or because the injury was said not to be the "proximate" result of the breach, but in such cases if the court attempts a definition it will practically always be found that it is expressed in terms of the possibility of foresight.[59]

Essentially, this seems to be true in California, where *Sealy* was decided, insofar as substantial factor causation arguably is easier to establish than *Hadley* foreseeability. That is, if the result of a breach is reasonably foreseeable as probable, the breach likely "is more than a slight, trivial, negligible, or theoretical factor in producing a particular result."[60]

The *Sealy* court ignored the substantial factor test and largely failed to analyze foreseeability. Had the court stated and applied the substantial factor test, it would have had difficulty disputing *Radisson*'s suggestion that the test is satisfied where a franchisee fails to make payments to the chronic extent that the franchisee in *Sealy* did.[61] Such a failure would seem more than a "slight, trivial, negligible, or theoretical factor" in causing a franchisor's decision to terminate. And the decision to terminate necessarily causes a cessation of royalty payments from the franchisee.

With respect to foreseeability, *Sealy* inadequately considered whether the parties should have reasonably foreseen, when contracting, PIP would probably lose future royalties if the Sealys repeatedly failed to pay royalties when due and PIP terminated as a result. Without reviewing any evidence of the parties' actual expectations or whether, under an objective reasonable person standard, such damages would be foreseeable, the court simply asserted:

> we do not construe the franchise agreement as permitting this form of damages as part of the franchisor's "benefit of the bargain" when it elects to terminate the franchise because a franchisee failed to timely make some past royalty payments. As pointed out in this earlier section, in the context of a franchise arrangement "future lost profits" are not a result of the franchisee's breach in failing to timely pay royalties but of the franchisor's election to cancel the franchise agreement. Consequently, the receipt of "lost future royalty payments" is not part of the bargain to which the franchise agreement entitles the franchisor when it terminates for this type of breach.[62]

The court, in other words, simply assumed that because, in its view, the franchisor had caused its own losses, the parties' agreement could not possibly have contemplated damages for such losses as a part of the "benefit of the[ir] bargain."

Misplaced Reliance on *Fageol*

In addition to inadequately stating and applying rules regarding causation and foreseeability, the *Sealy* court, as noted above, relied on a prior case, the 1931 *Fageol* decision (holding that a patent licensor's decision to terminate a breached patent license agreement also terminated the licensee's duty to pay future royalties under the agreement). Basing its decision in large part on a loose analogy between franchising and licensing, the *Sealy* court concluded that the *Fageol* rule should apply to a franchisor that terminates a franchisee for failure to pay. *Fageol* seems to reflect a rule stated in the current version of 69 *Corpus Juris Secundum, Patents* § 379 (2007): "When a license has been properly terminated, the licensee is no longer liable for royalties." Furthermore, this rule holds true, among other situations, where a licensee "unequivocally repudiates" or where a licensor terminates for "failure of the licensee to pay royalties."

As the *Radisson* court suggested in passing, the *Sealy* court seems to have leapt too quickly on *Fageol* to support its analysis.[63] There are at least two reasons. To begin, thirteen years after it was decided, *Fageol* was distinguished in another decision, where a licensor was entitled, under an unjust enrichment theory, to future royalties because after the licensor terminated the license, the licensee continued to use the licensed patent.[64] The Sealys, by virtue of California's refusal to enforce non-compete covenants, remained in business.[65] Thus, *Fageol* arguably provided no safe harbor in their situation.

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More fundamentally, however, a franchise agreement is more than a patent license, which basically is an agreement allowing a manufacturer to avoid infringement liability for the duration of the license.[66] Franchisors not only license trademarks and authorize use of trade secrets; they also train franchisees in exchange for some future performance and provide other forms of support that can be licensed but do not have to be secret or protected intellectual property. In these contexts, future profits may be recoverable even after termination of the license.

Two decisions illustrate this. In *Universal Gym Equipment, Inc. v. ERWA Exercise Equipment Ltd.*,[67] Universal licensed the defendant to make and sell exercise machines in return for a royalty. Universal was obligated to provide plans, specifications, and engineering knowledge to ensure proper assembly and performance of the product. The defendant agreed to keep the technical knowledge confidential. The license allowed termination by either party without cause, in which event the defendant should not "manufacture, use, sell or distribute any products which include any of the features, designs, technical information, or said know-how of [Universal]."[68] Universal eventually exercised its option to terminate. The defendant then began making and selling exercise equipment through a newly formed company. The lower court found that the information imparted by Universal was not a trade secret.[69] Nonetheless, the appellate court affirmed an award of damages, including future profits Universal lost due to the defendant's sales of machines using Universal features and designs. *Universal* demonstrates that under know-how licenses, post-termination future damages may be awarded, depending upon the provisions of the license agreement.

Californians for Population Stabilization v. Hewlett-Packard Co.[70] is a somewhat similar case. It concerned a liquidated damages provision in a contract by Tata, a company that trained Indian computer engineers and contracted with Silicon Valley manufacturers to supply the engineers for time-limited projects (deputations) in California. The engineers signed contracts with Tata promising to complete their California deputations and pay $30,000 in liquidated damages if they did not. A public interest group challenged the contracts as an unfair business practice. The court held that the liquidated damages provision for failure to complete deputations was enforceable and not an unjust business practice. In other words, having trained the engineers (as franchisors train franchisees), Tata was entitled to compensation for post-termination losses.

In sum, though the *Fageol* rule may apply in certain patent licensing situations, it should not have been imported into franchising law to support *Sealy*'s proximate cause rationale.[71]

Mistaken Assumptions

Finally, rather than asking whether it was reasonably foreseeable that the franchisee's breaches probably would cause PIP to terminate (and cause the cessation of future payments under the contract), the *Sealy* court focused on PIP's role in the chain of causation. It spent considerable time contrasting the Sealys' "mere failure to pay," which it said gave PIP an "election" to terminate,[72] with cases that awarded lost profits for breaches involving "total failures to perform at all."[73] The discussion created the impression that a non-breaching party is, as a matter of law, entitled to expectation damages only if it had no alternative in the circumstances, i.e., a defendant's breach cannot "proximately cause" a plaintiff's lost future profits if the plaintiff elects to terminate. Under traditional contract principles, this simply is wrong.[74]

An uncured material breach generally discharges the non-breaching party's remaining performance and entitles it to sue for damages for total breach, i.e., damages based on all of the injured party's remaining rights to performance.[75] Materiality does not require that a non-breaching party have no alternative but to walk away from the contract. To the contrary, as the Restatement recognizes, such a party can elect to sue for total breach damages or, instead, choose to waive such a breach and continue performance:

> If, in spite of the [total] breach, he wishes to await performance by the party in breach and to have merely a claim for damages for partial breach rather than for total breach, he can excuse the non-occurrence of the condition of his remaining duties (§ 237) by promising to perform them in spite of its non-occurrence (§ 84).[76]

The franchise decision in *Center Garment Co., Inc. v. United Refrigerator Co.*[77] illustrates the principle that the circumstances creating total breach are not always so clear-cut and non-elective as *Sealy* suggests, and that even franchisees can have the option to proceed with their agreement or, instead, elect to leave the system (i.e., to terminate) and obtain damages for total breach.

The franchisor in *Center Garment* sold a machine that made plastic signs. The franchisee agreed to buy components such as acetate from the franchisor or, in the alternative, from an approved supplier. After the franchisee went into business successfully, the franchisor had problems with its acetate supplier and could not provide that component for two months. Instead of procuring it elsewhere, the franchisee chose to close the business, claiming total breach. Relying on the former draft of what is now Restatement (Second) of Contracts Section 243, the court affirmed the lower court's decision that the plaintiff could take "the more drastic response" even though the plaintiff "may have seized the chance for terminating the contract with some enthusiasm, as it had been considering disposing of the business."[78]

Indeed, the Restatement does not even require proof of material breach excusing further performance (or partial breach plus repudiation) to entitle a non-breaching party to a claim for total breach damages. That remedy can be available in other cases if the breach "so substantially impairs the value of the contract to the injured party at the time of the breach that it is just in the circumstances to allow him to recover damages based on all his remaining rights to performance."[79] Such a balancing process is hardly the either/or situation involving "total failures to perform at all," which the *Sealy* court assumed to be necessary.

A California Supreme Court decision on which the Restatement is based, *Coughlin v. Blair*,[80] makes clear that just as the Sealys' failures to pay increased over time, failure to perform on a timely basis can rise to the level of total breach even if, initially, it was not:

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> Defendants could not reasonably expect plaintiffs to continue indefinitely to treat the breach as partial. . . . Although defendants had not expressly repudiated the contract, their conduct clearly justified plaintiffs' belief that performance was either unlikely or would be forthcoming only when it suited defendants' convenience. Plaintiffs were not required to endure that uncertainty or to await that convenience and were therefore justified in treating defendants' non-performance as a total breach of the contract.[81]

Sackett v. Spindler[82] illustrates that failures to pay, as in the *Sealy* case, are within the scope of this rule. A purchaser of corporate stock paid part, but not all, of the price. Relying on *Coughlin*, the court held that though the buyer frequently expressed willingness to pay, his delays in the face of the seller's many requests for payment warranted the inference that he never would perform, or would do so at his own convenience. The seller was not required to endure the uncertainty or await the buyer's convenience[83] and was entitled to the difference between the contract price and the net amount received from a subsequent sale, the full benefit of the seller's bargain.[84]

Coughlin and *Sackett* thus support the proposition that a franchisor need not endure forever a franchisee's convenience in receiving payment, or not, before electing to sue for the full benefit of the parties' bargain. For a court such as *Sealy* to conclude as a matter of law that the exercise of such an election eliminates the possibility of proximate causation is to deny the existence of this rule of law.[85]

In sum, it is inappropriate to rely in a franchise case on a patent licensing rule regarding post-termination damages. Well-established authority disproves the notion that an election to terminate for material breach necessarily defeats proximate causation. The proper proximate cause analysis simply is whether it is reasonably foreseeable, at the time of contracting, that a franchisor's loss of future profits will be the probable result of a franchisee's breaches.[86] Had this test been applied, the outcome in *Sealy* might have been different.

Mitigation Principles

In addition to improperly analyzing proximate causation, *Barnes* and *Sealy* each in its own way misapplied the rules of mitigation in the context of those cases. *Barnes* denied the franchisee the defense of mitigation. *Sealy*, on the other hand, concluded that damages were unreasonable based in part on assumptions that were unsupported in the record because the franchisee offered no evidence supporting the defense of mitigation (or showing speculative damages).

The general mitigation rule is that a party injured by a breach of contract must do everything reasonably possible to avoid the loss and thus reduce the damages for which the other party is liable. Accordingly, there can be no recovery for losses that could be avoided without "undue risk, burden or humiliation."[87]

According to the Restatement (Second) of Contracts, the mere fact that an injured party can enter an alternative transaction "does not necessarily mean that by doing so he will avoid loss. If he would have entered into both transactions but for the breach, he has 'lost volume' as a result of the breach. . . . In that case the second transaction is not a 'substitute' for the first one."[88]

"Whether a subsequent transaction is a substitute for the broken contract sometimes raises difficult questions of fact. If the injured party could and would have entered into the subsequent contract, even if the contract had not been broken, and could have had the benefit of both, he can be said to have 'lost volume' and the subsequent transaction is not a substitute for the broken contract."[89]

"Whether an available alternative transaction is a suitable substitute depends on all the circumstances. . . ."[90]

Barnes

As noted earlier, *Barnes*, a federal court decision applying Florida law, held that mitigation by the franchisor was not an issue because the franchise agreement did not grant the franchisee an exclusive territory. The rationale seems to be that only in an exclusive contract situation does termination of a franchisee create an otherwise unavailable opportunity to avoid losses by installing a replacement franchisee. Some apparently believe that this is the law outside of Florida, too.[91]

We agree with the cited commentator that such a rule does not make sense because, as a practical matter, exclusive territory or not, a franchisor is barred by economic reality from installing a new franchise at least some distance from its existing ones:

> Can it be said that the franchisor who refuses to grant exclusivity truly has the opportunity to put the next franchise anywhere it wants? Realistically, there are only so many Burger Kings or McDonald's restaurants that can be opened in a specific trade area. In effect, as long as there is one such restaurant in that territory, the franchisor is foreclosed from opening a second one there, even if it may have a legal right to do so.[92]

Put differently, the termination of a franchisee, particularly one that does not then remain in business and independently compete, generally creates a new opportunity to install another franchisee, whether or not the franchise agreement is exclusive. Accordingly, terminated franchisees should be allowed to present evidence regarding mitigation, such as, for example, evidence of the time it took the franchisor to appoint the terminated franchisee at the beginning of their relationship. Franchisor future damages should be limited as appropriate based on the circumstances affecting a franchisor's ability to refranchise.

We question, however, the assumption that the law precludes such an analysis where the franchise agreement does not expressly grant an exclusive territory. To our knowledge, *Barnes* is the only franchise case to apply this rule.[93] *Barnes* relied on two decisions by intermediate Florida courts of appeal outside the franchise context. *Gary Massey Chevrolet, Inc. v. Ritch*[94] held that a non-exclusive construction contract allowed the plaintiff contractor, had he chosen to do so, to have entered into other similar contracts, so he was under no duty to minimize his losses from an auto dealership's breach of their agreement. *Gary Massey* relied on, among others, *Graphic Associates*, *Inc. v. Riviana Restaurant Corp.*,[95] the

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second case that *Barnes* cited. *Graphic Associates* held that whether a plaintiff's damages should be reduced under mitigation principles "depends upon the facts" and on whether, "under all the circumstances," the contract was either exclusive or non-exclusive.

The *Graphic Associates* court relied on discussion in the hornbook by Calamari and Perillo, *The Law of Contracts*, which has a section (Section 14.16) entitled "Non-Exclusive Contracts—An Apparent Exception to the Doctrine of Avoidable Consequences." The authors explain as follows the general notion of whether the fruits of a subsequent contract should reduce the damages lost from breach of an earlier agreement: "[I]f the relation between the parties is such that the wronged party was legally free to enter into similar contracts with others, that subsequent to the breach the wronged party could have or actually has made similar contracts, in no way reduces the entitlement to damages."[96]

The hornbook section's remaining discussion of case examples draws no hard-and-fast rule as to "non-exclusive" contracts, however. Calamari analyzes the particular facts of the relationship and businesses, that is, "all the circumstances," as *Graphic Associates* itself said was appropriate, some of which require, because of the nature of the contract, that consequences of breach be avoided whether or not the contract is expressly "exclusive."[97]

Williston, by contrast with the Calamari hornbook, does not suggest that "non-exclusivity" is necessarily a determining factor in whether mitigation can be asserted.[98] The most recent edition of the Corbin treatise is authored by Calamari's co-author, Perillo, who includes a lengthier chapter with the same heading as the hornbook section (see above). Corbin begins with a generalized rule that says nothing about "non-exclusive" contracts.[99] The chapter is like the hornbook, identifying no hard-and-fast rule on "non-exclusive" contracts. Significantly, it does not even cite *Barnes*, which arguably creates such a rule, or to the decisions in *Gary Massey* or *Graphic Associates* on which *Barnes* was based.[100]

We submit that Florida courts, including *Barnes*, are mistaken in assuming that mitigation principles do not apply when a franchise contract does not provide an "exclusive" territory. Instead, as an older Florida Supreme Court case cited by *Gary Massey* suggested, an obligation to avoid loss, i.e., a mitigation defense issue, can be established with evidence showing that "it was *impracticable* for plaintiffs to be engaged in other business and the performance of other contracts contemporaneously with the performance of the contract in controversy."[101] Evidence that it was economically impracticable under all the circumstances, even if not illegal, for a franchisor to open another franchise within a certain distance from a defendant franchisee would thus seem probative under Florida law of whether the franchisor should not have attempted to refranchise at least within that area after termination.[102] This assumes, of course, that a franchisee asserts such a defense.

Sealy

Sealy presents a different issue as to mitigation. The court there concluded that the damages awarded PIP were unconscionable, grossly excessive, and contrary to substantial justice, all contrary to California Civil Code Section 3359,[103] and were also disproportionate, contrary to the Restatement (Second) of Contracts Section 351(3).[104] The court believed that PIP received adequate reasonable damages from past due royalties and attorney fees and costs, "along with its right to immediately install a new franchisee in what formerly had been the Sealys' exclusive territory. . . ."[105] Indeed, the court expressed concern that PIP could receive double profits both from the future damages awarded for the remaining term of the franchise agreement and from royalties that a new franchisee would pay the franchisor over the same period.[106]

The problem with this analysis is that the franchisee never offered evidence regarding mitigation in the trial court—thus waiving the defense for which it bore the burden of proof—so there was no record of evidence to support the appellate court's assumption.[107] Clearly, the Sealys could have raised the defense because, unlike the situation in *Barnes*, the PIP franchise agreement gave them an exclusive territory.[108] A fully litigated mitigation defense presumably could have explored how long it generally took PIP to install a new franchisee; whether that would have taken longer in this case because, for example, the Sealys remained in competition in the market (because California does not enforce post-termination non-compete clauses); and also, as the *McAlpine* court considered, how long it would have taken a new franchisee to begin paying PIP the same level of royalties that it enjoyed before the Sealys' termination. This type of analysis would have kept PIP from recovering avoidable losses and thus would have ensured no double recovery of the type that the *Sealy* court assumed.[109]

Armed with such a record, the court would have been able to evaluate more intelligently, and consistently with traditional contract principles, whether the damages awarded to PIP were, in fact, reasonable or contrary to the principles of the statute on which the court relied. The irony is that the Sealys were, in practical reality, rewarded by waiving such a defense because this made PIP's damages larger than they otherwise might have been and positioned the Sealys to argue that they were excessive. That seems an unjust application of a statute intended to serve justice.[110]

Conclusion

In conclusion, we suggest *Radisson* points toward a more consistent approach to these issues based on traditional contract principles. A franchisor that terminates a franchisee for its breach may recover lost future profits, including lost royalties if, at the time of contracting, it might reasonably have been foreseen by the parties that loss of such profits would be the probable result of the franchisee's breach. A franchisor may not, however, recover future losses that a franchisee proves could have been mitigated by installing a replacement franchisee, or otherwise could have been avoided, as stated by the Restatement, without "undue risk, burden or humiliation." A franchise agreement need not be expressly exclusive for there to be an opportunity to avoid lost future profits through mitigation. Of course, all other traditional contract doctrines, such as certainty of damages, apply.

In addition, though objective foreseeability is not dependent on the parties' intentions at the time of contracting, we also

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suggest the admittedly unremarkable proposition—as illustrated clearly by *Radisson*, the other liquidated damages cases, and some other decisions in this area—that drafting express and clear statements of the parties' expectations in the franchise agreement will increase the likelihood of recovering lost future profits. Franchisors that seek such remedies yet nonetheless persist, for whatever reason, in relying upon ambiguous language as to the remedy they want reduce the likelihood of achieving their goals.

There are some ways in which clarity in drafting can be achieved. One, of course, is to be specific about the remedy. An obvious example is a liquidated damages provision as in *Radisson*. Another idea, illustrated by the recent *Lady of America* decision, is to make termination mandatory if a franchisee fails to pay its royalties, thus perhaps "vitiat[ing] the effect" of the *Sealy/Barnes/Hinton* proximate causation rule.[111] This, however, may have the ironic result of reducing the flexibility franchisors generally want to have in working with their franchisees to avoid termination until, as *Coughlin* and *Sackett* illustrate, the franchisor can no longer tolerate the franchisees paying at their convenience.

Another form of specificity is simply to draft, with greater clarity than the "benefit of the bargain" language from *Sealy* that *Radisson* found to be "vague,"[112] language stating expressly that the franchisor is entitled to lost future profits including royalties in the event the franchisor elects to terminate for a franchisee's breach.[113] As the court held in *Lady of America*, this at least eliminates argument as to whether future royalties were within the reasonable contemplation of the parties.

Finally, still another, though more subtle, area for potential drafting is to clarify, as illustrated by *Mid-America*,[114] that the franchisee is obligated to operate for the entire term, and failure to do so for any reason, including the franchisor's termination for the franchisee's breach, is a default.

We hope that the law will move toward a more consistent approach to the issue of future royalties, as outlined in this article. In the meantime, careful drafting may reduce some of the uncertainties that presently exist in this controversial area of the law.

Endnotes

1. 43 Cal. App. 4th 1704 (1996).

2. 203 F. Supp. 2d 1357 (S.D. Fla. 2002).

3. Damages for lost future profits may, of course, be denied to a franchisor for other reasons, too. One example is where the damages sought are too speculative. *See, e.g.*, ATC Healthcare Servs., Inc. v. Personnel Solutions, Inc., 2006 WL 3758618, at *12 (E.D.N.Y. Dec. 19, 2006) (unpublished) (adopting recommendations of magistrate judge); I Can't Believe It's Yogurt v. Gunn, No. 94-OK-2109-TL, 1997 U.S. Dist. LEXIS 14480 (D. Colo. Apr. 15, 1997) (unpublished); *In re* Mid-Am. Corp., 159 B.R. 48, 55 (M.D. Fla. 1993) (discussed in text below); *see also* Healy v. Carlson Travel Network Assocs., Inc., 227 F. Supp. 2d 1080, 1089 (D. Minn. 2002) (franchisor cannot reasonably establish lost profits where it is "uncontested" that franchisee's business was a failure).

4. 2007 WL 1321967 (C.D. Cal. Jan. 25, 2007).

5. The rule is named for the *Sealy* and *Hinton* cases and for *Burger King Corp. v. Barnes*, 1 F. Supp. 2d 1367 (S.D. Fla. 1998), discussed in text below, holding that mitigation is not required when a franchisor terminates a non-exclusive contract.

6. 461 F. Supp. 1232 (E.D. Mich. 1978).

7. As is common, the franchisor brought other claims, too, e.g., trademark infringement and misappropriation of the merchandising system. *Id.* at 1238. For a discussion of the many types of post-termination remedies a franchisor can seek, *see generally* Ted P. Pierce et al., *The Enforcement of Post-Termination Remedies in the Franchise Contract*, 24 Okla. City U. L. Rev. 81 (1999).

8. *McAlpine*, 461 F. Supp. at 1238.

9. *Id.* at 1238–39.

10. *Id.* at 1274.

11. *McAlpine* was followed by two decisions that franchisees commonly cite, but they add little to meaningful analysis: *In re* Arthur Treacher's Franchisee Litig., 689 F.2d 1137 (3d Cir. 1982); Brennan v. Carvel Corp., Bus. Franchise Guide (CCH) ¶ 9,446 (D. Mass. 1989). The *Sealy* court, discussed below, cited both decisions as expressing reluctance to award future royalties to franchisors once their franchisees lost the trademark and other benefits to which they had been entitled. Postal Instant Press, Inc. v. Sealy, 43 Cal. App. 4th 1704, 1713 n.4 (1996). In *Arthur Treacher's*, a lower court preliminarily enjoined identification with the franchise system unless the franchisee continued to pay the required future royalties as they came due, a condition and remedy the franchisor had not sought. While appealing this injunction, the franchisee elected to disassociate. The appellate court held that "[s]ince [the franchisee] is no longer an Arthur Treacher's franchisee using Arthur Treacher's trademarks, it should no longer be required to pay royalties." *Arthur Treacher's*, 689 F.2d 1137 at 1143. This decision does not, we submit, stand for the "reluctance" noted by the *Sealy* court.

Sealy also quoted *Brennan*'s statement that "[w]hen [the franchisee] ceased to be a Carvel franchisee and stopped using Carvel trademarks, they were no longer required to pay royalties to Carvel Corporation [full cite to *Arthur Treacher's* omitted]." But, as *Sealy* conceded at least, *Brennan* "differ[ed]" because the franchisor there had breached, excusing, to an extent, any further performance by the franchisee. *Sealy*, 43 Cal. App. at 1713 n.4. Thus, the "reluctance" statement is dictum at most and not supported by the citation to *Arthur Treacher's*.

See also from this time period Sparks Tune-Up Ctrs. v. Addison, Bus. Franchise Guide (CCH) ¶ 9,439, at 20,286 (E.D. Pa. 1989) (franchisee whose termination was effected pursuant to consent decree for failing to pay royalties and advertising contributions was obligated to pay future royalty fees).

12. 159 B.R. 48 (M.D. Fla. 1993).

13. 138 Cal. App. 1 (1931).

14. Bus. Franchise Guide (CCH) ¶ 10,534 (Bankr. W.D.N.C. Sept. 2, 1994).

15. *Id.* at 26,077.

16. *Id.* at 26,078.

17. Postal Instant Press v. Sealy, 43 Cal. App. 4th 1704 (1996).

18. *Id.* at 1711.

19. *Id.* at 1712.

20. Restatement (Second) of Contracts § 351(3) (1981).

21. *Sealy*, 43 Cal. App. 4th at 1714 n.5.

22. *Id.* at 1715–16.

23. *Id.* at 1715–18.

24. 138 Cal. App. 1 (1931).

25. *Sealy*, 43 Cal. App. 4th at 1711–12.

26. *Id.* at 1718.

27. *See, e.g.*, Mary deLeo, Case Note, *Emasculating Goliath: Did* Postal Instant Press v. Sealy *Strike an Unfair Blow at Franchising Industry?*, 25 W.

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ST. U. L. REV. 117 (1997); Pierce, *supra* note 7, at 105–08; Rupert Barkoff, *Recent Precedents Say Recoveries for Lost Future Royalties Aren't Likely*, FRANCHISE TIMES, May 2003 (*Sealy* was an "out of mainstream" "anomaly" providing motivation for franchisors to try to manipulate the facts so that the franchisee terminates first or, at a minimum, the franchisor can claim constructive termination); Lane Fisher, *Hinted By* Hinton*: Court Clarifies When Lost Future Royalties Are Recoverable Under California Law*, 7 FRANCHISE L. 1 (2003) (suggesting result of "PIP-like analysis" in *Hinton*, discussed below, is that franchisee that breaches and continues to use franchisor's marks without paying royalties is in better position to defeat claim for lost future royalties than one that abandons the marks altogether); Wiley, Rein & Fielding, *New Hope for Recovering Lost Future Royalties in California*, FRANCHISE ALERT, Sept. 12, 2003 (referring to "infamous" *Sealy* ruling); *see also* Piper Rudnick LLP, *California and Michigan Courts Examine Recovery of Lost Future Royalty Damages*, FRANCAST, Feb. 6, 2004.

28. *See also* Lady of Am. Franchise Corp. v. Arcese, No. 05-61306, 2006 U.S. Dist. LEXIS 68415, at *17–18 (S.D. Fla. May 25, 2006) (counsel for franchisee in *Barnes* successful in arguing as counsel for franchisor that franchisee that gave notice of intent to close franchise was within *Barnes* rule and obligated to pay lost future royalties); Oil Express Nat'l, Inc. v. D'Alessandro, No. 96 C 1528, 1997 WL 723027, at *4 (N.D. Ill. Sept. 4, 1997) (unpublished) (fact issue to be decided as to whether franchisee anticipatorily repudiated, as alleged); Shoney's, Inc. v. Morris, 100 F. Supp. 2d 769, 771 (M.D. Tenn. 1999) (closed six restaurants midway through twenty-year term; contract expressly required that if franchisee ceased operating, franchisee had to pay franchisor damages for the right to receive royalty fees for each year remaining on original term of agreement); It's Just Lunch Franchise, LLC v. BLFA Enters., LLC, Bus. Franchise Guide (CCH) ¶ 12,620, at 36,920 (S.D. Cal. July 21, 2003) (accepting allegations in franchisor's complaint for purposes of motion challenging the pleadings, suggesting in dictum discomfort with *Sealy* rule); United Consumers Club, Inc. v. Bledsoe, 441 F. Supp. 2d 967, 987 (N.D. Ind. 2006) (distinguishing *Sealy* as "totally inapposite" in denying franchisees' motion for summary judgment on franchisor's breach of contract claim because the franchisees allegedly closed instead of merely failing to pay debts); Remedytemp v. Taylor, No. 96-6778, 1998 WL 111806, at *2 (E.D. Pa. Feb. 5, 1998) (unpublished) (distinguished *Sealy* in applying California law because each side claimed at pleadings stage that the other breached and terminated). *See generally* Robert M. Einhorn, *Burger King Corporation v. Hinton, Inc.: Are Lost Future Profits Disappearing?*, 22 FRANCHISE L. J. 159, 166 (2003); Howard Wolfson, *Court Allows Recovery for Lost Future Royalties*, 4 LEADER'S FRANCHISING BUS. & L. ALERT 10 (July 1998) (allowing franchisees to abandon, particularly when they remain in business under a new name, signals to other franchises that this is permissible, potentially causing damage to the system if repeated by others).

29. 1 F. Supp. 2d 1367 (S.D. Fla. 1998). The *Sealy* opinion does not disagree with the rule that damages are recoverable when the franchisee terminates, repudiates, or abandons, and the circumstances of *Sealy* suggest, remarkably, that the appellate court apparently made an error and the case should have been decided on this basis, i.e., on grounds that the Sealys in fact repudiated. PIP complained about the error in its Petition for Review to the California Supreme Court, which was denied. Postal Instant Press v. Sealy, 1996 Cal. LEXIS 4008 (Cal. July 24, 1996). It was also mentioned by deLeo, *supra* note 27, which we have confirmed through our own research of the *Sealy* lower and appellate court files.

Sealy said in a footnote that the court did not have to consider whether a different result would have been reached if the franchisee, rather than the franchisor PIP, had unilaterally canceled or repudiated the agreement. *Sealy*, 43 Cal. App. 4th at 1710 n.2. The *Sealy* opinion justified not reaching this issue by also stating expressly that "[t]he trial court's statement of decision does not include a finding of a contract repudiation[.] Indeed the statement of decision does not even contain the term 'repudiation.'" *Id*. That statement is not correct. The lower court in *Sealy* issued a Minute Order and Memorandum of Tentative Decision after trial stating the following: "PIP's and Defendant's evidence established that without legal excuse Defendants failed to make the monetary contributions legally required of Defendants under the Franchise Agreement and repudiated the agreement." Postal Instant Press v. Sealy, Bus. Franchise Guide (CCH) ¶ 10,427, at 25,474 (Cal. Super. Ct. Sept. 15, 1993). Thus, the trial court did find that the Sealys repudiated, so it would seem that *Sealy* was decided wrongly considering the precedential rule that a franchisor may collect damages where the franchisee terminates the relationship.

30. *Barnes*, 1 F. Supp. 2d at 1372.

31. 203 F. Supp. 2d 1357 (S.D. Fla. 2002).

32. Barkoff, *supra* note 27.

33. *See also* ATC Healthcare Servs., Inc. v. Personnel Solutions, Inc., 2006 WL 3758618, at *11 (E.D.N.Y. Dec. 19, 2006) (unpublished) (denying future lost profits to franchisor that terminated for franchisee's breaches, including misuse of payment program and failure to pay amounts owed, because franchisor chose to terminate in lieu of remedying situation in an alternative manner; "persuaded by the reasoning" in *Sealy*); I Can't Believe It's Yogurt v. Gunn, No. 94-OK-2109-TL, 1997 U.S. Dist. LEXIS 14480, at *63–65 (D. Colo. Apr. 15, 1997) (unpublished) (expressly following *Sealy* in reliance on *Fageol* where franchisor terminated franchisee chronically late in paying fees); Kissinger, Inc. v. Singh, 304 F. Supp. 2d 944, 949–51 (W.D. Mich. 2003) (applying Michigan law, denied franchisor lost future profits in reliance on *Sealy* and *Hinton*, where only sustainable ground for termination was failure to pay fees); Dunkin' Donuts, Inc. v. Arkay Donuts, LLC, No. 05-387, 2006 WL 2417241, at *5 (D.N.J. Aug. 21, 2006) (unpublished) (no lost profits despite franchisee's failure to make any payments over many months or permit audit).

34. Bus. Franchise Guide (CCH) ¶ 12,616 (6th Cir. 2003).

35. *See also* Maaco Enters., Inc. v. Cintron, Inc., Bus. Franchise Guide (CCH) ¶ 11,863 (E.D. Pa. May 17, 2000) (awarding thirteen years of future profits and enforcing a non-compete clause where contract expressly required franchisee to operate the franchise for the entire term); Maaco Enters., Inc. v. Bremner, Bus. Franchise Guide (CCH) ¶ 11,498, at 31,182 (E.D. Pa. Sept. 29, 1998) (unpublished) (franchisee would get benefit if it did not have to pay future royalties); Maaco Enters., Inc. v. Waters, 2000 U.S. Dist. LEXIS 10293 (E.D. Pa. July 2, 2000) (same). *See also* McGann v. United Safari, 694 S.W. 2d 332, 336 (Tenn. Ct. App. 1985). In *McGann*, the only liquidated damages case outside the hotel industry, the court reversed a lower court's decision that the franchisor breached (by allegedly encroaching and not maintaining system quality at the other outlet), holding instead that the franchisee had been unjustified in refusing to pay royalties and thus had breached and was liable for liquidated damages of the highest yearly amount of all fees paid times the number of years remaining on the agreement (i.e., approximately $100,000 per year for six years). For further explanation of the later two *Maaco* decisions, *see* an article written by one of the counsel, Joseph Schumacher & Kimberly Toomey, *Recovering Lost Future Royalties in a Franchise Termination Case*, 20 FRANCHISE L. J. 116, 120 (2001).

36. *See, e.g.*, Ramada Worldwide, Inc. v. Homewood Hotel, Bus. Franchise Guide (CCH) ¶ 13,545 (N.D. Ill. Feb. 5, 2007) (enforcing $150,000 liquidated damages provision where franchisor terminated for franchisee's failure to pay royalty fees and provide monthly reports); Villager Franchise Sys., Inc. v. Dhami, Dhami & Virk, No. CVF046393, 2006 WL 224425, at *10 (E.D. Cal. Jan. 26, 2006) (unpublished) (enforcing $100,000 liquidated damages provision where franchisor terminated after franchisee failed to pay fees,

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maintain financial records, operate hotel according to franchisor's standards, report revenues, etc.).

37. Choice Hotels Int'l, Inc. v. Okeechobee Motel Joint Venture, No. AW-95-2862, 1998 U.S. Dist. LEXIS 23570, at *18–19 (D. Md. Mar. 1, 1998) (unpublished) (rejecting franchisee's counterclaims for fraud and a variety of breaches and permitting franchisor to recover lost future profits after termination over failed quality inspections); *see also* Holiday Hospitality Franchising, Inc. v. H-5 Inc., 165 F. Supp. 2d 937, 941 (D. Minn. 2001) (holding liquidated damages provision unenforceable under Minnesota franchise statute, but permitting franchisor to seek lost future royalties under standard contract damage principles; no mention of *Sealy*); Villager Franchise Sys., Inc. v. Thakore, No. IP 00-1946-C H/F, 2002 WL 1800205, at *2–3 (S.D. Ind. July 2, 2002) (unpublished) (franchisor must mitigate future lost profits under contract expressly obligating franchisee to pay all amounts that would otherwise be payable during the remaining, unexpired term, where franchisor terminated franchisee that did not maintain hotel system operating standards and failed to make timely payments).

38. *See, e.g.*, Ramada Franchise Sys., Inc. v. Motor Inn Inv. Corp., 755 F. Supp. 1570, 1579 (S.D. Ga. 1991) (upholding as reasonable provision liquidating damages at two years, the average time it took franchisor to replace terminated franchisee, where franchisee allegedly terminated prematurely by failing to continue operations); Ramada Inns, Inc. v. Gadsden Motel Co., 804 F.2d 1562, 1566 (11th Cir. 1986) (franchisor terminated for franchisee's failure to meet operational standards and failure to pay past due license fees; two-year liquidated damage provision enforced); *cf.* Howard Johnson Int'l Inc. v. HBS Family, Inc., No. 96 CIV. 7687, 1998 WL 411334, at *6–7 (S.D.N.Y July 22, 1998) (unpublished) (expressing willingness to enforce liquidated damages clause limited to two years of future profits, but refusing to enforce as unreasonable provision fixing minimum payment based on $2,000 for every room in hotel); *but cf.* Travelodge Hotels, Inc. v. Elkins Motel Assocs., Inc., No. 03-799, 2005 U.S. Dist LEXIS 24534, at *31–33 (D.N.J. Oct. 18, 2005) (unpublished) (enforcing mutually negotiated provision liquidating damages per formula multiplying $1,000 by number of hotel rooms).

39. *See, e.g.*, Travelodge Hotels, Inc. v. Kim Shin Hospitality, Inc., 27 F. Supp. 2d 1377, 1382–83 (M.D. Fla. 1998) (enforcing a liquidated damages provision over the eighteen-year unexpired term of the agreement); *see also Homewood Hotel*, Bus. Franchise Guide (CCH) ¶ 13,545 (fixed sum liquidated damages over remaining eleven-year term); *Elkins Motel*, 2005 U.S. Dist. LEXIS 24534, at *31–33 (unpublished) (enforcing mutually negotiated provision liquidating damages per formula multiplying $1,000 by number of hotel rooms). *Cf. McGann*, 694 S.W. 2d at 336–37 (enforcing liquidated damages provision outside the hotel industry for remaining term of the agreement).

40. *See Villager Franchise Sys.*, 2006 WL 224425 at *3 (unpublished).

41. Postal Instant Press, Inc. v. Sealy, 43 Cal. App. 4th 1704, 1711 (1996).

42. This is not the only hotel case giving the franchisor the election to terminate and obtain liquidated damages when the franchisee breached. Other examples include *Gadsen Motel*, 804 F.2d at 1565; *Kim Shin Hospitality*, 27 F. Supp. 2d at 1382; *Villager Franchise Sys.*, 2006 WL 224425, at *4; *Homewood Hotel*, Bus. Franchise Guide (CCH) ¶ 13,545.

43. Radisson Hotels Int'l, Inc. v. Majestic Towers, Inc., 2007 WL 1321967, at *8 (C.D. Cal. Jan. 25, 2007).

44. *Id.*

45. *Id.*

46. *Id.*

47. *Id.*

48. The court did not spend any time on *Sealy*'s alternative holding of "excessive" and "unconscionable" damages. In *Radisson*, the parties had mutually negotiated and revised the liquidated damages clause. It was clearly the result of an arm's-length agreement (*id.* at *5-6), though that was not the only factor that *Sealy* considered in holding on that second basis. *See also* Ramada Worldwide, Inc. v. Homewood Hotel, Bus. Franchise Guide (CCH) ¶ 13,545 (N.D. Ill. Feb. 5, 2007).

49. *Radisson*, 2007 WL 1321967, at *10 n.10.

50. *Id.* (quoting U.S. Ecology, Inc. v. State, 129 Cal. App. 4th 887, 909–10 (2005)).

51. Postal Instant Press v. Sealy, 43 Cal. App. 4th 1704, 1709 (1996).

52. 190 Cal. App. 3d 1051 (1987).

53. *U.S. Ecology*, 129 Cal. App. 4th at 909.

54. 9 Exch. 341, (1854) 156 Eng. Rep. 145.

55. *See generally* 1 B.E. WITKIN, *Foreseeability: Rule of* Hadley v. Baxendale, *in* SUMMARY OF CALIFORNIA LAW, CONTRACTS § 871 (10th ed. 2005); Joseph Perillo, *Damages Are Recoverable Only for Injury That There Was Reason to Foresee*, *in* 11 CORBIN ON CONTRACTS, § 56.2 (2005); 24 SAMUEL WILLISTON, *Foreseeability*, *in* A TREATISE ON THE LAW OF CONTRACTS § 64:13 (4th ed. 2002). *See also* RESTATEMENT (SECOND) OF CONTRACTS § 351 (1981), which provides in part: "(1) Damages are not recoverable for loss that the party in breach did not have reason to foresee as a probable result of the breach when the contract was made; (2) Loss may be foreseeable as a probable result of a breach because it follows from the breach: (a) in the ordinary course of events, or (b) as a result of special circumstances, beyond the ordinary course of events, that the party in breach had reason to know."

56. *See* CORBIN, *supra* note 55, § 56.4, at 94 (error to deny damages merely because parties did not in fact contemplate their possibility when they contracted).

57. WITKIN, *supra* note 55, § 871, at 977.

58. WILLISTON, *supra* note 55, § 64:12, at 125; *see also* WITKIN, *supra* note 55, § 871, at 977.

59. CORBIN, *supra* note 55, § 55.7, at 22–23; *see also* Mitchell v. Gonzales, 54 Cal. 3d 1041, 1048 (1991) (quoting Dean Prosser in rejecting five years before *Sealy* the use of a "but for" causation test in tort causes, favoring instead the "substantial factor" test relied on in *Bruckman* and *U.S. Ecology*: "'Proximate cause remains a tangle and a jungle, a palace of mirrors and a maze. . . .' Cases 'indicate that 'proximate cause' . . . is a complex term of highly uncertain meaning under which other rules, doctrines and reasons lie buried. . . .'").

60. U.S. Ecology, Inc. v. State, 129 Cal. App. 4th 887, 909 (2005). Consistent with these principles, the Judicial Council of California Civil Jury Instructions (CACI) Section 350 simply states, without expressly mentioning proximate causation, among other things: "To recover damages for any harm, [name of plaintiff] must prove: 1. That the harm was likely to arise in the ordinary course of events from the breach of the contract; or 2. That when the contract was made, both parties could have reasonably foreseen the harm as the probable result of the breach." (*based in part on* Wallis v. Farmers Group, Inc., 220 Cal. App. 3d 718, 737 (1990), a pre-*Sealy* case).

61. *See* Radisson Hotels Int'l, Inc. v. Majestic Towers, Inc., 2007 WL 1321967, at *10 n.10. (C.D. Cal. Jan. 25, 2007).

62. Postal Instant Press, Inc. v. Sealy, 43 Cal. App. 4th 1704, 1717 (1996).

63. *Radisson*, 2007 WL 1321967, at *10 n.10.

64. Seagren v. Smith, 63 Cal. App. 2d 733, 740–41 (1944).

65. *Sealy*, 43 Cal. App. 4th at 1707.

66. As some respected commentators have written: "At the very heart of most franchising is the licensing of a trademark and a business system for the marketing of products or services. If the franchisor has performed a valid function, it has devised a fairly complete business format . . . All of this is colloquially referred to as the franchisor's 'know how.' It is this knowledge and proven

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experience for which the franchisee is willing to make a capital payment, plus a royalty for usage." BROWN, DADY, HAFF & GARDNER, FRANCHISING, REALITIES AND REMEDIES § 8.03, at 8–9 (2d ed. 2006).

67. 827 F.2d 1542 (Fed. Cir. 1987).

68. *Id.* at 1545.

69. *Id.* at 1546.

70. 58 Cal. App. 4th 273, 287–90 (1997) (*overruled on other grounds by* Cortez v. Purolator Air Filtration Prods. Co., 23 Cal. 4th 163 (2000)).

71. The *Radisson* court suggested a different analogy, one between franchising and tenancy agreements. Radisson Hotels Int'l, Inc. v. Majestic Towers, Inc., 2007 WL 1321967, at *10 n.10. (C.D. Cal. Jan. 25, 2007) (citing City of San Diego v. Rider, 47 Cal. App. 4th 1473, 1502 n.5 (1996)). Under such contracts (which the court acknowledged are controlled by a specific statutory provision), a landlord may terminate for breach and seek lost future rent.

72. Postal Instant Press, Inc. v. Sealy, 43 Cal. App. 1704, 1711, 1714 n.5 (1996).

73. *Id.* at 1709–11.

74. If it were it true that a contractual election to terminate precluded proximate causation, franchisors might be better off under contracts mandating termination for breach. Lady of Am. Franchise Corp. v. Arcese, No. 05-61306, 2006 U.S. Dist. LEXIS 68415 (S.D. Fla. May 25, 2006), is an unusual example of a case involving such a clause. There, the court noted in dicta that the provision vitiated the effect of *Hinton*, suggesting, in other words, that the franchisor might be able to recover future damages had it been the party terminating. *Id.* at *18 n.7. The court, however, did not need to reach the issue since the franchisee terminated, as in *Barnes.*

75. RESTATEMENT (SECOND) OF CONTRACTS § 243(1), § 236 cmt. a (1981). Even where the breach is not so material as to discharge all performance, i.e., where it is only "partial," it gives rise to a claim for damages for total breach if accompanied or followed by a repudiation. *Id.* § 243(2). This confirms the correctness of the holdings discussed earlier that the Sealys' failure to pay and "repudiation" was sufficient to entitle PIP to future lost profits.

76. *Id.* § 243 cmt. a; *see also* 13 WILLISTON, *supra* note 55, § 39:32 (4th ed. 2002); CORBIN, *supra* note 55, § 57.11 (2005) (acknowledging the election that a non-breaching party can have).

77. 341 N.E. 2d 669 (Mass. 1976).

78. *Id.* at 673.

79. RESTATEMENT (SECOND) OF CONTRACTS § 243(4) (1981). Arguably, a "justice" factor might include whether the franchisee is still in business competing against the franchisor that trained it. We note in this regard that California is among those jurisdictions that does not enforce non-compete clauses, Scott v. Snelling & Snelling, Inc., 732 F. Supp. 1034, 1042–43 (N.D. Cal. 1990) (relying on CAL. BUS. & PROF. CODE § 16600), thus giving terminated franchisees there an opportunity to choose to compete directly against their former franchisors.

80. 41 Cal. 2d 587 (1953). See RESTATEMENT (SECOND) OF CONTRACTS § 243 cmt. b (reporter's note) (1981).

81. *Coughlin*, 41 Cal. 2d at 599–600.

82. 248 Cal. App. 2d 220 (1967).

83. *Id.* at 229–32.

84. *Id.* at 236. Other cases illustrating that total breach may be established from a failure to make payment include, e.g., *Firstar Communications of Louisiana, L.L.P. v. Tele-publishing, Inc.*, 798 So. 2d 1032, 1038 (La. Ct. App. 2001) (defendant's failure to pay percentage owed on balance of revenues received was material breach entitling plaintiff to terminate agreement); *Douglas v. Quick*, 5 Conn. Supp. 128 (Conn. Super. Ct. 1937) (if defendant's failure to pay part of consideration due under contract was material, plaintiff had option either to treat contract as still in force and sue for amount past due or treat the contract as broken and elect to sue for damages for the total breach); *SMR Technologies*, *Inc. v. Aircraft Parts International Combs, Inc.*, 141 F. Supp. 2d 923, 932 (W.D. Tenn. 2001) (defendant distributor's failure to pay manufacturer for products purchased was material breach entitling seller to terminate and retain any remedy for breach of the whole contract or any unperformed balance); and *Manganaro Corp. v. Hitt Contracting, Inc.*, 193 F. Supp. 2d 88, 100–01 (D.D.C. 2002) (subcontractor was relieved of further obligations and entitled to suspend performance under contract by general contractor's failure to pay as agreed).

85. One might respond that the *Sealy* court did not regard the franchisee's breach as material. However, it conceded that the parties' agreement expressly provided that the Sealys' breach was "material." Postal Instant Press, Inc. v. Sealy, 43 Cal. App. 4th 1704, 1707 (1996).

86. The *Sealy* court was troubled by the possibility that a franchisor might terminate and seek future damages for a franchisee's failure to timely make its first payment, or for other breaches significantly less egregious than those of the franchisee in the *Sealy* case. *Sealy*, 43 Cal. App. 4th at 1717. It is true that the failure to make a single payment arguably could be more than a "slight, trivial, negligible, or theoretical factor" in a franchisor's decision to terminate and the resulting loss of future profits, and thus satisfy the substantial factor causation test. It seems more arguable whether, at the time of contracting, it is reasonably foreseeable that termination would be the "probable result" of a single missed payment. Also, a franchisee in such a situation might argue, based on mitigation principles discussed in the text below, that the franchisor could reasonably have avoided lost future profits without undue risk or burden by permitting at least some additional opportunity for payment before terminating. Finally, doctrines related to unconscionability and justice might prevent award of future damages for a single missed payment. CAL. CIV. CODE § 3359 ("[W]here an obligation of any kind appears to create a right to unconscionable and grossly oppressive damages, contrary to substantial justice, no more than reasonable damages can be recovered."); *Sealy*, 43 Cal. App. 4th at 1714–15; RESTATEMENT (SECOND) OF CONTRACTS § 351(3) (1981) (suggesting that courts may limit damages for foreseeable loss by excluding recovery for loss of profits if the circumstances of justice so require in order to avoid disproportionate compensation).

87. RESTATEMENT (SECOND) OF CONTRACTS § 350 (1981); WILLISTON, *supra* note 55, § 64:27, at 193; CORBIN, *supra* note 55, § 57.11; WITKIN, *supra* note 55, § 914–15.

88. *See* RESTATEMENT (SECOND) OF CONTRACTS § 350 cmt. d (1981).

89. *Id.* § 347 cmt. f.

90. *Id.* § 350 cmt. e.

91. Rupert Barkoff, *Lost Future Royalties: Take the Money & Run?*, FRANCHISE UPDATE, June 2004 ("Generally, the courts have concluded that there is no duty to mitigate where a franchise contract does not provide for territorial exclusivity.").

92. *Id.* at 3.

93. *Lady of Am. Franchise Corp. v. Arcese*, No. 05-61306-CIV, 2006 U.S. Dist. LEXIS 68415 (S.D. Fla. May 25, 2006), recently relied on *Barnes* to hold that a franchisor had a duty to mitigate its damages where, unlike *Barnes*, the agreement was exclusive. *See also* Villager Franchise Sys., Inc. v. Thakore, No. IP 00-1946-C H/F, 2002 WL 1800205, at *3 (S.D. Ind. July 2, 2002) (requiring consideration of mitigation where the contract gave the franchisee an exclusive territory, but not suggesting the result would have been different without that fact); *cf.* McAlpine v. AAMCO Automatic Transmissions, 461 F. Supp. 1232, 1275 (E.D. Mich. 1978) (applying mitigation principles to franchise agreements apparently without exclusive territories because the franchisor had agreed around the time of the franchisees' departure from the sys-

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tem to a moratorium on expansion in the area for the next three years, so the new franchisees' income stream would not have been generated if the break-away franchisees were still associated with the system); United Consumers Club v. Bledsoe, 441 F. Supp. 2d 967, 987 (N.D. Ind. 2006) (after distinguishing *Sealy* in denying franchisees' motion for summary judgment against franchisor's contract claim for future damages, the court noted without mention of any exclusive territory that franchisees' arguments regarding mitigation presented a question of fact); Ramada Worldwide, Inc. v. Homewood Hotel, Bus. Franchise Guide (CCH) ¶ 13,545 (N.D. Ill. Feb. 5, 2007) (noting in finding fixed-sum liquidated damages provision reasonable that franchisor had been unable to locate another facility in the community); Choice Hotels Int'l, Inc. v. Okeechobee Motel Joint Venture, No. AW-95-2862, 1998 U.S. Dist. LEXIS 23570, at *18 (D. Md. Mar. 1, 1998) (unpublished) (where a franchisor sought lost future profits from a franchisee terminated under a non-exclusive agreement only to the time the franchise re-franchised).

94. 507 So. 2d 713, 715 (Fla. Dist. Ct. App. 1987).

95. 461 So. 2d 1011, 1014 (Fla. Dist. Ct. App. 1984).

96. CALAMARI & PERILLO, THE LAW OF CONTRACTS § 14.16, at 565 (4th ed. 1998).

97. For example, though Calamari says a car dealer's damages from a breaching car buyer should not generally be reduced because the dealer has an unlimited supply of cars, the hornbook also acknowledges that a different result would occur as to a "unique chattel" such as an ocean-going freighter (or, presumably, a special order car); and Calamari does not suggest that such a contract must necessarily have language of exclusivity for this result. Calamari does suggest that non-exclusive construction contracts do not require mitigation (e.g., *Gary Massey*) but concedes that a publisher whose advertiser breached its contract should try to mitigate by securing additional advertisers if the publication has limited space for advertising.

98. WILLISTON, *supra* note 55, § 64.27–.29 (mitigation of damages).

99. It says, "Gains made by the injured party on other transactions after the breach are not to be deducted from damages that are otherwise recoverable, unless such gains could not have been made had there been no breach." CORBIN, *supra* note 55, § 57.13, at 324.

100. In another chapter on a different subject, Corbin says that PIP may have failed to mitigate damages by installing a new franchisee and also says that the facts of *Sealy* do not indicate whether the defendants had an exclusive territorial franchise that could have been franchised to another franchisee. CORBIN, *supra* note 55, § 56.15, at 159 n.17. This is incorrect because the facts do reveal that the Sealys enjoyed an exclusive territory. Postal Instant Press, Inc. v. Sealy, 43 Cal. App. 4th 1704, 1715 (1996). This passing observation is also far from stating a rule of law on non-exclusive contracts of the type held by *Barnes.*

101. Sullivan v. McMillan, 37 Fla. 134, 136–43 (1896) (emphasis added).

102. We are not aware of any decisions outside the franchise context and outside Florida that apply the rule stated in *Barnes.*

103. This statute provides as follows: "Damages must, in all cases, be reasonable, and where an obligation of any kind appears to create a right to unconscionable and grossly oppressive damages, contrary to substantial justice, no more than reasonable damages can be recovered." CAL. CIV. CODE § 3359.

104. This rule provides as follows: "A court may limit damages for foreseeable loss by excluding recovery for loss of profits, by allowing recovery only for loss incurred in reliance, or otherwise if it concludes that in the circumstances justice so requires in order to avoid disproportionate compensation." RESTATEMENT (SECOND) OF CONTRACTS § 351(3) (1981).

105. *Sealy*, 43 Cal. App. 4th at 1715.

106. *Id.* at 1714 n.5.

107. *See, e.g.*, Brandon & Tibbs v. George Kevorkian Accountancy Corp., 226 Cal. App. 3d 442, 460–61 (1990) (citing Vitagraph, Inc v. Liberty Theatres Co., 197 Cal. 694, 699 (1925)); *accord*, Carnation Co. v. Olivet Egg Ranch, 189 Cal. App. 3d 809, 818 (1986); Frederick v. Kirby Tankships, Inc., 205 F.3d 1277, 1286 (11th Cir. 2000) (collecting cases under federal law); *see also* CORBIN, *supra* note 55, § 57.13, at 327 (defendant bears burden of proving possibility of mitigating losses under California law). *See generally* 11 JOSEPH PERILLO, CORBIN ON CONTRACTS § 57.11 (2005) ("The burden of proving that losses could have been avoided by reasonable effort and expense must always be borne by the party who has broken the contract.").

108. *Sealy*, 43 Cal. App. 4th at 1715.

109. For a contrasting example, in *Villager Franchise Systems, Inc. v. Thakore*, 2002 WL 1800205, at *3 (S.D. Ind. July 2, 2002), the court granted the franchisor summary judgment on liability and for past due fee damages but denied summary judgment before trial as to lost future royalties. The court expressed concern that unless the franchisor tried to refranchise in the protected territory, it would be in a better situation than if the breach had not occurred because it would have damages for the remaining franchise agreement period without providing any support to the terminated franchisee's business and would retain the right to establish a new franchise in the same area. *See also* Lady of Am. Franchise Corp. v. Arcese, 2006 U.S. Dist. LEXIS 68415, at *23–24 (S.D. Fla. May 25, 2006) (reaching a similar result).

110. Remarkably, the *Sealy* court actually excused the franchisee from its omission. The court began by suggesting that franchisors like PIP would be motivated not to refranchise before getting a lost future profits award at trial, lest it recover none. Thus, the court reasoned in a classic non sequitur, "it is hardly surprising the Sealys failed to introduce evidence PIP had awarded a competing franchise or was about to or even had done anything suggesting it might be considering that option. Moreover, short of finding and tendering its own competition, the Sealys had no way of mitigating the 'lost future profits' damages they might be inflicting on PIP." *Sealy*, 43 Cal. App. 4th at 1714 n.5. This makes no sense at all. If anyone, it was PIP, not the Sealys, that arguably should have taken reasonable steps to avoid its loss and, absent such efforts, been denied recovery under mitigation principles. WITKIN, *supra* note 55, § 914, at 1012. But that was the franchisee's defense to raise, not PIP's, and the franchisee did not do so. If the damages awarded as a result seemed large, the fault lay with the franchisee. The same is true with respect to whether PIP's damages award was reasonably certain, an argument that the franchisee did not contest at trial, though it could have done so as was done in *McAlpine* and *Mid-Am.*, discussed earlier and as the *Sealy* court's footnote shows it believed the Sealys should have done as well. *Sealy*, 43 Cal. App. 4th at 1714 n.5.

111. *Lady of Am.*, 2006 U.S. Dist. LEXIS 68415, at *18 n.7.

112. Radisson Hotels Int'l, Inc. v. Majestic Towers, Inc., 2007 WL 1321967, at *8 (C.D. Cal. Jan. 25, 2007).

113. *See, e.g., Villager Franchise Sys.*, 2002 WL 1800205, at *2 (in the event of termination, franchisee must pay all amounts otherwise payable during the remaining, unexpired term of agreement); *Lady of Am.*, 2006 U.S. Dist. LEXIS 68415, at *8, 17-20 (upon termination, franchisee must fully prepay agreements to pay moneys over time to the franchisor, including future royalties, a provision ensuring that such damages were within the reasonable contemplation of the parties; also, automatically terminating agreement if franchisee is unable to pay debts when due, perhaps vitiating *Sealy/Hinton* proximate cause rule); Shoney's Inc. v. Morris, 100 F. Supp. 2d 769, 775 (M.D. Tenn. 1999) (franchisee that ceased operating must pay franchisor damages for right to receive royalty fees for years remaining on original term of agreement).

114. *See also* Travelodge Hotels, Inc. v. Kim Shin Hospitality, Inc., 27 F. Supp. 2d 1377 (M.D. Fla. 1998) (provision obligating franchisee to operate hotel for twenty-year term).

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