IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

SHADEWELL GROVE IP, LLC, a Delaware limited liability company, Plaintiff, v. MRS. FIELDS FRANCHISING, LLC, a Delaware limited liability company, Defendant.	)	Civil Action No. 1691-N

MEMORANDUM OPINION

Submitted: February 1, 2006
Decided: May 8, 2006

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PARSONS, Vice Chancellor.

Shadewell Grove IP, LLC ("Shadewell") brought this action against Mrs. Fields Franchising, LLC ("Mrs. Fields") seeking declaratory judgment, specific performance, and damages resulting from Mrs. Fields's alleged breaches of three licensing agreements and the covenants of good faith and fair dealing implied therein.[1] This opinion reflects the Court's post-trial findings of fact and conclusions of law.

For the reasons stated, the Court finds that the parties did not orally modify the license agreements as Shadewell averred, Mrs. Fields did not waive its right to strict compliance and Shadewell's payments should be applied ratably over the three agreements. Therefore, Mrs. Fields terminations of two of the three license agreements remains in effect.

I. BACKGROUND

A. Parties

Shadewell is a Delaware limited liability company with its principal place of business in Tulsa, Oklahoma.[2] A licensee of Mrs. Fields, Shadewell is primarily in the business of marketing and selling Mrs. Fields food products in a variety of outlets, including supermarkets.[3] Shadewell acquired the licenses in dispute in March 2004 from a prior licensee.

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1 On November 5, 2005, the Court bifurcated the trial, with the damages portion of Shadewell's claims to be tried, if necessary, at a later date.

2 Pretrial Order ¶ II.1.

3 *Id.* at ¶¶ II.4–7; Tr. at 285 (Bruer). Citations in this form are to the trial transcript ("Tr.") and indicate the page and, where it is not clear from the text, the witness testifying.

Shadewell is the successor-in-interest to Nonni's Food Company, Inc. ("Nonni's").[4] Before entering into the licensing agreements with Mrs. Fields, Nonni's was a $19 million biscotti business.[5] Sometime in 1999, Mrs. Fields contacted Swander Pace Capital[6] ("Swander Pace") with an interest in licensing its brand to a packaged food company that could create a shelf-stable, ready to eat product.[7] Swander Pace then contacted Nonni's. Nonni's submitted a bid and it and Mrs. Fields, over time, entered into several licensing agreements.

Mrs. Fields is a publicly traded Delaware limited liability company with its principal place of business in Salt Lake City, Utah.[8] Mrs. Fields is primarily in the business of selling baked goods through retail locations nationwide. The company also enters into licensing agreements with companies like Shadewell to distribute shelf-stable food products in other retail outlets. Mrs. Fields owns less than 5% of Shadewell's stock and has a representative on Shadewell's board.[9]

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4 Shadewell was spun-off from Nonni's in March 2004. Tr. at 314 (Bruer).

5 Tr. at 278 (Bruer).

6 Swander Pace Capital is a private equity fund and, in 1999, was Nonni's primary equity investor. Tr. at 279 (Bruer).

7 *Id.*

8 Pretrial Order ¶ II.2.

9 *Id.* ¶ II.3.

B. Agreements

Since January 2000, Nonni's and Shadewell have entered into a variety of trademark license agreements with Mrs. Fields. Only three of these agreements are at issue in this case.[10] The agreements provide Shadewell with the exclusive right to "develop, manufacture, package, distribute, and sell various food products that utilize Mrs. Fields trademarks, service marks, and trade names."[11]

The first of the agreements at issue was entered into on January 3, 2000 (the "2000 Agreement").[12] This agreement makes Shadewell the exclusive provider of shelf-stable ready to eat cookies packaged for retail sale in North America under the Mrs. Fields name. The vast majority of Shadewell's revenue comes from the 2000 Agreement.[13]

The second agreement was entered into on February 21, 2001 (the "2001 Agreement").[14] This agreement gives Shadewell the same exclusivity as the 2000 Agreement but for commercially pre-baked ready to eat cookies packaged for food services.

The language of the termination provisions of the 2000 and 2001 Agreements are identical. They provide:

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10 In addition to the three agreements at issue, Shadewell and Mrs. Fields are parties to a fourth licensing agreement concerning brownies and ice cream toppings. Tr. at 5.

11 PX 38.

12 PX 1.

13 Tr. at 31–32 (Ward).

14 PX 2.

> If [Shadewell] defaults in the payment of any Running Royalties then this Agreement and the license granted hereunder may be terminated upon notice by [Mrs. Fields] effective thirty (30) days after receipt of such notice, without prejudice to any and all other rights and remedies [Mrs. Fields] may have hereunder or by law provided, and all rights of [Shadewell] hereunder shall cease.[15]

Neither the 2000 nor the 2001 Agreement defines the term "default." Further, the agreements do not provide a way for Shadewell to cure a default once declared by Mrs. Fields.

The third agreement was entered into on March 31, 2003 (the "2003 Agreement").[16] The 2003 Agreement gives Shadewell the right to manufacture, package, and sell pre-packaged chocolate chips bearing Mrs. Fields trademarks, service marks, and trade names. While the 2003 Agreement also fails to define the term "default," it varies substantially from the 2000 and 2001 Agreements in a major respect: it gives Shadewell five days from the date of notice of default to pay any outstanding balance to cure a default. The termination provision of the 2003 Agreement provides:

> If [Shadewell] defaults in the payment of any Running Royalties then this Agreement and the License granted hereunder may be terminated upon notice by [Mrs. Fields] effective thirty (30) days after receipt of such notice, without prejudice to any and all other rights and remedies [Mrs. Fields] may have hereunder or by law provided, and all rights of [Shadewell] hereunder shall cease, *provided that*

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15 PX 1 § 16(b)(i); PX 2 § 16(b)(i).

16 PX 3. The Court will refer to the 2000, 2001 and 2003 Agreements collectively as the "Agreements."

> *[Shadewell] has not cured such default within five (5) days of receipt of such notice*.[17]

As part of the consideration for each of the exclusive licenses, Shadewell had to pay Mrs. Fields running royalties on the "last day of the month following the end of each calendar quarter covered by the Agreement."[18] Shadewell consistently had difficulty making these payments on time.

Because Shadewell did not pay the running royalties for the first three quarters of 2004 on time, on December 24, 2004, the parties amended the running royalty provisions of the Agreements.[19] Pursuant to this amendment, the running royalty payments were due "no later than 60 days following the end of each calendar quarter covered by the Existing Agreement."[20] The amendment gave Shadewell an additional month to pay the running royalties to Mrs. Fields.

Each of the Agreements includes a "Waiver by Custom or Practice" provision that states:

> [Mrs. Fields and Shadewell] shall not be deemed to have waived or impaired any right, power or option reserved by this Agreement (including, without limitation, the right to demand exact compliance with every term, condition and covenant herein or to declare any breach thereof to be a default and to terminate this Agreement prior to the expiration

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17 PX 3 § 16(b)(i) (emphasis added).

18 PX 1 § 5; PX 2 § 5; PX 3 § 5.

19 The only payment Shadewell made on time was for the second quarter of 2005. That was after the initiation of this litigation. Pretrial Order ¶ 39.

20 DX 4 ¶ 1.

> of its terms) by virtue of any custom or practice of the parties at variance with the terms hereof . . . .[21]

Each agreement required some up front expenditures by Nonni's. Pursuant to the 2000 and 2001 Agreements, Nonni's paid Mrs. Fields an upfront fee.[22] In addition, under the 2000 Agreement, Nonni's had to create the product before Mrs. Fields would sign the agreement.[23] Creating the product took approximately four to five months.[24] Nonni's also had to develop the product for the 2001 Agreement, which required Nonni's to create new packaging and hire a new team of salespeople.[25] Nonni's thus made substantial investments because of the 2000 and 2001 Agreements.[26]

C. Transfer of Shadewell's Assets

In July 2005, Shadewell began negotiations to transfer substantially all of its assets to a prospective acquirer, including the Agreements. Shadewell has the contractual right

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21 PX 1 § 22(f); PX 2 § 22(f); PX 3 § 22(f).

22 The 2000 Agreement required Nonni's to pay an upfront fee of $2,000,000. Tr. at 290 (Bruer). Bruer could not recall exactly how much Nonni's paid upfront under the 2001 Agreement, but estimated it to be around $500,000. Tr. at 298–99.

23 Tr. at 288 (Bruer).

24 Tr. at 287 (Bruer).

25 Tr. at 301–03 (Bruer).

26 It is unclear from the record exactly how much Nonni's invested in each Agreement. The 2000 Agreement likely involved the largest investment by Nonni's.

to sell the Agreements as part of a transfer of all or substantially all of its assets.[27] The Shadewell board discussed this transaction at several meetings.

Representatives from Mrs. Fields, including its President and CEO, Stephen Russo, met with the prospective acquirer in June 2005 approximately one week after Shadewell informed Mrs. Fields of the possible transfer of the Agreements.[28] Shortly thereafter, Mrs. Fields expressed opposition to the deal. While Russo was impressed with the quality of personnel and cleanliness of the prospective acquirer's operations, he was unsure about a future between Mrs. Fields and the prospective acquirer.[29]

D. Termination of the Agreements

From its inception in March 2004, Shadewell had difficulty paying the running royalties on time to Mrs. Fields. In fact, a payment plan was necessary every quarter that Shadewell was a party to the Agreements.[30] Shadewell's CEO, Tim Bruer, claimed that the late payments resulted from both the undercapitalization of Shadewell and the fact that Shadewell was making substantial investments in developing Mrs. Fields brand products.[31]

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27 PX 1 § 4; PX 2 § 4; PX 3 § 4.

28 Tr. at 622, 624 (Russo).

29 Tr. at 626.

30 *See* Pretrial Order ¶¶ II.16–II.39. The only exception occurred after the initiation of this litigation. *See supra* n.19.

31 Tr. at 310–11.

For each quarter of 2004, the parties successfully negotiated a payment plan for Shadewell's late payment of the running royalties. The negotiation of those plans typically involved Bruer and Michael Ward, Mrs. Fields general counsel.

Shadewell was unable to make its first payment of running royalties due on April 30, 2004 for the first quarter. After the due date, Bruer, in an email to Ward, requested that the parties enter into a payment plan.[32] The parties did agree on a payment schedule, and it was fairly lengthy. It took Shadewell almost five months to pay in full the first quarter of 2004 royalties.[33] Shadewell made the first payment on June 9, 2004 and the final payment on September 28, 2004.[34]

Similarly, Shadewell was unable to pay the second quarter 2004 royalties. Shadewell was then unable to meet the terms of the negotiated payment plan.[35] To induce payment of the second quarter royalties, Mrs. Fields sent a draft termination letter to Shadewell on August 29, 2004, explaining that it would send an official termination letter the following week.[36] The draft termination letter included a provision allowing

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32 Tr. at 400–01.

33 Pretrial Order ¶ 18.

34 *Id.*

35 The second quarter royalties were due by July 31, 2004. The parties entered into a payment plan on August 3 that provided for payment by September 4, 2004. By late August, Shadewell told Mrs. Fields that it could not meet the September 4 deadline. DX 17; Tr. at 412–14.

36 DX 16.

Shadewell to cure the default by paying in full within five days.[37] Upon receipt of the draft termination letter, Shadewell attempted to negotiate another payment plan but was unsuccessful. Mrs. Fields then sent an official termination notice. After Shadewell received that notice, Bruer contacted Russo directly on September 10, 2004 about negotiating another payment plan.[38] Russo testified that he "was very firm and clear about my expectation that we [Mrs. Fields] be paid on time."[39]

Shadewell complied with the terms of this second payment plan. It made its final payment for the second quarter 2004 royalties on November 17, 2004, almost four months after the contract deadline.[40]

The third quarter 2004 royalties totaled $588,635 and were due on October 31, 2004.[41] When that date passed without payment being made, Mrs. Fields contacted Shadewell to find out why it had not paid.[42] Like the previous two quarters, the parties

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37 DX 25.

38 Tr. at 588.

39 Tr. at 591. Russo also testified that "I was clear with him [Bruer] about, you know, my experience and, you know, in franchising and licensing and the expectation that, while he had use of what is one of America's most important and famous brands, that he ought to pay us for it and that I expected to be paid on time. And I also expected him to keep his word when he said that -- you know, when we agreed a payment would be late by ten days that, you know, on that occasion it would be paid in ten days. So I was very clear." Tr. at 592.

40 The parties agreed to defer $100,000 of second quarter royalties to March 1, 2005. Shadewell paid this deferred payment on or about March 17, 2005. Pretrial Order ¶ II.22.

41 Pretrial Order ¶ II.23.

42 DX 34.

entered into a payment plan, but it was shorter in duration. Shadewell finished paying the full amount of the third quarter royalties by November 22, 2004, less than one month after the due date.[43]

As 2004 progressed, Mrs. Fields communicated to Shadewell its concern about the continual late payments. In each consecutive quarter that Shadewell was a party to the Agreements, it paid the royalties closer to the deadline. Further, Mrs. Fields stayed on top of Shadewell, carefully monitoring their payment schedules and making contact whenever it feared that Shadewell was falling behind. In December 2004, Mrs. Fields agreed to amend the Agreements to extend the quarterly deadline an additional month to enable Shadewell to pay on time consistently.[44]

Despite the Amendment, Shadewell was still unable to pay the fourth quarter of 2004 royalties on time. Like the past three quarters, the parties discussed a payment plan. Full payment was made within three weeks of the due date.

In January 2005, Russo met with Shadewell's Chairman, Andrew Richards, and Mrs. Fields Chairman, Pug Winoker, to discuss the relationship between Shadewell and Mrs. Fields. Russo told Richards that the late payments were unacceptable, as they had the potential to force Mrs. Fields to restate its earnings. Specifically, Russo told Richards that restating earnings "would be absolutely unacceptable to our company because no

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[43] Pretrial Order ¶ II.25.

[44] Pretrial Order ¶ II.26; DX 4.

licensee, no matter how big they were, was worth our credibility in the marketplace with our bondholders and our equity owners."[45]

On May 5, 2005, Shadewell informed Mrs. Fields that their royalties for the first quarter of 2005 totaled $490,502.[46] The royalties were due on May 30, 2005, but Shadewell did not pay on time.[47] Unlike with previous quarters, Shadewell did not attempt to negotiate a payment plan for the first quarter 2005 royalties.

Mrs. Fields immediately began to press Shadewell for the money. An email from Lori Largo in accounts receivables at Mrs. Fields to Scott Simon, Shadewell's controller,[48] sent on the morning of May 31, states: "I received your voice mail. Please overnight the $200,000.00 today. We will need the remaining amount to be received in our office no later than June 7, 2005."[49] Shadewell made a $100,000 payment on May 31 and a $200,000 payment on June 1, 2005.[50] On June 13, 2005, Shadewell made an additional payment of $50,000,[51] bringing the total paid to $350,000.

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45 Tr. at 594 (Russo).

46 PX 38. Shadewell owed approximately $15,000 under the 2003 Agreement, $14,000 under the 2001 Agreement and $461,502 under the 2000 Agreement. *Id.*

47 Pretrial Order ¶ II.31.

48 Tr. at 78, 179 (Ward).

49 PX 31.

50 Pretrial Order ¶ II.31.

51 Shadewell's payment of $50,000 was originally returned by Shadewell's bank. Mrs. Fields later re-deposited the check and it cleared. Pretrial Order ¶ II.31.

On July 14, 2005, Mrs. Fields sent Shadewell a Notice and Termination letter. Bruer never attempted to contact Ward about negotiating a payment plan until after Mrs. Fields sent this letter.[52] At trial, Shadewell suggested that the usual negotiations between Bruer and Ward over a payment plan for the first quarter of 2005 did not occur because Ward and others from Mrs. Fields were on vacation. Ward testified at trial, however, that he did not leave for vacation until June 16, more than two weeks after the payment was due, and returned on July 5, 2005.[53]

There were discussions in June and early July between Largo and Simon about when Shadewell would pay off the outstanding balance. These discussions were not negotiations, however. They consisted mainly of Mrs. Fields personnel emphasizing the need for prompt payment and asking when Mrs. Fields was going to receive the royalty payments.[54]

Mrs. Fields's executive committee met on July 12, 2005. Among other things, the committee discussed whether to terminate the Shadewell licenses. According to Russo, some members of the committee wanted to terminate the Agreements immediately, and others felt that Mrs. Fields should give Shadewell another opportunity.[55] At the end of the meeting, Russo concluded that in addition to not paying on time, Shadewell did not share the same fundamental principles about operating and doing business. With the

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52 Tr. at 235 (Ward).

53 Tr. at 235.

54 *See, e.g.*, DX 74.

55 Tr. at 596.

support of Mrs. Fields's senior executives, Russo made the decision to terminate the Agreements.[56] Therefore, he instructed Ward to take the necessary steps to terminate the Agreements.[57] Lauck, Mrs. Fields's representative on Shadewell's board of directors, was present at this meeting.

On July 14, 2005, Ward faxed Shadewell a Notice of Default and Termination (the "Notice of Default and Termination").[58] The Notice of Default and Termination reads, in pertinent part:

> We hereby put you on notice as required pursuant to Section 16(b) of the Existing Agreements that you are in default under Section 5(b) and Section 8(a) of the Existing Agreements . . . in that you have failed to pay the Running Royalty Payments under the Existing Agreements in a timely manner . . . .
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> Specifically, Section 1 of the Amendment provides, "Shadewell shall remit such Running Royalties to MFF no later than 60 days following the end of each calendar quarter covered by the Existing Agreement." The first calendar quarter for 2005 ended on March 31, 2005. The 60-day period for making Running Royalty payment had run as of May 30, 2005.[59]

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56 Tr. at 597 ("I went back to my team and asked, you know, for their commitment to that decision, to make sure that when we left the room they would be absolutely committed to it. And I believe that I received a very solid commitment, even from the folks who initially had said that they didn't think we should terminate.").

57 Tr. at 595–97.

58 DX 83. Although the Notice of Default and Termination is dated July 13, both parties agree that it was not sent to Shadewell until July 14, 2005. Pretrial Order ¶ II.32.

59 DX 83.

Upon receipt of the Notice of Default and Termination, Bruer contacted Ward; they spoke by telephone on the evening of July 14.

What Bruer and Ward agreed to, if anything, during this call is in dispute. Bruer testified that Ward agreed that if Shadewell paid the remaining $140,502 on or before July 21, the default would be cured and Shadewell would no longer be in default as to *any of the three* Agreements.[60] The following day, Bruer sent an email to Ward asking him to confirm in writing that payment in full by July 21, 2005 would cure all the Agreements.[61]

In contrast, Ward denied that there was any such agreement and testified that Bruer's email "was a misstatement of what we had talked about the night before."[62] On July 15, 2005, Ward sent a letter to Bruer (the "July 15 Letter") confirming that the 2003 Agreement could be cured by payment of the remaining balance due to Mrs. Fields by July 21.[63] Ward testified that he sent the July 15 Letter because he told Bruer in their conversation on July 14 that he would confirm in writing what they had discussed. According to Ward, the only cure he and Bruer discussed related to the 2003 Agreement. As recited previously, Bruer claims to have had a different understanding.

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60 Tr. at 347–50.

61 PX 38 ("It is our understanding that sending this remaining $140K no later than 7/21 will remedy this second issue."). Bruer testified that the "second issue" refers to curing the default for all three Agreements. Tr. at 354.

62 Tr. at 141.

63 DX 86.

The July 15 Letter did not conform to the view of the telephone conversation Bruer expressed in his email, but rather espoused a materially different view. While the July 15 Letter could have been more explicit, *i.e.*, it could have spelled out the fact that the 2000 and 2001 Agreements could not be cured by payment of the remaining balance, it did make clear that Shadewell had the ability to cure only the 2003 Agreement.[64] In the Court's opinion, the July 15 Letter could not reasonably be read to mean that Shadewell could effect a cure as to the 2000 and 2001 Agreements.

The record is not clear as to whether Ward faxed the July 15 Letter before or after he received Bruer's email of the same date. For purposes of this decision, it is not necessary to resolve this dispute. If it were, however, the Court would find: (1) that Ward never agreed that a further payment would cure the defaults as to the 2000 and 2001 Agreements; and (2) that Ward did see the email before he sent the July 15 Letter, which was prepared by one of his subordinates. With the benefit of hindsight, Ward testified at his deposition that he believes he would have sent a more direct repudiation of Bruer's email had he seen it before he sent the July 15 Letter. Having considered the evidence and the relevant testimony, the Court finds it more likely than not that Ward simply did a poor job and did not take the time or make the effort to eliminate any possibility of a misunderstanding or, if he saw the email later, to send another, more

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[64] DX 86 ("The Trademark License Agreement *dated March 31, 2003* states that you can cure a default for the failure to pay Running Royalties . . . .") (emphasis added).

direct communication promptly thereafter.[65] Either way, Ward's less than stellar performance provides no basis for finding an agreement along the lines Bruer alleged or for excusing Shadewell's default on the 2000 and 2001 Agreements.

Without any attempt to clear up the apparent conflict in the exchange of correspondence as to what was agreed to during the telephone conversation, Shadewell paid the remaining $140,502 it owed for the first quarter of 2005 on July 21, 2005.[66]

One week later, on July 28, 2005, Shadewell held a telephonic board meeting.[67] Lauck attended. At no time during the meeting did Bruer or anyone else mention the recently received Notice of Default and Termination.[68] Instead, Bruer and the Shadewell board acted as if the Agreements were still in full effect and had never been terminated.

Around the same time, Russo learned (perhaps from Lauck) that Shadewell was acting as if the Agreements had never been terminated.[69] Russo then instructed Ward to send another letter to Shadewell to make certain that "there wasn't any misunderstanding

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65 Ward's testimony on this issue was confusing and equivocal. He also exhibited a non-confrontational style that the Court believes would have made him reticent to send as direct and pointed a letter as others might. At the same time, the Court considers it probative that Ward was under direct orders from Russo to terminate Shadewell and evinced no willingness or intent to act contrary to those orders.

66 Pretrial Order ¶ II.35. To the extent Shadewell contends the July 15 Letter was consistent with its understanding, I find that argument unpersuasive.

67 Tr. at 570.

68 Tr. at 571 (Lauck).

69 Tr. at 618–20 (Russo).

that the licenses had been terminated."[70] Ward drafted this letter on July 27 and sent it to Shadewell on July 28.[71] The letter stated that while the 2003 and 2004 Agreements remained effective, the 2000 and 2001 Agreements would terminate on August 13, 2005, thirty days after the Notice of Default and Termination.[72]

II. ANALYSIS

The Agreements contain choice of law provisions providing for the application of Utah Law.[73] Delaware courts enforce such provisions "so long as the jurisdiction selected bears some material relationship to the transaction" and the law of the foreign jurisdiction is not repugnant to the public policy of Delaware.[74] Here, the principal place of business for Mrs. Fields is Utah. Furthermore, the relevant provisions of Utah contract law are not repugnant to the public policy of Delaware. Accordingly, the Court will apply Utah law.

A. Modification

Shadewell contends that during the telephone call on July 14, 2005, Ward agreed to allow Shadewell to cure the default on all three Agreements by paying the remaining balance within five days. Thus, Shadewell argues, the parties orally modified the

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70 Tr. at 621 (Russo).

71 Tr. at 153 (Ward).

72 PX 44.

73 PX 1 § 22(l); PX 2 § 22(l); PX 3 § 22(l).

74 *J.S. Alberici Constr. Co. v. Mid-West Conveyor Co.*, 750 A.2d 518, 520 (Del. 2000).

contracts. In the alternative, Shadewell makes a promissory estoppel argument: Because Ward did not correct Bruer's belief, as reflected in his July 15 email, that payment in full would cure all three Agreements, the Court should interpret the contract in accordance with Bruer's understanding. Because Shadewell paid the balance within five days, Shadewell claims that it cured the default under all three Agreements.

Mrs. Fields argues that there was no modification, and even if there was, it would be unenforceable for lack of consideration or void under the statute of frauds. Because the Court concludes that no modification occurred, it is not necessary to address Mrs. Fields consideration and statute of frauds arguments.

"[P]arties to a contract may, by mutual consent, modify any or all of a contract."[75] Mutual consent requires the same "meeting of the minds" required to form the contract initially.[76] The party claiming modification bears the burden of showing mutual consent by a preponderance of the evidence.[77] Shadewell failed to meet its burden of proof.

Shadewell has not proven that Ward agreed to allow Shadewell to cure all the defaults by paying in full within five days. Bruer's testimony was quite vague regarding

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75 *Harris v. IES Assoc. Inc.*, 69 P.3d 297, 310 (Utah Ct. App. 2003**)** (citing *Pasker, Gould, Ames & Weaver, Inc. v. Morse*, 887 P.2d 872, 877 (Utah Ct. App. 1994)).

76 *Id.*

77 *Malstrom v. Consol. Theatres, Inc.*, 290 P.2d 689, 691 (Utah 1955) ("This plea of [oral] modification . . . cast upon the defendant the burden of proving it by a preponderance of the evidence."); *Wilson v. Gardner*, 348 P.2d 931, 933 (Utah 1960) (affirming the use of jury instructions that stated that "[T]he burden is upon the party claiming [oral] modifications in the written agreement to prove by a preponderance of the evidence that such modifications, if any, were made.").

the telephone conversation he had with Ward on July 14, 2005. In fact, a careful review of the testimony reveals that Bruer never specifically testified that Ward told him that full payment within five days would effect a cure as to all of the Agreements.[78] Further, Bruer claimed an inability to recall in response to a number of questions at trial, thereby casting doubt upon his credibility.[79]

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[78] Bruer described the conversation as follows:

> I said, "I got your letter. What does it mean? How do we take care of this? By the way, you've got a" -- "something that's inaccurate in it, the statement about not having submitted the royalty report information. We actually had done that. What do we do to cure the issue on the payment" and then -- do you want me to keep going what the conversation. . . . And -- and he said, "Well, when can you get us the remaining" -- I said -- I said, "By the way, do you know we paid $350,000 already? And so we're only talking about the 140,000." And -- and he -- I think he said, "When" -- "when can you get that to us?" And then we sort of went back and forth as to what the right date for that would be. And we picked a date of July 21st. And that was it.

Tr. at 347–48. There is no dispute that Shadewell owed the $140,000. Whether payment of that amount would cure the defaults is a different question.

[79] *See, e.g.*, Tr. at 396–97 (Bruer could not recall negotiating section 22(f) of the Agreements, but remembered discussing the section during his deposition), 494–98 (Bruer could not remember if Simon told him of Mrs. Fields's concern about having to restate its earnings due to Shadewell's late payment). Based in part on Bruer's elusive testimony, the Court finds Ward to be a more credible witness. The Court also finds that Bruer deliberately delayed contacting Mrs. Fields as long as possible concerning the second quarter 2005 royalties in hopes of postponing the establishment of a payment plan. When asked by the Court, Bruer admitted that he knew Shadewell would be unable to pay on time when he received Largo's email on May 26, 2005, five days before the due date. Tr. at 472–73. Yet, Bruer waited until he received the Notice of Default and Termination Letter on July 14 before contacting anyone at Mrs. Fields.

Ward unequivocally testified to the contrary. When asked what he told Bruer about the effect of paying the remaining first quarter 2005 running royalties, Ward stated:

> I said that the 2003 agreement had a five-day cure period and that any payment for the royalties owed under that agreement, that it would be okay. And he asked me if I would put that in a letter, and I said yes, but I would make that clarification. And I told him that, you know, paying 140 does not -- there's no ability to cure the default under the 2000 and the 2001 agreements.[80]

Shadewell relies on Bruer's July 15 email to Ward to support its claim that payment within five days would cure all three Agreements. The email reads, in pertinent part:

> Regarding the second issue, that of the royalty payments, we will send no later than for delivery on Thursday July 21st the remaining balance of $140K in running royalties. . . . It is our understanding that sending this remaining 140K no later than 7/21 will remedy this second issue.[81]

Bruer claims that the "second issue" refers to the cure of all three delinquent payments,[82] but the email is ambiguous on that point. Furthermore, Bruer testified that he requested confirmation from Ward of their alleged oral agreement.[83] Ward's July 15 Letter indicates only that payment by July 21 would cure the default as to the 2003 Agreement. Shadewell apparently contends that it reasonably relied on Bruer's email of the same date and the absence of any explicit repudiation of that email until July 28 for its broader

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80 Tr. at 134–35.

81 PX 38.

82 Tr. at 354–55.

83 Tr. at 525.

interpretation of the July 14 conversation, notwithstanding the inconsistent letter from Ward. The Court finds that contention unpersuasive. In particular, the Court concludes that Bruer could not reasonably have inferred from Ward's letter and the absence of any other contemporaneous reply to Bruer's July 15 email that the 2000 and 2001 Agreements had been modified.

At most, from Shadewell's perspective, the record indicates that the parties simply misunderstood each other. Bruer believed Ward had agreed to allow a cure of all three Agreements, while Ward believed that Bruer understood that only the 2003 Agreement could be cured. Thus, the Court finds there was no meeting of the minds on an oral modification.

Assuming that Bruer understood Ward to say on July 14 that Shadewell could cure the defaults by paying within five days, it was unreasonable for Bruer to continue so believing after he received Ward's July 15 Letter. While Shadewell emphasizes that this letter did not unequivocally state that it could not cure the 2000 and 2001 Agreements, the Court finds nothing in the letter that supports the existence of an agreement by Mrs. Fields that Shadewell could cure the 2000 and 2001 Agreements. The July 15 Letter notes that "[t]he Trademark License Agreement dated March 31, 2003 states that you can cure a default for the failure to pay Running Royalties within five (5) days of receipt of such notice."[84] There is no mention in the letter of a cure provision in the 2000 and 2001 Agreements. Bruer, a sophisticated businessman, should have known from the

[84] DX 86.

contents of the July 15 Letter that he and Ward had different recollections of their phone call. Instead of contacting Ward for clarification or informing him that his July 15 Letter was inconsistent with the telephone call, Bruer kept silent.

B. Mrs. Fields did not Waive its Right to Strict Compliance with the Terms of the Agreements

Shadewell argues that because Mrs. Fields allowed Shadewell to negotiate payment terms for payment of the running royalties for nearly every quarter since the first quarter of 2004, it waived its right to strict compliance with the terms of the Agreements. According to Shadewell, Mrs. Fields now may only terminate after providing Shadewell with notice of the default and a meaningful opportunity to cure such default. In support of its argument, Shadewell relies on *Call v. Timber Lakes Corp.*[85] and *Calhoun v. Universal Credit Co.*[86]

Mrs. Fields contends that Shadewell's reliance on *Call* and *Calhoun* is misplaced. Mrs. Fields claims that it never sat idle when Shadewell paid late and always insisted on negotiating payment plans. Further, Mrs. Fields notes that it attempted to help Shadewell make timely payments by extending the due date for Shadewell's quarterly payments by a month in the December 24, 2004 amendment. Finally, Mrs. Fields points to the "Waiver by Custom or Practice" provision[87] to show that Mrs. Fields never intended to

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85 567 P.2d 1109 (Utah 1977).

86 146 P.2d 284 (Utah 1944).

87 PX 1 § 22(f); PX 2 § 22(f); PX 3 § 22(f).

waive any rights under the Agreements. Mrs. Fields relies on *Living Scriptures, Inc. v. Kudlik*[88] and argues that the licensing agreements in this case are most similar to a lease.

It is well settled that "[a] waiver is the intentional relinquishment of a known right. To constitute waiver, there must be [1] an existing right, benefit or advantage, [2] a knowledge of its existence, and [3] an intention to relinquish it."[89] Waiver can be express or implied.[90] Silence, however, does not constitute waiver "unless there is some duty or obligation to speak."[91] On the other hand, the presence of a nonwaiver provision, such as Section 22(f), is not dispositive. A nonwaiver provision is simply one factor for the court to consider in determining whether waiver has occurred.[92] To "ensure[] that waiver [will] not be found from any particular set of facts unless it was clearly intended," Utah courts require that waivers be distinctly made.[93] If a party waives strict compliance with the terms of an agreement, that party cannot terminate the agreement without providing notice of default and an opportunity to cure.[94] The question here is whether Mrs. Fields waived strict compliance.

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88 890 P.2d 7 (Utah Ct. App. 1995).

89 *Soter's, Inc. v. Deseret Fed. Sav. & Loan Ass'n*, 857 P.2d 935, 942 (Utah 1993).

90 *Id.*

91 *Id.* (quoting *Plateau Mining Co. v. Utah Div. of State Lands & Forestry*, 802 P.2d 720, 730 (Utah 1990)).

92 *Living Scriptures*, 890 P.2d at 10 n.5.

93 *Soter's Inc.*, 857 P.2d at 940.

94 *Calhoun*, 146 P.2d at 287.

Based on the evidence and relevant testimony, the Court finds that Mrs. Fields did not waive its right to strict compliance with the terms of the Agreements for several reasons. First, each agreement contains a nonwaiver provision. Bruer not only knew of the existence of the provision, but also was involved in negotiating the Agreements.[95] While this factor is not dispositive, the Court considers it probative in determining Mrs. Fields's intent.

Second, Mrs. Fields never sat silent while Shadewell paid late. In fact, every time Shadewell failed to pay on time, the lower level employees of Mrs. Fields would ask for immediate payment and Shadewell would seek to negotiate a payment plan. Reminding a contracting party that its payment is due and then negotiating a payment plan is different from consistently acquiescing to late payments. As the court stated in *Living Scriptures*, discussed *infra*, such behavior does not demonstrate an intentional relinquishment of a right, but rather "a consistent attempt to resolve the dispute and reach an agreement concerning the late rental payments without evicting [the tenant] at the first sign of trouble."[96]

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95 Tr. at 389–93 (Bruer).

96 *Living Scriptures*, 890 P.2d at 10. Shadewell did not seek a payment plan for the first quarter 2005 royalties. Shadewell attributes this to the vacation plans of Ward and other Mrs. Fields' employees. Ward's vacation, however, did not begin until June 16, more than two weeks after the payments were due. Tr. at 235. Furthermore, it is undisputed that Bruer did not contact anyone at Mrs. Fields concerning the running royalties until he received the Notice of Default and Termination on July 14, 2005. By that time, he had to act to preserve any hope of resolving the matter short of termination.

It is worth noting that Mrs. Fields did not place Shadewell in default immediately after Shadewell missed the due date. Rather, the Notice of Default and Termination was sent to Shadewell approximately six weeks after the first quarter running royalties were due. Mrs. Fields sent the notice after many attempts to obtain payment.[97] It was not a sudden termination as in the cases cited by Shadewell.[98]

In addition, the record demonstrates that Mrs. Fields began to lose patience with Shadewell's late payments long before the termination. In September 2004, Russo spoke directly with Bruer and expressed his frustration with Shadewell's inability to pay in a timely fashion.[99] That same month, Mrs. Fields placed Shadewell in default for failure to timely pay the running royalties.[100] Further, in January 2005, Russo met with the Chairmen of Shadewell and Mrs. Fields and unequivocally told them that late payments are "absolutely unacceptable to our company because no licensee, no matter how big they were, was worth our credibility in the marketplace with our bondholders and our equity

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97 Largo began questioning Shadewell about the running royalties days before the royalties were actually due. On May 26, Largo emailed Simon of Shadewell and wrote "I just want to be sure that we will receive the first quarter royalty on Tuesday, May 31." DX 59. On May 31, she informed Shadewell that Mrs. Fields needed the money no later that June 7. DX 61. Numerous emails between Mrs. Fields and Shadewell ensued.

98 Communications continued right up until the time Mrs. Fields terminated the Agreements. Mrs. Fields sent Shadewell an email on July 8, 2005 asking when the remainder would be paid. DX 82. After receiving no response, Mrs. Fields re-sent the email three days later. *Id.* Shadewell's Simon responded "[a]t the moment, I don't have a feel for when we'll pay the remainder of Q1 until I have a discussion with Tim Bruer to get his input on timing of final payment." *Id.*

99 Tr. at 601–02.

100 DX 25.

owners."[101] Similarly, Bruer was informed on June 8, 2005, just over a month before Mrs. Fields terminated the Agreements, that Russo personally was watching Shadewell's payment habits.[102] This evidence shows not only that Mrs. Fields had grown impatient with Shadewell's delinquent payments, but also that Shadewell knew it.

The *Call*, *Calhoun*, and *Living Scriptures* cases are all distinguishable from this case. *Call* dealt with a forfeiture provision in a land installation contract. In *Call*, the plaintiff had made several payments late and missed several other payments entirely. The defendant allowed the plaintiff to make up the missed payments. Thereafter, the defendant suddenly notified the plaintiff that it was in arrears in the amount of $1,558.90 and if that amount was not paid in full within ten days, the defendant would terminate the contract. The plaintiff attempted to pay the full amount of arrearages twelve days after the defendant's notice required. The defendant refused to accept the payment and, instead, demanded full payment of the contract price. The court held that after allowing the plaintiff to pay late, and sometimes not at all, for approximately three years, the defendant could not suddenly require the plaintiff to pay the arrears within ten days. The court stated that it would only interfere with the parties' right to contract and refuse to enforce a forfeiture provision when "the forfeiture would be so grossly excessive as to be

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101 Tr. at 594.

102 DX 62 (email to Bruer from Diane Wood, a Shadewell employee, stating that "Mark [McBride of Mrs. Fields] receives a lot of heat from the CEO when our payments are late"). Simon was also informed of Russo's involvement. DX 71.

entirely disproportionate to any possible loss that might have been contemplated, so that to enforce it would shock the conscience."[103]

Calhoun dealt with an express waiver. The purchaser of an automobile had fallen behind on payments. An agent of the car company told the purchaser on February 4 that he could have some time to sell the car in order to capture his equity in it. On February 16, without notice, the agent repossessed the car. The court held that the car company, through its agent, expressly waived the right to strict compliance by allowing the plaintiff time to sell the car. "[T]he vendor waived default and was therefore under the necessity of giving notice and an opportunity for payment before a forfeiture and repossession could be claimed."[104]

Living Scriptures involved the termination of a lease. The tenant did not pay property taxes for 1991 and 1992 and fell two months behind in rent. The landlord and tenant subsequently entered into a Memorandum of Understanding whereby the tenant agreed to cure the existing defaults and pay on time. The tenant then paid late the next three months and failed to pay at all the following two months. The landlord demanded payment in full and gave the tenant numerous opportunities to cure the defaults by paying in full, but the tenant only paid one month's rent. After the tenant failed to bring the payments up to date, the landlord terminated the agreement. The court held that the landlord did not waive strict performance by accepting late payments. Rather, the court

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103 *Call*, 567 P.2d at 1109.

104 *Calhoun*, 146 P.2d at 287.

characterized the landlord's behavior as "a consistent attempt to resolve the dispute and reach an agreement concerning the late rental payments without evicting [the tenant] at the first sign of trouble."[105]

Neither *Call* nor *Calhoun* or *Living Scriptures* is on all fours with the facts of this case. *Call* and *Calhoun* involved situations where the plaintiffs stood to lose an equity interest. *Living Scriptures*, on the other hand, involved simply a lease. The present case falls somewhere between those two paradigms. While Shadewell does not have any equity in the Agreements, it did make some substantial up front expenditures including fees and product development costs. In the end, however, the cited cases do not support a different conclusion. On the facts of this case, the Court concludes that Shadewell failed to prove the elements of waiver. Thus, the Court finds that Mrs. Fields did not waive its right to terminate the Agreements.

C. The Payments Should be Allocated Ratably Among the Three Agreements

As of July 14, 2005, the date of the Notice of Default and Termination, Shadewell had paid $350,000 of the $490,000 in running royalties that were due on May 30, 2005. Mrs. Fields applied the $350,000 ratably across all three Agreements. Shadewell argues that the amount paid should have been allocated in such a way as to satisfy, in full, the 2001 and 2003 Agreements. Accordingly, the argument goes, Shadewell was only in default with respect to the 2000 Agreement.

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105 *Living Scriptures*, 890 P.2d at 10.

Shadewell argues that the payments should be applied to the Agreements consistent with the law's "notions of justice,"[106] and that since "equity abhors forfeiture," this Court should allocate the $350,000 in such a manner as to satisfy the 2001 and 2003 Agreements running royalties in full.

The general rule of payment allocation is that if neither the creditor nor the debtor state how the payment should be allocated, "the law will apply the payments, according to its own notions of justice."[107] The party should, however, designate a specific allocation before trial.[108] In a case where neither party has designated a specific allocation of payments, it is entirely consistent with "notions of justice" to follow the approach outlined by the Restatement (Second) of Contracts § 260.[109]

Section 260 of the Restatement provides a four level hierarchy for applying payments in the event the parties have not contracted or specified any specific application of payments.[110] Payments should be allocated in the following order. First, the payments should be applied to a debt that the debtor is under a duty to a third person to pay immediately. Second, any payments are applied to overdue interest before principal and unsecured debt before secured debt. Third, the oldest matured debt should be paid first.

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106 *Pickering v. Day*, 1866 WL 1046 (Del. Ch. 1866).

107 *United States v. Kirkpatrick*, 22 U.S. (1 Wheat.) 720, 737 (1824).

108 *See id.* ("It is certainly too late for either party to claim a right to make an appropriation, after the controversy has arisen, and *a fortiori* at the time of trial.").

109 *Lee v. Yano*, 997 P.2d 68, 78 (Haw. Ct. App. 2000) (concluding that "the law's notions of justice are stated in Restatement (Second) of Contracts § 260").

110 Restatement (Second) of Contracts § 260 (1981).

Finally, if the first three are inapplicable, the payments should be applied pro rata among debts of the same maturity. Section 260, particularly the final tier, appears to be the method of payment allocation most accepted by courts.[111]

The payments in this case must be applied ratably over the Agreements for several reasons. First, all three Agreements lack a provision providing for a specific allocation of payments. Second, Shadewell never requested a specific allocation of the payments. Third, Shadewell commingled the royalties for the 2000 and 2001 Agreements in their royalty reports to Mrs. Fields. For example, in Shadewell's royalty report for the first quarter 2005, Shadewell reported only the total royalties due under the 2000 and 2001 Agreements combined.[112] There is no way to determine how much of the royalties came from the 2000 or 2001 Agreements individually. Such commingling suggests that Shadewell had no expectation before this litigation that the payments would be allocated in any specific order.

While Shadewell correctly points out that equity abhors a forfeiture, application of that maxim is not appropriate where there are "equitable circumstances which would make it unjust to permit a defaulting party to breach the contract and to walk away with impunity despite whatever damages the non-defaulting party may have suffered."[113] In

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111 Williston on Contracts § 72:17 (4th ed.) ("[I]t is the rule in most jurisdictions that the interest of the creditor is preferred when there are no countervailing equities interposed in favor of the debtor).

112 PX 38.

113 *Wilkins v. Birnbaum*, 278 A.2d 829, 830 (Del. 1971).

those situations, "equity is being done between the parties by making the non-defaulter whole from damages suffered as a result of the breach."[114]

In this case, Mrs. Fields seeks to terminate its relationship with Shadewell under the 2001 Agreement based on Shadewell's failure to pay its royalties when due.[115] The facts demonstrated that Mrs. Fields made reasonable efforts to accommodate Shadewell's difficulties in making timely payments. Nevertheless, the problem persisted. Having never requested a specific allocation before, Shadewell now urges the Court to order an allocation that results in full payment of the royalties due under the 2001 Agreement. Acceptance of Shadewell's argument would compel Mrs. Fields to continue to license Shadewell against its wishes. The only counterbalancing equities in Shadewell's favor are (1) the substantial upfront investment its predecessor made in the 2001 Agreement and (2) the relatively small amount of royalties due under the 2001 Agreement ($14,000) compared to the 2000 Agreement ($461,502). On the latter point, the Court considers it significant that Shadewell did not break out the two separate amounts in its quarterly royalty report to Mrs. Fields. Regarding the upfront investment, I note that the investment was made approximately four years before the purported termination. More importantly, Shadewell did not acquire its rights in the Agreement until 2004. Because Shadewell presented no evidence as to its own investment in the 2001 Agreement, I do

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114 *Id.*

115 Allocation as to the 2003 Agreement is not relevant because that Agreement included a cure provision and the parties agree that any default as to the 2003 Agreement was cured.

not consider its predecessor's upfront investment important in terms of the allocation issue. Thus, in the circumstances of this case and based on the general rule in Section 260, the Court concludes that the equities and notions of justice favor a pro rata allocation among the three Agreements.

Accordingly, the Court declines to order Mrs. Fields to alter its allocation of the payments ratably across the Agreements.

D. Mrs. Fields Gave Proper Notice of Default and Termination

Section 16(b)(i) of the 2000 and 2001 Agreements allows Mrs. Fields to terminate the agreements for a failure to pay the running royalties thirty days after providing notice to Shadewell. Shadewell argues that Mrs. Fields did not give proper notice of the default and termination as required by Section 16(b) of the Agreements.[116]

Mrs. Fields's July 14 Notice of Default and Termination is a valid notice of termination. The document was faxed to Bruer with "Notice of Default" in the "re:" line of the fax cover sheet.[117] The top of the Notice read "*****NOTICE OF DEFAULT AND TERMINATION*****." Furthermore, the first paragraph states "[w]e hereby put you on notice as required pursuant to Section 16(b) of the Existing Agreements . . . ." Section 16 is the termination provision of the Agreements.

Bruer is a sophisticated businessman who should have understood that the letter put Shadewell on notice of their default and termination. On cross-examination, he

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116 Pl.'s Opening Post-Trial Br. at 40.

117 DX 83.

admitted that he understood the meaning of the Notice of Default and Termination.[118] This understanding explains why he immediately contacted Ward after receiving it to try to work something out.

III. CONCLUSION

For the reasons stated, I find that the parties did not modify the 2000 and 2001 Agreements to allow for a cure provision. Additionally, Mrs. Fields did not waive its right to strict compliance with the terms of the Agreements. Further, because there is no evidence that the parties intended the payments to be applied in any specific fashion, they must be allocated pro rata across the three Agreements. Finally, Mrs. Fields Notice of Default and Termination was proper.

Plaintiff Shadewell's claims for declaratory judgment, specific performance and damages are denied and judgment is granted in favor of Defendant, Mrs. Fields Franchising, LLC.[119]

IT IS SO ORDERED.

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118 Tr. at 505.

119 Mrs. Fields is entitled to its costs as the prevailing party pursuant to Court of Chancery Rule 54(d).