Problem 6-2

(1) (a) The contract does not give Mr. Fallon any rights in the event his start-up expenditures exceed $80,000. In addition, he would have great difficulty enforcing any oral assurances made by Captain Donut. Paragraph 5 requires Fallon to prepare his property for operation of the franchise and to obtain equipment to prepare donuts. Paragraph 16 contains a merger clause. The contract is between commercial parties, and Fallon has had the benefit of counsel. Thus, Fallon faces the strong possibility that a court would conclude that contract is a complete integration and cannot be supplemented by any term, including the assurance concerning the maximum cost of outfitting the store.

Fallon could attempt to persuade the court that the merger clause should not be decisive and the writing should not be deemed a complete integration, even though he had the assistance of counsel and plenty of opportunity to review the agreement. Even if Fallon somehow convinced the court that the writing is only a partial integration, he would still need to show that the representation concerning the total cost of outfitting the store was a consistent additional term and one that reasonably might have been left out of the writing. In light of the provisions in Paragraph 5, that would be a difficult challenge.

Moreover, it is questionable whether the oral statements constitute promises, or whether they would be viewed as statements of opinion or projections.

(1)(b) This question raises two issues under paragraph 9 of the agreement. If Mr. Fallon's wife opens a restaurant, is Mr. Fallon "indirectly . . . associated with" it? Is a restaurant a "food shop"? These two questions involve problems of ambiguity. A number of arguments could be made. Fallon could argue that the maxim of contra proferentem should be used to revolve ambiguity against the franchisor, the drafting party. Fallon could also argue that the "indirect ownership" notion is probably best understood as restricting him from investing in a corporation that would operate a competing donut or pastry shop rather than attempting to restrict his wife's ability to open a restaurant. With regard to the term, "foodshop," there is a maxim of interpretation that suggest a general term should be interpreted in light of any specific examples given with it. See the commentary on page 358. Thus, "foodshop" should be understood to mean pastry shop, donut shop, etc., and not to include a "sit-down" restaurant that might serve seafood, Italian food, steaks, etc.

In response, Captain Donut could argue plain meaning for both the "indirect ownership or interest" and "foodshop" terms. Fallon's wife owning a restaurant would plausibly fall within the plain meaning of both terms, and Fallon had full notice of this provision when he entered into the contract. Captain Donut could also argue that Paragraph 14 of the agreement bears on this problem. Paragraph 14, entitled "Transfer of Rights," defines the word "Franchisee" to include "heirs" of the franchisee. Captain Donut could argue that Mr. Fallon's wife is covered by the noncompetition clause by virtue of the definition of paragraph 14.

(1)(c) Nothing in the agreement seems explicitly to prevent Mr. Fallon from selling donuts at wholesale to hotels. Paragraph 8, dealing with the weekly franchise fee, if read literally, only

applies to sales "in the Shop." Is a sale to a hotel restaurant off the premises a sale "in" the shop? Fallon could make several arguments in favor of his claim that such sales are not subject to the fee. First, he is not trading on the Captain Donut name because sales are made without label or reference to Captain Donut. Second, Captain Donut is being paid for the mix that is used, so no unfair advantage is being taken of it. Finally, the maxim of contra proferentem should be used to construe the agreement against Captain Donut.

Captain Donut could make several arguments in response. First, if the hotels contact Fallon at the shop, the sales are effectively being made "in" the shop. Second, the clear intent of the agreement is that Captain Donut should exercise control over Fallon's sale of donuts. Paragraph 5 requires all donuts to be made from Captain Donut's secret mix. The paragraph also requires Fallon to perform to the satisfaction of Captain Donut. Paragraph 9 requires the Franchisor to devote "substantially its full time to the operation of the Shop" and includes a noncompetition clause. Finally, for Fallon to try to have a donut business on the side, using Captain Donut's secret formula, without paying a royalty fee, is bad faith. The doctrine of good faith should be used to carry out the intention of the parties and protect the spirit of the agreement.

(2) Many issues could be raised. The following list is illustrative but almost certainly not exhaustive.

Mr. Fallon's decision to acquire the franchise has been based on assurances from the company. Perhaps he should be advised to ask for a list of names of franchisees whom he can contact to discuss their experiences, in particular the profitability of their operations.

Paragraph 2 provides a 10-year term with renewal based on mutual agreement. Such a provision may well be an unenforceable agreement to agree.

Paragraph 3 provides an exclusive license for five miles. Is this too close? What about a clause giving Fallon a right of first refusal for any new shops within a certain distance?

Paragraph 5 provides for Fallon to operate the business to the satisfaction of Captain Donut. To protect Fallon, the word "reasonable" could be inserted to apply a more objective standard and to avoid a court applying only a subjective test of good faith.

Paragraph 6 requires Fallon to purchase donut mix from Captain Donut at prices to be set by Captain Donut. This sort of open price term is allowed by the UCC §2-305 with the seller's discretion limited by the standard of good faith. Fallon might want to ask for more assurance that the prices will be raised in excessive manner. See Note 4 on page 461.

Paragraph 7. Fallon may not want to agree that the initial fee should be "nonrefundable" without any qualifying language. Otherwise it could be argued that even if there is a termination without any fault on his part (or even with fault on the part of Captain Donut) the fee would still not be refundable.

Paragraph 9. Is the noncompetition clause too broad? Should Fallon be prohibited from owning

a convenience market? If Mr. Fallon's wife is contemplating some type of food business, the application of this paragraph may need to be clarified.

Paragraph 11. Should Fallon have a right of termination in the event the business is not as successful as he hopes or in the event of illness or other problems?

Paragraph 14. Insert language providing that consent to assignment should not be unreasonably withheld.