

# PUBLICATION

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## Hardee's Successfully Defends Market Contraction Claims After Franchisee Blames "Lewd" Advertisements

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The advertising by the super-competitive QSR burger-themed chains clamors for viewer attention. When it plays to the young male demographic exclusively, at the risk of offending female patrons and viewers, does it justify abandoning the franchise? Specifically, would hamburger advertisements entitled "Patty Melts for You" and "Flat Buns," depicting scantily clad women, play in Peoria beyond the 18-49 male audience? Customers of a Hardee's franchise in nearby Ottawa, Illinois, a "primarily agricultural and union oriented community,"<sup>1</sup> took offense, as did a group known as "One Million Moms" who shut down the Hardee's email servers in protest. When the owners of the Ottawa franchise experienced a dip in sales and an alleged decline of the goodwill in the Hardee's brand and trademarks licensed to them as Hardee's market share and store count declined in the DMA of greater Chicago, the owners closed the doors and abandoned the franchise more than a year before the end of their five-year renewal.

In *Hardee's Food Systems, Inc. v. Jeffrey T. Hallbeck*, 2011 U.S. Dist. LEXIS 107038 (E.D. Mo. Sept. 21, 2011), Hardee's sued the owners of the Ottawa franchise seeking lost future franchise fees, but the franchisees counterclaimed that by running the allegedly lewd ads, Hardee's breached its advertising obligations under the five-year Renewal Franchise Agreement signed in 2005 (a year after Hardee's five-year ad campaign began to run).

The franchise agreement required the franchisees to pay into the Hardee's National Advertising Fund (HNAF) "for the creation and development of advertising, marketing and public relations, research and related programs, activities and materials that [Hardee's], in its sole discretion, deems appropriate."<sup>2</sup> The agreement further provided that Hardee's would have the "sole discretion over creative concepts, materials and endorsements used in those programs and activities, and the geographic, market and media placement and allocation of advertising and marketing materials." The agreement also included an acknowledgement that the HNAF is intended to enhance the recognition and patronage of the Hardee's restaurants and a waiver of liability with respect to the maintenance, direction or administration of the HNAF.

One of the Ottawa franchise owners testified that he was aware of the ad campaign before he entered into the renewal agreement and that he was "unhappy" with the advertisements.<sup>3</sup> Hardee's stated purpose in producing these ads "was to appeal to a particular target demographic – 18-49 year old males – which [Hardee's] sees as important to the success of the Hardee's brand nationwide as it competes with larger chains of quick-service restaurants with large advertising budgets."<sup>4</sup>

The commercial entitled "Patty Melt," for the new "Patty Melt Thickburger," featured a model "beck[oning] the viewer with her finger," in a suggestive pose as a female voice reads: "Ten: Shhh, kiss me on the lips. Nine: Run your fingers through my hair. Eight: Touch me. Hold it; no wait, let's go straight to number one." The tag line is "Patty melts for you."<sup>5</sup>

The commercial entitled "Flat Buns," which ran for the Hardee's affiliate Carl's Jr., featured a female teacher dancing in a lewd manner as students begin rapping suggestively about "flat buns," with lyrics such as "flatter makes a better rear; stand sideways, girl, you disappear," and "in anatomy class, you got a butt minus."<sup>6</sup>

The ads ran in all market areas in which all of the Hardee's restaurants were operated by Hardee's Food Systems, Inc. itself, "whereas the decision whether to run the ads in other market areas was made by individual advertising cooperatives composed of the operators of Hardee's restaurants within the market areas – or by those owned by [Hardee's Food Systems, Inc.] itself and those owned by the franchisees."<sup>7</sup> The ads did not air in the Ottawa market, but when they ran in the nearby Peoria market, "the public became aware of them and [the franchise owners] received repeated complaints from residents in Ottawa's predominantly agricultural and union oriented community, about the unacceptable nature of these ads."<sup>8</sup>

The Ottawa franchise owners claimed that by running the allegedly "lewd" advertisements, Hardee's "exercised its duties and discretion related to the HNAF in a manner so as to deny the [Ottawa franchisees] the expected benefit of the contract, in violation of the implied contract of good faith and fair dealing."<sup>9</sup> Hardee's moved for summary judgment.

The U.S. District Court for the Eastern District of Missouri, applying Missouri law, held that "no reasonable factfinder could find that [Hardee's] breached the implied covenant by its challenged actions. Under Missouri law, a covenant of good faith and fair dealing is imposed on every contract. When, as here, a decision is left to the discretion of one party, 'the question is not whether the party made an erroneous decision but whether the decision was made in bad faith or was arbitrary or capricious so as to amount to an abuse of discretion.'"<sup>10</sup> Since the court found that the Ottawa franchise owners failed to provide any evidence of bad faith on behalf of Hardee's in producing and airing the advertisements in question, the court dismissed the franchise owner's claims on summary judgment to dismiss the counterclaim. While the marketplace second-guessed the campaign, the court refused to do so and allowed the campaign to be the basis of a successful affirmative defense by the Ottawa franchisee to the franchisor's claim for wrongful termination of the franchise. In the furor over the titillation of the advertising, the claim that the franchisee could terminate for Hardee's loss of market share and market presence was largely ignored.

The franchisees may not have had a lot of firepower behind their counterclaims under Missouri law, but Hardee's had ample defenses in reserve. The Missouri court did not discuss the provisions of the franchise agreement reserving "sole discretion" to Hardee's over the creative concepts of its advertisements, but such language may prove useful and necessary in similar cases and in other jurisdictions.

The case reminds franchisors of all varieties of brands and products to check the language in their franchise agreements that retains the ability to control and direct the chain's advertisements, particularly given the unpredictability of market reaction to aggressive, suggestive advertising that appeals to a narrow demographic, even if it is the primary customer group of the chain. Franchisees must overcome a heavy burden to obtain redress when advertising goes awry and causes customer loss, particularly in declining markets.

1. See Defendants' Second Amended Answer, Affirmative Defenses, and Counterclaim to Plaintiff's First Amended Complaint [R. Doc. No. 166], p. 14, ¶ 15 (hereinafter, "Franchisees' Counterclaim"), in *Hardee's Food Systems, Inc. v. Jeffrey T. Hallbeck*, 2011 U.S. Dist. LEXIS 107038 (E.D. Mo. Sept. 21, 2011).

2. *Hardee's*, 2011 US Dist. LEXIS 127169, at \*9.

3. *Id.* at \*7.

4. *Id.*

5. See Franchisees' Counterclaim, p. 12, at ¶ 13.

6. See Franchisees' Counterclaim, p. 12, at ¶ 14.

7. *Hardee's*, 2011 US Dist. LEXIS 127169, at \*7.

8. See Franchisees' Counterclaim, p. 13, at ¶ 15, & Ex. "A," at p. 2.

9. *Hardee's*, 2011 US Dist. LEXIS 127169, at \*6.

10. *Id.* at \*8 (citing *Mo. Consolidated Health Care Plan v. Community Health Plan*, 81 S.W.3d 34, 48 (Mo. Ct. App. 2002)).

