

The Importance of Termination Provisions in Franchise Agreements and License Agreements

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Key Take: *Franchisees may be subject to injunctions for improper termination of franchise agreements.*

Franchise agreements, which are often accompanied by license agreements, grant franchisees the right to use the franchisor's brand, including the franchisor's registered trademarks and system manuals needed to operate the brand. Franchisors are generally the primary drafter of their franchise and license agreements, which often tend to favor the franchisors. As a result, franchise and license agreements are usually one-sided and minimally negotiable.

When entering into franchise agreements, franchisors and franchisees should pay special attention to the termination provisions contained within their agreements. Often, franchisors will include termination provisions allowing the

franchisor to terminate the franchise agreement on a variety of grounds. On the other hand, *franchisees* will usually have few to no grounds for termination, leaving them little recourse if they become dissatisfied with the performance of the franchisor's brand or otherwise wish to terminate their franchise agreements.

Franchisees should also be aware of the potential for franchisors to obtain injunctions and/or specific performance when faced with the threat of termination. Generally, courts do not view license agreements or franchise agreements as contracts for personal services, which are not subject to the remedy of specific performance in the event of one party's breach.^[1] In *CPTS Hotel Lessee LLC v. Holiday Hospitality Franchising, LLC*, the First Department affirmed the trial court's grant of plaintiff Holiday Hospitality Franchising LLC's motion for a preliminary injunction enjoining defendant CPTS Hotel Lessee LLC from terminating a license agreement by which Holiday granted CPTS a license to continue operating under the Crowne Plaza system.^[2] Here, CPTS sought to terminate the license agreement due to Holiday's alleged material breach of a provision whereby Holiday was required to market and promote the hotel. The license agreement, however, contained a provision explicitly waiving CPTS' right to terminate the license "on any legal, equitable or other grounds."^[3] The waiver included arguments that the license was void or that a breach on behalf of Holiday would relieve CPTS of its obligations to honor the agreement, but included an authorized exception for claims that Holiday failed to adequately market the hotel.^[4]

While CPTS argued that the license agreement created "a personal services relationship between the two parties and, therefore, any waivers of CPTS' right to terminate the agreement is invalid," the court rejected this argument. The First Department held that the trial court "correctly determined that the license agreement between Holiday Hospitality and CPTS is not a contract for personal services, because

it lacks the requisite delegation of substantial discretion to the licensee (CPTS) in the operation of the subject hotel.”[5] The First Department further held that the trial court “correctly found that the harm to licensor Holiday Hospitality’s brand reputation and goodwill as a result of an improper termination of the agreement, which would cause the Times Square location to lose its branding as a Crowne Plaza hotel, was within the parties’ contemplation at the time the agreement was signed.”[6] *CPTS Hotel* indicates that courts may consider reputational harm to the brand as irreparable harm and are willing to order specific performance when franchisors are faced with termination.

In addition to provisions regarding termination *for cause*, franchisees should also pay close attention to any damages provisions, including liquidated damages. Recognizing that a franchisee’s ability to negotiate the terms of a franchise agreement or license agreement are often limited, franchisees should (to the extent possible) ensure that any liquidated damages provisions apply to termination by both franchisors *and* franchisees. Courts generally find that liquidated damages clauses preclude recovery of actual damages, which allows for a degree of predictability in assessing whether termination is an affordable option.[7] Both franchisors and franchisees should ensure that they carefully review franchise agreements and license agreements and are aware, at the outset, of their recourse options in the event the relationship sours before the expiration of the franchise term.

[1] *Husain v. McDonald’s Corp.*, 205 Cal.App.4th 860 (Cal. Ct. App. 2012).

[2] *CPTS Hotel Lessee LLC v. Holiday Hospitality Franchising LLC*, 171 A.D.3d 484 (1st Dep’t 2019).

[3] *Holiday Hospitality Franchising LLC v. CPTS Hotel Lessee LLC*, No. 653096/2016, 2018 WL 2123971, at *2 (Sup. Ct. N.Y. Cnty. May 1, 2018), *aff'd* 171 A.D.3d 484 (1st Dep't 2019).

[4] This type of waiver is just one example of the many ways that most franchise agreements and license agreements favor franchisors.

[5] *CPTS Hotel*, 171 A.D.3d at 485.

[6] *Id.*

[7] *See Brecher v. Laikin*, 430 F.Supp. 103, 106 (S.D.N.Y. 1977) (“Where the court has sustained a liquidated damages clause the measure of damages for a breach will be the sum in the clause, no more, no less.”).