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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION FOUR

FAMOUS DAVE'S OF AMERICA, INC., Plaintiff and Respondent, v. SR EL CENTRO FD, INC. et al., Defendants and Appellants.	B276088 (Los Angeles County Super. Ct. No. BC589329)

APPEAL from an order of the Superior Court of Los Angeles County, Elihu M. Berle, Judge. Affirmed.

Zfaty/Burns, Ryan N. Burns and Isaac Zfaty for Defendants and Appellants.

Vedder Price, Germain D. Labat and Deborah A. Hedley for Plaintiff and Respondent.

Franchisees SR El Centro FD, Inc.; SR Long Beach FD, Inc.; SR Palmdale FD, Inc.; SR Simi Valley FD, Inc., and SR Tracy FD, Inc., appeal from a preliminary injunction prohibiting them from using, displaying, and infringing upon the intellectual property of respondent franchisor Famous Dave's of America, Inc., after the termination of their franchise agreements. Appellants argue the court misapplied the standard for issuance of a mandatory injunction, and abused its discretion in finding that respondent would succeed on the merits and in balancing the harms. We disagree and affirm.

FACTUAL AND PROCEDURAL SUMMARY

Respondent is a Minnesota corporation that owns, operates, and franchises Famous Dave's restaurants throughout the United States. It owns the registered trademark "Famous Dave's," as well as other marks, trade names, logos, symbols, slogans, and tag lines.

Pursuant to a bankruptcy reorganization plan in 2010, the franchise agreements for the Famous Dave's restaurants in El Centro, Palmdale, Simi Valley, Long Beach, and Tracy were assigned to appellants, and appellants are subject to their provisions. Appellants are wholly-owned subsidiaries of SR Restaurant Holdings Group, Inc. (Holdings Group), which in turn is owned in equal parts by two entities: M Mart and Shoreline FD Investors, LLC (Shoreline). M Mart is controlled by Kurt Schneiter, an investor who became involved with the restaurants in 2013 through the bankruptcy proceeding; Shoreline is controlled by John and Allen Gantes, the owners of the original franchisees that had declared bankruptcy. Schneiter is president and sole director of the Holdings Group. The Ganteses managed the restaurants through Synergy Pacific Management, LLC (Synergy) until the fall of 2014, when Schneiter terminated Synergy, and became embroiled in a shareholder dispute with the Ganteses.[1]

In the following months, respondent refused to deal with Schneiter and his team, specifically operations director Sandy Kraus, who worked closely with Schneiter. In response to Kraus's e-mail request for access to marketing resources in December 2014, respondent's then-chief executive officer Ed Rensi instructed his staff that Schneiter had "no standing" with respondent and "Gantes is the Franchisee we hold accountable for these restaurants." As a result, Kraus was denied access absent permission from the Ganteses. Synergy and the Ganteses had access to marketing resources until June 2015, when Kraus was allowed access to such resources. In January 2015, respondent conducted "surprise inspections" of the restaurants. In February 2015, respondent refused to print menus ordered by Kraus, and at Allan Gantes's request, Schneiter was removed from all distribution lists. Rensi assured the Ganteses that Schneiter would not be allowed to attend respondent's events, and in March 2015, Schneiter was prevented from attending an operations conference. He estimated that respondent's interference with his operation of the restaurants resulted in a six-percent decrease in sales, loss of staff, and increased attrition costs.

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[1] Lawsuits filed by the Gantes-controlled entities against appellants, Schneiter, his team, and entities he controlled were voluntarily dismissed in June 2015 after the denial of motions for appointment of a provisional director, preliminary injunction, and appointment of a receiver in April 2015.

Under the franchise agreements, appellants are obligated to use the Famous Dave's marks and distinctive restaurant system only with respondent's approval, to pay monthly royalty and marketing fees, to provide accurate records of daily revenues, and not to allow untrained management staff to participate in restaurant operations. The obligation to pay fees is "absolute and unconditional" and may not be offset by any claims appellants may have against respondent.

Appellants stopped reporting sales in January 2015. They attempted to stop the January 2015 payment of fees and afterwards failed to make timely and complete payments. Schneiter claimed respondent denied appellants access to respondent's portal for reporting sales, but according to respondent's witnesses, Kraus had access to the external portal between April 2014 and July 2015; temporary interruptions in access to the portal occurred after termination of the franchise agreements.

In January 2015, appellant's counsel sent a letter to Rensi questioning why he considered John Gantes, rather than appellants, to be the franchisee of record, whose permission was necessary to access franchise resources. Counsel stated that if respondent did not recognize appellants' franchise agreements, appellants would "simply re-brand." Respondent's counsel replied that rebranding would be a violation of the franchise agreements, explaining that respondent had not been formally advised of Schneiter's claim of ownership and operation of the restaurants, nor had Schneiter undergone the management training required in the franchise agreements. In March 2015, appellant's counsel advised respondent of the pending management-related lawsuits filed by the Gantes-controlled entities against Schneiter and appellants. Counsel described the lawsuits as lacking merit, but acknowledged that the Ganteses appeared to be "controlling the narrative at this juncture."

According to respondent's chief financial officer, respondent knew Schneiter was a passive investor. Although in fall 2014 respondent's management learned that Synergy had been terminated, and in conversation Schneiter had claimed to be running the restaurants, the Ganteses remained the contacts of record as there was no formal written communication regarding the change in appellants' management until April 2015. It was then that appellants' counsel explained the change in management and asked that all communications between respondent and appellants be directed to Schneiter, rather than to the Ganteses.

In March and April 2015, respondent sent successive notices of default to each appellant, allowing for cure of the unpaid fees. A notice of immediate termination was served on them in May 2015. The March default notices were addressed to John Gantes, and the Ganteses' attorney transferred the wiring instructions for immediate payment to Schneiter's counsel. All subsequent notices included Schneiter.

The franchise agreements provide that any unauthorized use of the Famous Dave's marks post-termination constitutes an infringement on respondent's rights, and that respondent may seek injunctive relief to prevent it. The parties engaged in unsuccessful post-termination negotiations, and appellants paid some of the outstanding fees, but did not fully cure the defaults. They continued to operate the restaurants as though they were still licensed franchisees, despite receiving cease and desist letters from respondent.

In July 2015, respondent sued appellants, Schneiter, the Ganteses, and the entities that own the Holdings Group. The lawsuit was for infringement of intellectual property rights, unfair competition, breach of contract, and other claims. In October 2015, respondent moved for a preliminary injunction to prevent the continued use and infringement of its marks. Appellants cross-complained for breach of contract, breach of the covenant of good faith and fair dealing, and aiding and abetting breach of fiduciary duty.

In May 2016, the trial court granted respondent's request for a preliminary injunction. The court found that appellants had breached the franchise agreements by failing to pay fees. The court also found that even if respondent was on notice about the change in appellants' management, it did not materially breach the agreements by communicating with the Ganteses instead of Schneiter, since the Ganteses had served as long-term contacts and continued to have 50-percent ownership in the restaurants. The court found respondent was not required to provide Schneiter with training, as the obligation to obtain training was upon him, and he had access to training at the Long Beach site, which is a certified training location. Alternatively, the court found that even if respondent had breached the agreements, appellants did not provide notice of the breaches and opportunity to cure, as required by the franchise agreements. The court ruled that as to any uncured breach appellants should have terminated the franchise agreements, instead of continuing operation as licensees while withholding fees. The court noted that the franchise agreements prohibit offsetting any claims against the fee obligations. The court concluded that it was reasonably probable that respondent would prevail on the merits.

On the balance of harms, the court rejected appellants' argument that this was a dispute exclusively about money damages; it presumed that trademark dilution and infringement cause irreparable harm and warrant appropriate injunctive relief. The court also rejected appellants' argument that forcing them to "de-brand" would be devastating, noting that the argument emphasized the importance of respondent's brand. It concluded that the equities favored respondent.

This appeal from the preliminary injunction order followed.

DISCUSSION

I

The granting of a preliminary injunction requires consideration of "'two interrelated factors: (1) the likelihood that the plaintiff will prevail on the merits, and (2) the relative balance of harms that is likely to result from the granting or denial of interim injunctive relief.' [Citation.]" (*Jay Bharat Developers, Inc. v. Minidis* (2008) 167 Cal.App.4th 437, 443 (*Jay Bharat*).) "'The party challenging an order granting or denying a preliminary injunction has the burden of making a clear showing of an abuse of discretion. [Citation.] An abuse of discretion will be found only where the trial court's decision exceeds the bounds of reason or contravenes the uncontradicted evidence. [Citation.]' [Citation.] 'Where the evidence with respect to the right to a preliminary injunction is conflicting, the reviewing court must "interpret the facts in the light most favorable to the prevailing party and indulge in all reasonable inferences in support of the trial court's order."' [Citation.]" (*Ibid.*)

Appellants argue that a higher level of scrutiny is required because the order effectively requires that they close the restaurants and hence is a mandatory, not a prohibitory, injunction. We do not agree.

"To determine whether an injunction is mandatory or prohibitory, we 'examine the terms and effect of the injunction in order to discover its character. [Citation.]' [Citation.] 'The purpose of mandatory relief is to compel the performance of a substantive act or a change in the relative positions of the parties. [Citations.] By contrast, the prohibitive order seeks to restrain a party from a course of conduct or to halt a particular condition. [Citation.] The character of prohibitory injunctive relief, however, is not changed to mandatory in nature merely because it incidentally requires performance of an affirmative act. [Citation.]' [Citation.]" (*People ex rel. v. iMergent, Inc.* (2009) 170 Cal.App.4th 333, 342.)

Appellants were enjoined from "using, displaying and infringing on" respondent's intellectual property. They also were ordered to "remove and cease to use" any items that contain respondent's marks and to preserve and return such items to respondent. Contrary to appellants' assumption, the purpose of the injunction was not to maintain the status quo at the time the lawsuit was filed, but to prevent appellants' unauthorized use of respondent's intellectual property in order to prevent infringement on its brand and dilution of its trademarks. (See *14859 Moorpark Homeowner's Assn. v. VRT Corp.* (1998) 63 Cal.App.4th 1396, 1408 [status quo is """"the last actual peaceable, uncontested status which preceded the pending controversy""""]; see also 5 McCarthy on Trademarks and Unfair Competition § 30:50 (4th ed. 2003) ["In a trademark case, the status quo ante litem to be preserved by a preliminary injunction is the situation prior to the time the junior user began use of its contested mark: the last peaceable, noncontested status"].) Any aspects of the injunction that require appellants to engage in affirmative conduct are merely incidental to the injunction's preventive objective. Thus, the preliminary injunction is prohibitory in nature. (See, e.g., *Jaynes v. Weickman* (1921) 51 Cal.App. 696, 700–701 [enjoining trucker business from operating under certain trade name was preventive even if it incidentally required removal of name from trucks and signs]; *McDonald's Corp. v. Robertson* (11th Cir. 1998) 147 F.3d 1301, 1306, fn. 2 [prohibiting franchisee from operating specific restaurant and using trademarks was prohibitory, not mandatory].)

II

Appellants contend respondent cannot establish a likelihood of success on the merits because it, too, breached the franchise agreements. The contentions are based on claims that respondent refused to work with Schneiter and his team. Appellants do not cite the specific provisions of the franchise agreements that respondent breached, and it is undisputed that Schneiter was not the franchisee and did not have management training. The Ganteses were the contacts of record for appellants, and the evidence indicates that either they or Kraus had access to resources respondent offered its franchisees. Nor do appellants show that they gave respondent a proper notice of any claimed breaches of the franchise agreements while continuing to perform their obligations under those agreements. Rather, the evidence, viewed in favor of respondent, indicates that appellants stopped paying fees and reporting sales even before their attorney clearly advised respondent of Schneiter's status and rights under agreements to which respondent was not a party.[2]

Even were we to assume the validity of some of appellants' claims against respondent, those breach of contract claims do not defeat respondent's right to a preliminary injunction since it is undisputed that appellants breached the franchise agreements, did not cure the breaches in time to prevent termination of the agreements, and continued their then-unauthorized use of respondent's trademarks after termination. In rejecting a claim similar to the one appellants make in this case, the court in *Jay Bharat*, *supra*, 167 Cal.App.4th 437, 443–444 explained: "'Under basic contract principles, when one party to a contract feels that the other contracting party has breached its agreement, the non-breaching party may either stop performance and assume the contract is avoided or continue its performance and sue for damages. Under no circumstances may the non-breaching party stop performance *and* continue to take advantage of the contract's benefits.' [Citation.] Yet that is exactly what appellants tried to do. According to the evidence presented to the trial court, appellants breached the [franchise agreement] by failing to make royalty payments and failing to pay advertising fees. Despite their breaches, appellants still wanted to use the . . . franchise and trademarks. They cannot do so. Once appellants breached the [franchise agreement], respondents could terminate that franchise agreement and prevent appellants from utilizing the . . . franchise." (*Id.* at pp. 443–444; see also *S & R Corp. v. Jiffy Lube Int'l., Inc.* (3d Cir. 1992) 968 F.2d 371, 377 ["Where the franchise agreement gives the franchisor the power

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[2] At oral argument, appellant's counsel conceded that notice was given only after termination.

to unilaterally terminate the agreement under certain conditions, and those conditions exist, pre-termination complaints are not relevant to infringement . . . . Rather, pre-termination disputes affect the issue of damages"].)

Appellants misread *Jay Bharat*, *supra*, 167 Cal.App.4th 437 in arguing they have sued for damages while attempting to continue their performance under the franchise agreements. Appellants' attempts to bring overdue fees current as part of post-termination negotiations do not negate the fact that the franchise agreements were terminated for nonpayment of fees. Whether or not they are entitled to damages for respondent's alleged breaches, appellants lost the right to operate the restaurants pursuant to the franchise agreements when those agreements were terminated.

Appellants' reliance on Civil Code section 1439 also is misplaced. That statute provides: "Before any party to an obligation can require another party to perform any act under it, he must fulfill all conditions precedent thereto imposed upon himself; and must be able and offer to fulfill all conditions concurrent so imposed upon him on the like fulfillment by the other party. . . ." (Civ. Code, § 1439.) By its plain terms, section 1439 applies only to conditional obligations, whereas appellants' obligation to pay fees in the franchise agreements is expressly declared unconditional. Appellants cite no authority for their implied claim that section 1439 creates a nonwaivable statutory right or that an unconditional fee provision in a franchise agreement is unenforceable as written. (Cf., e.g., Civ. Code, § 3513 ["A contractual provision that contravenes public policy is illegal and either void or unenforceable"]; *Swenson v. File* (1970) 3 Cal.3d 389, 393–394 [enforcement of express non-compete clause limited by statute].) Moreover, appellants' factual assertions are unspecific as to time, without regard to whether respondent's complained-of actions preceded or followed appellants' own breaches and the termination of the franchise agreements.

Appellants' argument that respondent's breaches of unspecified conditions in the franchise agreements prevented their own performance also is not convincing. At most, Schneiter's declaration indicates the five restaurants experienced a drop in revenues and increased costs, but he does not claim the reduced profits made it impossible to pay fees. The claim that appellants were prevented from reporting sales because Kraus was denied access to the portal is disputed; viewed in respondent's favor, the evidence indicates that any break in access followed termination of the franchise agreements.

Appellants argue that a preliminary injunction is uncalled for because the dispute is purely monetary. This misrepresents the nature of the parties' post-termination conflict, which focuses on appellants' continued unauthorized use of respondent's intellectual property after the franchise agreements were terminated—a recognized basis for injunctive relief. (See *Jay Bharat*, *supra*, 167 Cal.App.4th at p. 444; *Foxworthy v. Custom Tees, Inc.* (N.D. Ga. 1995) 879 F.Supp. 1200, 1219 [trademark actions "are common venues for the issuance of preliminary injunctions"].)

The test for trademark infringement and unfair competition under both federal and California law "is whether the similarity between the two marks is likely to deceive or confuse the public." (*Mallard Creek Industries, Inc. v. Morgan* (1997) 56 Cal.App.4th 426, 435.) Similarly, under both federal and California law, trademark dilution requires that an infringer's use of an already famous and distinctive mark in commerce is likely to cause "dilution by blurring or dilution by tarnishment." (*Jada Toys, Inc. v. Mattel, Inc.* (9th Cir. 2008) 518 F.3d 628, 634.)

Irreparable harm has traditionally been presumed to flow from a finding of infringement, but after the United States Supreme Court in a patent case, *eBay Inc. v. MercExchange*, *LLC* (2006) 547 U.S. 388, 393–394 (*eBay*), rejected the automatic issuance of an injunction upon proof of infringement, there has been growing doubt about the use of the presumption in trademark cases. (See *Herb Reed Enterprises, LLC v. Florida Entertainment Management, Inc.* (9th Cir. 2013) 736 F.3d 1239, 1250–1251 [rejecting presumption in trademark case]; accord *Ferring Pharmaceuticals, Inc. v. Watson Pharmaceuticals, Inc.* (3d Cir. 2014) 765 F.3d 205, 216; cf. *North American Med. Corp. v. Axiom Worldwide, Inc.* (11th Cir. 2008) 522 F.3d 1211, 1228-1229 (suggesting, without deciding, presumption may be barred in trademark cases); accord *Swarovski Aktiengesellschaft v. Bldg. No. 19* (1st Cir. 2013) 704 F.3d 44, 54; but see J. Thomas McCarthy, *McCarthy on Trademarks and Unfair Competition* § 30:47.70 (5th ed. 2017) ("the presumption of irreparable injury traditionally followed in trademark preliminary injunction cases is in [no] way inconsistent with the letter or the spirit of the Supreme Court's *eBay* decision").`

Nevertheless, even after *eBay*, federal courts have found irreparable harm based on a showing of strong likelihood of consumer confusion and loss of control over reputation and goodwill from the continued unauthorized use of trademarks. (See *U.S. Polo Assn., Inc. v. PRL USA Holdings, Inc.* (2d Cir.

2013) 511 Fed.Appx. 81, 85 [finding irreparable harm from ceding to infringer control over one's reputation and goodwill "might be made in many infringement cases, [but] it is a factual finding nonetheless, and not simply the product of a legal presumption"]; *Paulsson Geophysical Services, Inc. v. Sigmar* (5th Cir. 2008) 529 F.3d 303, 313 [substantial threat to goodwill and value of trademark from infringer's continuing use of it while modifying associated technology]; *Audi AG v. D'Amato* (6th Cir. 2006) 469 F.3d 534, 550 [continued unauthorized use of trademarks in domain name and in counterfit goods established potential future harm].) The likelihood of consumer confusion and loss of control over one's reputation and goodwill is "almost certain" in franchise cases where a franchisee continues to hold out its continued use of trademarks as authorized. (See *Petro Franchise Systems, LLC v. All American Properties, Inc.* (W.D. Tex. 2009) 607 F.Supp.2d 781, 794–795; *TGI Friday's Inc. v. Great Northwest Restaurants, Inc.* (N.D. Tex. 2009) 652 F.Supp.2d 763, 772; see also *Sylvan Learning Inc. v. Learning Solutions, Inc.* (S.D. Ala. 2011) 795 F.Supp.2d 1284, 1300 [continued unauthorized use of license].)

Respondent has shown that it has distinctive registered trademarks that are nationally recognizable. Appellants' continued unauthorized use of those trademarks after the termination of the franchise agreements is almost certain to cause consumer confusion, regardless of the quality of services appellants provide, if appellants continue to hold themselves out as legitimate franchisees when they are not. Appellants' complaints that they have continuously been denied access to the full range of marketing and menu options and that they have experienced loss of revenue as a result further support the harm to respondent from their provision of incomplete franchise services. Their continued operation prevents the establishment of legitimate franchises in the locations. Appellants have in the past refused routine inspections by respondent or have sought to impose conditions on such inspections, to which respondent has not agreed. Viewed in favor of respondent, the evidence shows that the parties have been unable to negotiate a good working relationship that would give respondent the ability to control its goodwill and reputation. Thus, respondent is reasonably likely to suffer irreparable harm from appellants' continued unauthorized operation of the franchises.

While irreparable harm to the franchisor from a former franchisee's continued unauthorized use of distinctive trademarks may be virtually certain, courts have been much less sympathetic to the infringing franchisee's claim of irreparable harm. (See, e.g., *Wetzel's Pretzels, LLC v. Johnson* (C.D. Cal. 2011) 797 F.Supp.2d 1020, 1028 [threat of closing small family business insufficient to overcome harm to franchisor]; *TGI Friday's Inc. v. Great Northwest Restaurants, Inc.*, *supra*, 652 F.Supp.2d at pp. 772–773 [harm from restaurant closing compensable through money damages].) As the trial court found here, the fact that the franchisor's marks "are so integral to defendants' restaurant operations that they will be forced to close their restaurants if they cannot use the marks . . . further demonstrates the value of [the franchisor's] name and marks and the substantial threat *it* faces if . . . unlicensed restaurants are permitted to pass themselves off as [the franchisor's] restaurants." (*Id*. at p. 773.) Furthermore, appellants' claim of irreparable harm from having to close the restaurants in order to re-brand rings hollow since through counsel, they threatened to do just that in 2015.

We find no abuse of discretion in the trial court's issuance of a preliminary injunction in favor of respondent.

DISPOSITION

The order is affirmed. Respondent is entitled to its costs on appeal.

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EPSTEIN, P. J.

We concur:

MANELLA, J.

COLLINS, J.