Cycle City, Ltd. v. Harley-Davidson Motor Company: Can Statutory Law or the Implied Covenant of Good Faith and Fair Dealing Override Express Provisions of Contract?

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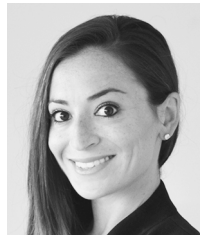

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When entering into a franchise relationship, the parties strive to put all material terms of their agreement in a writing, delineating their respective rights and obligations. However, it is virtually impossible for these types of business contracts to predict every single transaction and situation that could possibly occur over the course of their relationship, which often spans years, if not decades. As such, when a dispute does arise, parties, practitioners, and courts alike are left with the difficult task of interpreting the franchise agreement at issue.

Usually, it is clear that the franchisee has agreed to abide by a specific set of requirements and standards imposed by the franchisor in consideration for the right to use the franchisor's business model and marks. However, franchise agreements often contain provisions allowing the franchisor "discretion" to act a certain way, make certain decisions, or determine whether it will perform certain duties. When the relationship sours, franchisors, which desire strict and consistent interpretation of their franchise agreements, often use such provisions as a shield from contract breach claims for taking action that the contract does not expressly prohibit or for failing to perform discretionary or implied duties. Franchisees, which have traditionally been in a position of unequal bargaining power, are more interested in the historical, long-term, and practical aspects of the relationship. Many states have also enacted franchise relationship statutes in an attempt to regulate and define the franchise relationship and impose statutory duties and rights that may not be specifically delineated in the parties' contract.

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Consequently, suits brought by franchisees against franchisors will often contain claims of breach of the "implied covenant of good faith and fair dealing" in an effort to convince a court to interpret the franchise agreement in conjunction with common law principles and applicable statutory law. Unfortunately, there are no clear guidelines or rules that courts apply uniformly and, as a result, there is little predictability in these types of suits. Although most courts hold that the covenant of good faith and fair dealing may not serve as an independent cause of action for breach of the franchise agreement and cannot impose additional obligations that are inconsistent with or not contained in the franchise agreement,[1] one recent judicial decision has articulated how franchisees can potentially bring successful claims against franchisors based on applicable statutory law or the implied covenant of good faith and fair dealing.

Cycle City, Ltd. v. Harley-Davidson involved a forty-eight-year-long distributorship with Harley-Davidson, which was alleged to have failed to renew the parties' agreement consistent with the parties' historical relationship and to have imposed arbitrary increased prices on its exclusive distributor in Hawaii.[2] The complaint alleged claims of violations of the Hawaii Motor Vehicle Industry Licensing Act and breach of contract based on the implied covenant of good faith and fair dealing.[3] Harley-Davidson moved to transfer the suit and dismiss the complaint, citing to the distributorship agreement's forum selection clause and its express language providing for automatic termination and unilateral price changes.[4] The court denied the request to transfer and refused to find that Harley-Davidson could not be liable as a matter of law for failing to renew or for imposing increased prices on its distributor.[5] Notably, the decision serves as a reminder that the franchise relationship involves a unique blend of contractual, equitable, statutory, and common sense principles. As courts continue to recognize and comprehend the uniqueness that is a franchise, the law too continues to develop in order to remedy and resolve the disputes that arise in these distinctive business relationships.

1. *See* Burger King v. Weaver, 169 F.3d 1310, 1318 (Fla. 1999) (refusing to recognize an independent cause of action for breach of the implied covenant in contravention of the parties' contract where franchisee could not establish a breach of express provision of the contract); Cutrone v. Daimler-Chrysler Motors Co., LLC, 160 F. App'x 215, 219 (3d Cir. 2005) ("a duty of good faith arises only in connection with specific contractual obligation").

2. Order Denying Defendant Harley-Davidson Motor Company Inc.'s Motion to Transfer Case, Granting in Part and Denying in part Defendant Harley-Davidson Motor Company Inc.'s Motion to Dismiss, and Granting Plaintiff Cycle City, Ltd.'s Request for Leave to Amend (Order), Cycle City, Ltd. v. Harley-Davidson Motor Co., CV. No. 14-00148 HG-RLP, Doc. No. 48 (D. Haw. Oct. 17, 2014).

3. *Id.* at 1.

4. *See* Motion to Dismiss, *Cycle City*, Doc. No. 21 (D. Haw. June 4, 2014).

5. *See* Order, *supra* note 2, at 38–42.

I. Overview of the Implied Covenant of Good Faith and Fair Dealing

The implied covenant of good faith and fair dealing is generally recognized at common law in almost all jurisdictions.[6] Accordingly, states will imply in a contract an obligation to deal honestly and in good faith in the performance and enforcement of the agreement and not to do anything that will destroy or injure the right of the other party to receive and enjoy the reasonable benefits, or "fruits" of the contract.[7] In franchising, the implied covenant is invoked in a multitude of situations, including, but not limited to, encroachment,[8] transfers,[9] use of advertising funds,[10] and issues relating to termination and renewal.[11]

Although the implied covenant of good faith and fair dealing is widely accepted as a principle of law, courts still grapple with how to apply it. The majority rule is that the covenant of good faith and fair dealing may not serve as an independent cause of action for a breach of the franchise agreement and cannot override express contractual terms.[12] However, the

6. *See, e.g.* Wood v. New Jersey Mfrs. Ins. Co., 21 A.3d 1131, 1140 (N.J. 2011) ("We recently re-emphasized that 'every contract in New Jersey contains an implied covenant of good faith and fair dealing, [t]hat is, neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract[.]'"); *In re* Hennepin Cnty. 1986 Recycling Bond Litig., 540 N.W.2d 494, 502 (Minn. 1995) ("Under Minnesota law, every contract includes an implied covenant of good faith and fair dealing requiring that one party not 'unjustifiably hinder' the other party's performance of the contract."); Scheck v. Burger King Corp., 798 F. Supp. 692 (S.D. Fla. 1992) ("Florida contract law recognizes the implied covenant of good faith and fair dealing in every contract."). *But see* Barrand, Inc. v. Whataburger, Inc., 214 S.W.3d 122, 139 (Tex. App. 2006) (Under Texas law, "[a] common-law duty of good faith and fair dealing does not exist in all contractual relationships," but arises when a "special relationship" exists.) (citation omitted).

7. AAMCO Transmissions, Inc. v. Harris, 759 F. Supp. 1141, 1148 (E.D. Pa. 1991).

8. *See* Scheck v. Burger King, 756 F. Supp. 543 (S.D. Fla. 1991) (where franchise agreement expressly denied territorial exclusivity to franchisee, franchisee is still entitled to expect that franchisor will not act to destroy the fruits of the contract by placing a competing restaurant two miles away).

9. *See* Dunkin' Donuts Inc. v. Taseski, 47 F. Supp. 2d 867, 876 (E.D. Mich. 1999) (franchisee alleged breach of the implied covenant of good faith and fair dealing based on franchisor's refusal to sanction requested transfer failed absent any behavior evincing "fraud, deceit, or misrepresentation").

10. Burger King Corp. v. Agad, 941 F. Supp. 1217, 1221–22 (N.D. Ga. 1996) (where franchise agreement provided that all advertising expenditures "shall be at the discretion" of franchisor, claim of breach of the implied covenant of good faith and fair dealing based on objectionable use of advertising funds to make charitable donation could not prevail because the court could not "second guess" the franchisor's "legitimate business decisions").

11. McDonald's Corp. v. C.B. Mgmt. Co., 13 F. Supp. 2d 705, 711 (N.D. Ill. 1998) (franchise agreement made clear that franchisor "had the unfettered 'right' to terminate in the event of a material breach, defined to mean, inter alia, the failure to make timely payments of amounts owing under the agreements. This is not, therefore, a situation where the covenant of good faith must be implied to 'fill the gap' in a contract where the terms offer insufficiently clear guides to interpretation".).

12. *See* Copans Motors, Inc. v. Porsche Cars N. Am., Inc., No. 14-60413-CV, 2014 WL 2612308, at *8 (S.D. Fla. June 11, 2014) (in order to have claim of implied covenant of good faith and fair dealing, there must be a breach of an express provision of the contract); Cook v. Little Caesar Enters., Inc., 210 F.3d 653, 657 (6th Cir. 2000) (where franchisor expressly

problem with the majority rule is that it does not give the implied covenant of good faith and fair dealing any real teeth to hold parties to any independent obligations apart from what is expressly contained in the terms of the contract. As a result, franchisees must meet the challenge of pleading and proving separate and distinct facts for their covenant of good faith and breach of franchise agreement claims. This feat can seem daunting where the franchise agreement is silent or drafted to expressly allow the franchisor to engage in the very conduct that is alleged to be unlawful or to unambiguously preclude franchisee rights that are alleged to have been destroyed. For example, franchise agreements often contain provisions giving franchisors unfettered discretion or sole authority to make certain decisions, thereby creating possible contractual defenses to implied covenant claims.[13]

Case law suggests, however, that courts are becoming more willing to apply the implied covenant of good faith and fair dealing as a gap-filler to address ambiguities and uncertainties in the franchise relationship.[14] Pursuant to this approach, a party vested with discretion in a contract may be held liable for breach of contract based on a violation of the implied covenant of good faith and fair dealing if such discretion was not exercised in good faith or otherwise frustrated the parties' contract, notwithstanding the fact that no express term was breached.[15] Specifically, if a party exercises its vested discretion in a way that is arbitrary, capricious, discriminatory, or unreasonable, a court can find a violation of the covenant of good faith and fair dealing.[16] Although the facts of a given case may strongly support a franchisee's claim

reserved the right to grant licenses to others subject only to franchisee's "exclusive" one-mile territory, franchisee "could not employ the implied covenant of good faith and fair dealing to override the express terms of the franchise agreement").

13. *See, e.g.*, De Walshe v. Togo's Eateries, Inc., 567 F. Supp. 2d 1198, 1204 (C.D. Cal. 2008) ("if conduct is permitted under the express terms of a contract it does not violate the covenant of good faith. This rule is of special significance where the terms of the contract vest 'uncontrolled discretion' in one party of the contract because this discretion removes any role for the implied covenant of good faith, making it irrelevant."); *McDonald's Corp.*, 13 F. Supp. 2d at 711.

14. *In re* Magna Cum Latte, Inc., No. 07-31814, 2007 WL 4412143, at *3 (Bankr. S.D. Tex. Dec. 13, 2007) (implied covenant of good faith and fair dealing is not limited to the contract's expressed terms, as it would "imply nothing if it was limited to rights and obligations expressly provided in the contract.").

15. Bike Fashion Corp. v. Kramer, 46 P.3d 431, 435 (Ariz. Ct. App. 2002) ("Arizona law recognizes that a party can breach the implied covenant of good faith and fair dealing both by exercising express discretion in a way inconsistent with a party's reasonable expectations and by acting in ways not expressly excluded by the contract's terms but which nevertheless bear adversely on the party's reasonably expected benefits of the bargain.").

16. For example, in *Carvel Corp. v. Diversified Management Group, Inc.*, the Second Circuit stated as follows in finding that the franchisee presented sufficient evidence to support a claim of breach of the implied duty of good faith:

> The evidence presented by DMG purportedly showing Carvel's bad faith included Carvel's rejection of proposed store locations and franchisees, refusal to allow changes in store blueprints to accommodate Maryland Health Department requirements, and apparently abrupt and unexplained decisions to reverse wholesale sales and advertising policies. While the distributorship agreement gave Carvel considerable discretion with regard to advertising, store location, wholesale sales, and other matters, this did not relieve Carvel of its duty to act in good faith.

of breach of the implied covenant of good faith and fair dealing, such claims can be subject to dismissal because of contradictory or inconsistent provisions in the franchise agreement, negating a franchisee's reasonable expectations.[17] Notwithstanding such express contractual language, *Cycle City* demonstrates that, depending on the circumstances and applicable law, courts may be willing to explore new methods of interpreting and modifying franchise agreements based on the implied duty of good faith and fair dealing.

Although most courts look to contract law in determining issues relating to interpretation of the parties' agreement and relationship, there are often additional applicable sources of law that further muddy the waters. Indeed, many states have enacted statutes that govern franchises, specific industry relationships such as motor vehicle dealerships and distributorships and other business opportunities involving unequal bargaining power.[18] A number of these states, in addition to Puerto Rico and the Virgin Islands, have further enacted legislation that specifically governs the termination and renewal of the business relationship, further adding to the analysis in determining the circumstances under which a sale, termination, or non-renewal may be permitted.[19] These statutory laws impose additional non-uniform requirements of reasonableness and good faith and further expressly prohibit conduct that may not otherwise be prohibited by the parties' contract. In such cases, critical determinations must be made as to what law applies, what was reasonably expected of the parties, and how to reconcile principles of contract interpretation with statutory law. As *Cycle City* demonstrates, the law applied, the relevant forum, and the judge deciding the case will inevitably affect the result of disputes involving breach of contract based on breach of the implied covenant of good faith and fair dealing.

II. *Cycle City v. Harley-Davidson*

A. *Alleged Facts of the Case*

Since 1966, Cycle City had been Harley-Davidson's exclusive distributor for the distribution, sale, and service of Harley-Davidson motorcycles, parts, accessories, and licensed products in Hawaii.[20] Since that time, Harley-Davidson had never sold its products directly to consumers in Hawaii, and

930 F.2d 228, 230–31 (2d Cir. 1991). "'Since the duty of good faith and fair dealing is implied in every contract, contracting parties' fields of discretion under a contract are bounded by the parties' mutual obligation to act in good faith.'" *Id.* (quoting Cross & Cross Props., Ltd. v. Everett Allied Co., 886 F.2d 497, 502 (2d Cir. 1989)).

17. *See, e.g.*, Payne v. McDonald's Corp., 957 F. Supp. 749, 758 (D. Md. 1997).

18. *See, e.g.*, IOWA CODE § 537A.10; CONN. GEN. STAT. ANN. § 42-133v(a); N.Y. ALCOHOLIC BEV. CONTROL LAW § 55-c3.

19. *See e.g.* California Franchise Relations Act, CAL. BUS. & PROF. CODE §§ 20000 through 20043 (requires "good cause" for termination); Connecticut Franchise Law, CONN. GEN. STAT. ANN. §§ 42-133e through 42-133h; Indiana Deceptive Franchises Practices Act, INDIANA CODE §§ 1–7; Michigan Franchise Investment Law, MICHIGAN COMP. LAWS § 445-1527.

20. Order, *supra* note 2, at 3.

Cycle City alone had increased Harley-Davidson's brand awareness in the state for the past forty-eight years.[21] While Cycle City served as exclusive distributor, the parties operated pursuant to several distributorship agreements that renewed automatically.[22] On November 24, 2008, the parties entered into their final exclusive distributorship agreement, which is the subject of Cycle City's pending lawsuit.[23]

During the course of the parties' relationship, Cycle City invested millions of dollars toward the development of the Harley-Davidson brand and goodwill and the development of its dealer network.[24] However, on March 12, 2013, Harley-Davidson notified Cycle City that it would not be renewing the distributorship agreement because it was not "in the brand's long term interest" to continue the exclusive distributorship in Hawaii.[25] Harley-Davidson also advised Cycle City that if it were compelled to enter into a new distributorship agreement, Harley-Davidson would unilaterally require Cycle City to enforce corporate policies and facility standards and would hold it accountable for failing to abide with such standards.[26] However, Harley-Davidson had never before suggested that Cycle City breached the distributorship agreement or that it otherwise failed to represent the brand adequately.[27]

Moreover, as a condition to renewing the distributorship agreement, Harley-Davidson said that it would impose new, additional terms, including: (1) Cycle City would be prohibited from making investments for the representation and support of its dealers; (2) Harley-Davidson would revise its discount structure so as to increase Cycle City's purchasing costs, which would ultimately be passed on to dealers and consumers in Hawaii; (3) Harley-Davidson would prevent Cycle City from accessing U.S. Dealer shipping and freight programs and expenses, which would become Cycle City's responsibility; (4) Harley-Davidson would prevent Cycle City's licensed dealers from accessing Harley-Davidson's digital ordering systems; and (5) Harley-Davidson would cease cost sharing for dealer training and support of shipping motorcycles purchased by Cycle City.[28]

In justifying its refusal to renew the distributorship agreement, Harley-Davidson relied on the following language in the distributorship agreement:

> 15.1 Unless terminated as provided in this [Agreement] or by agreement of the parties, this Agreement shall continue for a term ending on July 31, 2013. *Upon*

21. *Id.*
22. *Id.* at 4.
23. *Id.*
24. *Id.* at 5.
25. *See id.* at 27; Compl. ¶ 17, Cycle City, Ltd. v. Harley-Davidson Motor Co., CV No. 14-00148 HG-RLP, Doc. No. 1 (D. Haw. Mar. 26, 2014).
26. Compl. ¶ 22–23.
27. *Id.* ¶ 20.
28. *Id.* ¶ 22–23.

> *the end of the term, this Agreement shall automatically expire without any notice or prior action* (emphasis added).[29]

Further, Harley-Davidson validated its actions regarding unilateral changes to prices and terms based in part on the distributorship agreement's language regarding prices, discounts, terms, and taxes. Namely, the agreement required Harley-Davidson to notify Cycle City of prices, charges, and terms of purchase and provided that "[s]uch prices, charges and terms shall be [Harley-Davidson's] standard Distributor prices, charges, and terms for the Territory as established by [Harley-Davidson]."[30] Harley-Davidson also reserved the right, at any time and without prior notice, to change prices, discounts, charges and terms of purchase.[31]

When the distributorship agreement expired and Cycle City refused to agree to Harley-Davidson's required terms of renewal, Cycle City sued in the U.S. District Court for the District of Hawaii for violations of the Hawaii Motor Vehicle Industry Licensing Act (HMVILA) based on Harley-Davidson's failure to renew the distributorship agreement and its demand that Cycle City consent to the termination of the distributorship model.[32] Cycle City further sought a declaration of its rights under the distributorship agreement and the HMVILA, as well as damages for Harley-Davidson's breach of the distributorship agreement.[33] The contract claim was based on Harley-Davidson's breach of the implied covenant of good faith and fair dealing in failing to renew and for "maliciously, arbitrarily and capriciously" increasing prices and charges at which Cycle City purchased its products in order to force Cycle City to relinquish its rights under the distributorship agreement and applicable state law.[34]

B. *Harley-Davidson's Motion to Transfer*

Harley-Davidson moved to transfer the case to Wisconsin, relying on the following forum selection and governing law clause in the distributorship agreement:

> This Agreement shall be governed and construed in accordance with the laws of the State of Wisconsin. . . . [the parties] hereby submit to the exclusive jurisdiction of the courts of State of Wisconsin. *Any applicable state motor vehicle statute governing the relationship between [the parties] shall be controlling in the event of a conflict between any provision of this Agreement and the state statute* (emphasis added).[35]

Under Harley-Davidson's interpretation of the forum selection clause, the clause was valid and enforceable under the analysis set forth in *Atlantic*

29. *Id.*, Ex. A at 18.
30. *See* Order, *supra* note 2, at 41.
31. *Id.*
32. *See id.* at 6.
33. *Id.*
34. *Id.* at 38, 41.
35. *Id.* at 10.

Marine Construction Co. v. U.S. District Court for the Western District of Texas,[36] and Hawaii's applicable motor vehicle statute could not be applied retroactively to void the parties' enforceable forum selection clause.[37] In support of its argument, Harley-Davidson relied on prior court rulings involving similar claims, such as *Caribbean Restaurants, LLC v. Burger King Corp.*,[38] where the U.S. District Court for the District of Puerto Rico upheld a forum selection clause despite language in Puerto Rico's Law 75 providing that "any stipulation that obligates a dealer to . . . litigate any controversy . . . regarding his dealer's contract outside of Puerto Rico . . . shall be considered . . . null and void."[39]

However, Cycle City asserted that venue was proper pursuant to the express language of the forum selection clause and Haw. Rev. Stat. § 437.28.5(b), which provides:

> Notwithstanding the terms, provisions, or conditions of any dealer or distributor agreement, franchise, or waiver and notwithstanding any other legal or administrative remedies available, any person who is licensed under this chapter whose business is injured by a violation of section 437-28(a) (21) . . . may bring a civil action in a court of competent jurisdiction in the State to enjoin further violations and to recover any damages together with the costs of the suit. Laws of the State of Hawaii shall apply to any action initiated under this subsection.[40] [41]

Accordingly, under Cycle City's interpretation of the forum selection clause, the proper fora for any disputes arising out of or related to the distributorship agreement were the federal and state courts in Hawaii.[42]

Ultimately, in interpreting the parties' forum selection clause, the court found that certain conflicts existed between the distributorship agreement,

36. 134 S. Ct. 50 (2013).

37. Def. Harley-Davidson Motor Company, Inc.'s Motion to Transfer Case, *Cycle City*, Doc. 28 (July 2, 2014).

38. Civ. No. 14-1200(PG), 2014 U.S. Dist. LEXIS 76352 (D.P.R. June 3, 2014).

39. Motion to Transfer, *supra* note 37, at 6–7.

40. *See* Compl., *supra* note 21, ¶ 5; HAW. REV. STAT. § 437.28.5(b).

41. *See* Compl., *supra* note 21, ¶ 5; HAW. REV. STAT. § 437.28.5(b). Pursuant to Section 437-28(a)(21) of the HMVILA, Cycle City alleged that Harley-Davidson,

> [b]eing a manufacturer or distributor:
> (A) Has required any dealer in the State to enter into any agreement with the manufacturer or distributor or any other party, to perform any act not required by or to refrain from performing any act not contrary to the reasonable requirements of the franchise agreement with the dealer, by threatening to cancel the franchise agreement or by threatening to refuse, at the expiration of the current franchise agreement, to enter into a new franchise agreement with the dealer;
> . . . .
> (C) Has canceled or failed to renew the franchise agreement of any dealer in the State without good faith, as defined herein. As used in this subparagraph, "good faith" means the duty of each party to any franchise agreement to fully comply with that agreement, or to act in a fair and equitable manner towards each other.

HAW. REV. STAT. § 437-28(a)(21)(A), (C).

42. Pl's Mem of L. in Opp. to Def's Mtn. to Transfer Case, *Cycle City*, Doc. 35, at 16–18 (July 25, 2014).

and the HMVILA applied to the parties' relationship. First, Haw. Rev. Stat. § 437.28.5(b) conflicted with the Wisconsin contractual forum, and because of such conflict, venue was proper in the Hawaii district court.[43] Second, the court noted that the distributorship agreement also conflicted with Haw. Rev. Stat. § 437-52(1), which prohibits a manufacturer from requiring any dealer to enter any agreement that requires the law of another state be applied to the dispute or requires that the dealer bring an action in a venue outside of Hawaii.[44] Because of the foregoing conflicts, the court interpreted the parties' forum selection clause to mean that the provisions of the HMVILA controlled and were specifically incorporated into the parties' distribution agreement.[45] Based on such incorporation of statutory law, the forum selection clause pointed to Hawaii as the proper forum, and Cycle City's decision to sue in Hawaii was found to be in accord with the parties' contract.[46] [47]

In reaching its conclusion, the court noted that the decision in *Caribbean Restaurants, LLC* was distinguishable because the forum selection clause at issue in that case "did not contain a sentence similar to the last sentence" in the distributorship agreement between Cycle City and Harley-Davidson.[48] As such, because of the express incorporation of the HMVILA, Cycle City's "decision to file in Hawaii [wa]s in accord with the parties' forum selection clause" and "the factors identified by the Supreme Court in *Atlantic Marine* to determine whether a plaintiff can file in a forum *other* than that chosen by the parties by contract [we]re inapplicable."[49] By finding that Hawaii was the agreed upon forum, the court was able to circumvent the analysis set forth by *Atlantic Marine*.

Notably, however, the court indicated that a forum non conveniens analysis would still yield the same result even if Wisconsin was the agreed upon forum despite its conflict with the HMVILA, as Harley-Davidson contended.[50] Significantly, in construing Harley-Davidson's motion to transfer as a motion to dismiss on forum non conveniens grounds, the court noted

43. Order, *supra* note 2, at 12.

44. *Id.* at 12-13. *See also* HAW. REV. STAT. § 437-52(1).

45. Order, *supra* note 2, at 14.

46. *Id.* at 14. *But see* Caribbean Rests., LLC v. Burger King Corp., No. 12-1200, 2014 U.S. Dist. LEXIS 76352 (D.P.R. June 3, 2014) (where parties' agreement did not contain language specifically incorporating state dealership statute, court enforced forum selection clause despite state dealer/distributor protection statute invalidating such clauses).

47. Harley-Davidson also argued that application of the HMVILA violated the Contract Clause of the United States Constitution, based on the fact that Haw. Rev. Stat. § 437-52(1) was enacted after the parties entered into the distributorship agreement at issue. However, noting that Section 437-28.5(b) existed at the time of the parties' agreement, the court found that Section 437-52(1) did not "substantially impair the parties' contractual relationship." *Id.* at 18.

48. Order, *supra* note 2, at 14.

49. *Id.* at 14–15 (emphasis added). Because the court interpreted the parties' forum selection clause to point to Hawaii as the proper forum, the court did not apply the usual analysis under 28 U.S.C. § 1404(a), which would require an evaluation of the convenience of the parties and public interest considerations. *See* Order, *supra* note 2, at 10 (citing Atl. Mar. Constr. Co. v. U.S. Dist. Court for W. Dist. of Texas, 134 S. Ct. 568 (2013)).

50. *See id.* at 18.

that the following public interest factors "overwhelmingly" weighed against dismissal:

> There was a strong local interest in having the parties' dispute resolved in Hawaii. Cycle City has operated as Harley-Davidson's exclusive distributor in Hawaii for 48 years and the facts giving rise to the lawsuit took place in Hawaii. The HMVILA expresses a strong public policy in favor of resolving these types of disputes in Hawaii and the crux of Cycle City's Complaint is for violation of that law. . . . The Court's familiarity with Hawaii law also weighs in favor of maintaining the action [in Hawaii].[51]

Cycle City demonstrates an example of the type of "exceptional case" the Supreme Court referred to in *Atlantic Marine* where the public interest factors may defeat a party's efforts to transfer a case based on a forum selection clause. While the decision in *Atlantic Marine* will generally make it more difficult to invalidate forum selection clauses, *Cycle City* suggests that state substantive law that otherwise protects franchisees against litigation outside their home state may effectively serve to invalidate forum selection clauses as a matter of public policy.

C. *Harley-Davidson's Motion to Dismiss*

In addition to moving to transfer the case, Harley-Davidson moved for dismissal for failure to state a claim. In support of dismissing Cycle City's claims, Harley-Davidson argued that it could not be held liable as a matter of law for failing to renew the distributor agreement or for increasing prices, either under the HMVILA or the implied covenant of good faith and fair dealing, because the parties' agreement expressly provided for automatic termination and expressly permitted Harley-Davidson to impose increased price terms.[52] Relying on the recent case of *Uyeshiro v. Irongate Azrep BW LLC*,[53] Harley-Davidson asserted that the statute and any implied covenant of good faith and fair dealing could not override the express terms of the contract.[54] In *Uyeshiro*, the plaintiff alleged that the defendant breached the implied covenant of good faith and fair dealing by imposing "oppressive conditions" on third-party rentals and concealing such conditions until after

51. *Id.* at 18–19.

52. *See e.g.* S. Shore Imported Cars, Inc. v. Volkswagen of Am., Inc., Bus. Fran. Guide (CCH) ¶ 14,360 (D. Mass. 2010), *aff'd*, Bus. Fran. Guide (CCH) ¶ 14,635 (1st Cir. 2011) (parties cannot inject terms into the franchisor/franchisee relationship where agreement nor state statute contemplated such terms); Luso Fuel Inc. v. BP Prods. N. Am., Inc., Bus. Fran. Guide (CCH) ¶ 14,166 (D.N.J. 2009) (dismissing franchisee's good faith and fair dealing claim where claim sought to alter the clear terms of the agreements); Berger v. Home Depot U.S.A., Inc., 476 F. Supp. 2d 1174 (C.D. Cal. 2007) (granting motion to dismiss on good faith and fair dealing claim, finding "[i]t is universally recognized the scope of conduct prohibited by the covenant of good faith is circumscribed by the purposes and express terms of the contract," and "under traditional contract principles, the implied covenant of good faith is read into contracts in order to protect the express covenants or promises of the contract, not to protect some general public policy interest not directly tied to the contract's purpose").

53. Civ. No. 13-00043 ACK - MBK, 2014 WL 414219 (D. Haw. Feb. 3, 2014).

54. *See* Order, *supra* note 2, at 41–42.

the contract was executed.[55] However, the *Uyeshiro* court found that the applicable documents made clear that third-party rentals would "be subject to certain requirements" and the defendant, while given discretion, could not be found to have violated its implied duty by acting in a manner consistent with the contract.[56] The *Uyeshiro* court dismissed, noting that dismissal of breach of the covenant of good faith and fair dealing claims is proper where the allegations are inconsistent with the obligations imposed by contract.[57]

1. Violations of the HMVILA

In determining whether Cycle City sufficiently alleged that Harley-Davidson failed to renew the distributorship agreement in good faith, the court looked to Sections 437-28(a)(21)(A) and (C) of the HMVILA, which provide that "a manufacturer, such as Harley-Davidson, cannot attempt to force a dealer to accept certain terms by threatening not to renew the distributorship agreement and cannot fail to renew the distributorship agreement *without good faith*."[58] In interpreting the clear language of the provisions imposing a statutory duty of good faith in decisions not to renew in conjunction with the parties' contract, the court found that, in light of the conflict between the agreement and state law, the statute applied.[59] As a result, the court held that Cycle City sufficiently alleged that "Harley-Davidson threatened to allow the distributorship to expire if Cycle City would not agree to substantial changes to the parties' business relationship."[60] In considering Cycle City's allegations that Harley-Davidson "significantly and unreasonably increased wholesale prices" "in a malicious, capricious, and bad faith effort to financially squeeze Cycle City," forcing it to accept ultimate termination of a business model that had existed for over forty-eight years, the court found that Cycle City sufficiently supported its claim that Harley-Davidson failed to act in a "fair and equitable manner" and failed to renew in good faith in violation of the HMVILA.[61]

55. *Uyeshiro*, 2014 WL 414219, at *12.

56. *Id.* at *13.

57. Uyeshiro v. Irongate Azrep MBW LLC, No. 13-00043 ACK - MBK, 2014 WL 1233109 (D. Haw. Mar. 24, 2014).

58. Order, *supra* note 2, at 25–26 (emphasis added).

59. *See id.* at 35.

60. *Id.* at 28.

61. *Id.* at 29. The court in sum ignored the language in the parties' distributorship agreement providing for "automatic expiration" in its analysis regarding a violation of HMVILA § 437-28(a)(21)(A), (C). Notably, however, the court granted Cycle City leave to amend its complaint to allege violations of Haw. Rev. Stat. §§ 437-52 and 437-58, which prohibit a manufacturer or distributor from cancelling or failing to renew a franchise agreement without providing notice and without good cause and good faith. *Id.* at 38; *see also* HAW. REV. STAT. §§ 437-52, 437-58. In so doing, the court found that a retroactive application of the HMVILA to override the distributorship agreement's provision allowing for automatic termination was not a violation of the Contract Clause and was in accordance with the parties' reasonable expectations. *See* Order, *supra* note 2, at 32–35 (noting that the parties' agreement provides that the HMVILA shall be controlling in the event of a conflict). *But see* LaFontaine Saline, Inc. v. Chrysler Grp., LLC, 852 N.W.2d 78 (Mich.

2. Breach of Distributorship Agreement Under the Implied Covenant of Good Faith and Fair Dealing

In determining whether Cycle City stated a claim for breach of the distributorship agreement for failing to renew based on breach of the implied covenant of good faith and fair dealing, the court noted that because the HMVILA modified the distributorship agreement, such that the HMVILA controls in the event of a conflict, Cycle City was not attempting to create any "new, independent rights or duties beyond those agreed to by the parties."[62] Therefore, *Uyeshiro* did not apply to support dismissal because the allegations were not "inconsistent" with the terms of the distributorship agreement.[63] To the contrary, as contemplated by the parties' contract, Harley-Davidson was required to abide by the HMVILA's specific requirements for non-renewal such that the statutory requirements became terms of the parties' contract.[64] Moreover, Harley-Davidson was prohibited from acting in such a way as to "deprive the other of the benefits of the agreement."[65] As a result, the court held that there were sufficient facts to support Cycle City's claim for breach of contract based on the implied covenant of good faith and fair dealing.[66]

Likewise, Cycle City also alleged that Harley-Davidson breached the implied covenant of good faith and fair dealing by unlawfully and unreasonably increasing prices for its products.[67] In response, Harley-Davidson asserted that, although the distributorship agreement provided that prices, charges, and terms of purchase shall be Harley-Davidson's "standard" distributor prices, Harley-Davidson expressly reserved the right "*at any time and without prior notice, to change prices, discounts, charges and terms of purchase.*"[68] Relying on this language, and consistent with the prevailing view, Harley-Davidson asserted that it could not be held liable for breach of contract based on the increase of prices because the contract expressly permitted it to change the terms without notice at any time.[69] However, in denying dismissal, the court noted that, although the agreement gave Harley-Davidson the right to change prices, "[w]hen an express contract provision allows a party to exercise some discretion, that party is obligated to exercise its discretion in good faith."[70] Because Cycle City alleged that Harley-Davidson exercised its discretion "maliciously, arbitrarily and capriciously" in order to force

2014) (holding that retroactive application of amendment to Michigan Motor Vehicle Act that expanded the relevant market from a six-mile radius to a nine-mile radius would impair vested rights under previously reached dealer agreement, which was expressly subject to the Act's prior version).

62. *See* Order, *supra* note 2, at 39.
63. *Id.*
64. *Id.* at 35.
65. *Id.* at 38 (internal quotation, citation omitted).
66. *Id.* at 39.
67. *Id.* at 41.
68. *Id.* at 41–42.
69. *Id.*
70. *Id.* at 42 (citing Damabeh v. 7-Eleven, Inc., No. 12-CV-1739-LHK, 2013 WL 1915867, at *6 n.4 (N.D. Cal. May 8, 2013)).

Cycle City to relinquish its rights, a claim for breach of contract based on the implied covenant of good faith could withstand dismissal.[71]

III. Significance of Court's Ruling and Impact on Franchising

The judge's decision to deny Harley-Davidson's motion to transfer and motion to dismiss the contractual claims based on the implied covenant of good faith and fair dealing has given franchisees a novel possibility of ultimately prevailing on statutory or contractual claims for violations of duties that are otherwise inconsistent with or contradict express language in their contracts.

As a preliminary matter, *Cycle City* demonstrates the importance of the language of a forum selection clause and a governing law clause. Had it not been for the inclusion of the language expressly providing for the application of the applicable relationship statute, the result could have been considerably different. The application of a state dealership or franchise relationship statute in favor of filing suit in a venue different from a contractual forum is not a new concept. Indeed, many states have dealer/distributor/franchisee protection statutes that contain provisions similar to those of the HMVILA that prohibit a dealer, distributor, or franchisee from being required to litigate in a forum outside its home state, or otherwise declare void such forum selection clauses or other clauses limiting a dealer's rights.[72] However, in applying such statutes, courts—such as in *Caribbean Restaurants*[73]—have enforced forum selection clauses requiring suit to be brought in a certain state, notwithstanding statutory law voiding and prohibiting such clauses.[74] The difference will ultimately lie in what the parties' agreement says, what the parties intended, and the relevant substantive state law. With the benefit of the *Cycle City* ruling, franchisees now know that their home state's law can still apply to override the express language of

71. *Id.* at 41–42.

72. *See*, *e.g.* Puerto Rico Law 75, 10 LAWS P.R. ANN. § 278b2 (providing that "any stipulation that obligates a dealer to . . . litigate any controversy that comes up regarding his dealer's contract outside of Puerto Rico, or under foreign law or rule of law, shall likewise be considered as violating the public policy set forth by this chapter and is therefore null and void"); N.H. REV. STAT. ANN. § 357-C:6, III; California Franchise Relations Act ("a provision in a franchise agreement restricting venue to a forum outside [California] is voided with respect to any claim arising under or relating to a franchise agreement involving a franchise business operating within [California]"); Wisconsin Fair Dealership Law, WIS. REV. STAT. ANN. §§ 135.025(2)(b), 135.025(3) (purpose of state law is "to protect dealers against unfair treatment by franchisors, who inherently have superior economic power," while statute also directs that the effect and purpose of such law "may not be varied by contract or agreement" and "[a]ny contract or agreement purporting to do so is void and unenforceable").

73. See Part II.B., *supra.*

74. Minutes, Doc. No. 29, July 9, 2014, at 3. *See*, *e.g.* Caribbean Rests., LLC v. Burger King Corp., No. 12-1200, 2014 U.S. Dist. LEXIS 76352 (D.P.R. June 3, 2014); Rolfe v. Network Funding LP, No. 14-9, 2014 U.S. Dist. LEXIS 67476 (W.D. Wis. May 16, 2014). *But see* Kubis & Perszyk Assocs., Inc. v. Sun Microsys., Inc., 680 A.2d 618 (N.J. 1996) (forum selection clause inconsistent with New Jersey franchise law policy).

their agreement if the agreement's language anticipates this application.[75] If their home state contains a contractual duty of good faith and fair dealing, contract claims based on violations of the implied duty will likely be viable. On the other hand, franchisors that want their specific forum selection clauses to be upheld and enforced, notwithstanding applicable relationship laws, should include express language stating so.

Notwithstanding the governing law clause in the *Cycle City* distributorship agreement, the opinion indicates that the judge could have still denied dismissal of the contractual claims. First, with regard to Cycle City's claim based on improper price increases, the court stressed that a party cannot hide behind provisions reserving a discretionary right and at the same time exercise such discretionary power arbitrarily, capriciously, or in bad faith. Although courts have historically given broad deference to a franchisor's or manufacturer's business judgments, *Cycle City* demonstrates that in cases where the exercise of a discretionary right has the effect of injuring the other party, a claim based on breach of the implied covenant of good faith and fair dealing can be successful. Moreover, because the facts in *Cycle City* involved an almost fifty-year relationship involving continuous renewals, it is plausible that the court would have looked to the parties' historical relationship in assessing what was reasonably expected and whether the parties' expectations were frustrated.[76] As *Cycle City* progresses through the court system, it will be interesting to see how future franchisee suits involving similar conduct will develop.

75. *See* Cadapult Graphic Sys., Inc. v. Tektronix, Inc., 98 F. Supp. 2d 560 (D.N.J. 2000) (28 U.S.C. § 404(a) was applied so that valid forum selection clause selecting Oregon was entitled to substantial consideration and enforced against plaintiff in the absence of evidence of fraud or overreaching); Davis v. Great Am. Cleaners, Inc., 1996 WL 1185042 (Mass. Super. Ct. 1996) (forum clause not enforced due to unequal bargaining power, burden on franchisee).

76. *See* Atl. Richfield Co. v. Razumic, 390 A.2d 736, 746 (Pa. 1978) (Pomeroy, J., concurring) ("a franchisor should not be able, by use of multiple renewals of short term agreements, to provide opportunities for the arbitrary termination of a franchise to the detriment of the franchisee. . . . Likewise, although the duration of a fixed term may be of reasonable length, a franchisor, because of his prior course of dealing, may be estopped from refusing to renew without cause."); *see also* Sons of Thunder, Inc. v. Borden, Inc., 690 A.2d 575, 576 (N.J. 1997); Toysrus.com, L.L.C. v. Amazon.com Kids, Inc., No. A-3391-06T2, 2009 WL 747898, at *18 (N.J. Super. Ct. App. Div. Mar. 24, 2009) (in applying Delaware law, court stated that "the concept of good faith requires consideration of the 'spirit' of the agreement, as well as its expression.' In sum, the implied covenant of good faith is the obligation to preserve the spirit of the bargain rather than the letter, the adherence to substance rather than form.'") (citations omitted).