O

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

IT'S JUST LUNCH INTERNATIONAL LLC, a Nevada Corporation,

Plaintiff,

v.

ISLAND PARK ENTERPRISE GROUP, INC., a New York Corporation,

Defendants.

ISLAND PARK ENTERPRISE GROUP, INC., a New York corporation, and JOANNE BLOOMFIELD, an individual,

Counterclaimants,

v.

IT'S JUST LUNCH INTERNATIONAL, LLC, a Nevada limited liability company, DANIEL DOLAN, an individual, and IRENE LACOTA, an individual,

Counterdefendants.

Case No. EDCV 08-367-VAP (JCRx)

[Motion filed on August 20, 2008]

ORDER GRANTING IN PART AND DENYING IN PART COUNTERDEFENDANTS' MOTION TO DISMISS

Counterdefendants' Motion to Dismiss came before the Court for hearing on September 15, 2008. After reviewing and considering all papers filed in support of, and in opposition to, the Motion, as well as the arguments advanced by counsel at the hearing, the Court GRANTS IN PART Counterdefendants' Motion to Dismiss.

I. BACKGROUND

Plaintiff It's Just Lunch International, LLC ("Plaintiff" or "IJL") filed this action. On April 17, 2008, Defendant Island Park Enterprise Group, Inc. ("Island Park") filed a Counterclaim ("Countercl.").

After various amendments, the pleadings now stand in the following position: IJL, the sole named plaintiff, brings suit against Island Park and Joanne Bloomfield ("Bloomfield") as Defendants. Island Park and Bloomfield, who are referred to collectively here as "Counterclaimants," have filed a counterclaim against IJL, Daniel Dolan, and Irene LaCota, collectively referred to here as "IJL." The Complaint alleges Defendant and franchisee Island Park failed to pay required franchise fees and otherwise perform under two franchise agreements with Plaintiff, franchisor It's Just Lunch.

On August 20, 2008, IJL filed a Motion to Dismiss ("Mot.") the fourth claim (violation of California and New York franchise practice acts) and the seventh claim (California Business and Professions Code § 17200) of the First Amended Counterclaim. IJL also filed a supporting Memorandum of Points and Authorities. ("IJL Mem. P. & A.") Counterclaimants filed Opposition to the Motion to Dismiss on September 2, 2008. ("Opp'n".) IJL filed a Reply in Support of the Motion to Dismiss on September 8, 2008. ("Reply".)

II. LEGAL STANDARD

Under Rule 12(b)(6), a party may bring a motion to dismiss for failure to state a claim upon which relief can be granted. As a general matter, the Federal Rules require only that a plaintiff provide "'a short and plain statement of the claim' that will give the defendant fair notice of what the plaintiff's claim is and the grounds upon which it rests." Conley v. Gibson, 355 U.S. 41, 47 (1957) (quoting Fed. R. Civ. P. 8(a)(2)); Bell Atlantic Corp. v. Twombly, 550 U.S. __, 127 S. Ct. 1955, 1964 (2007). In addition, the Court must accept all material allegations in the complaint -- as well as any reasonable inferences to be drawn from them -- as true. See Doe v. United States, 419 F.3d 1058, 1062 (9th Cir. 2005); ARC Ecology v. U.S. Dep't of Air Force, 411 F.3d 1092, 1096 (9th Cir. 2005).

"While a complaint attacked by a Rule 12(b)(6) motion to dismiss does not need detailed factual allegations, a plaintiff's obligation to provide the 'grounds' of his 'entitlement to relief' requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do." Bell Atlantic, 127 S. Ct. at 1964-65 (citations omitted). Rather, the allegations in the complaint "must be enough to raise a right to relief above the speculative level." Id. at 1965.

Although the scope of review is limited to the contents of the complaint, the Court may also consider exhibits submitted with the complaint, Hal Roach Studios, Inc. v. Richard Feiner & Co., 896 F.2d 1542, 1555 n.19 (9th Cir. 1990), and "take judicial notice of matters of public record outside the pleadings," Mir v. Little Co. of Mary Hosp., 844 F.2d 646, 649 (9th Cir. 1988).

III. DISCUSSION

This dispute involves a franchise agreement with a choice of law provision requiring application of Nevada law. (IJL Mem. P. & A. 2.) IJL urges enforcement of the choice of law provision and asserts that Counterclaimants fail to state a claim upon which relief can be granted under Nevada law, or, if the choice of law provision is not enforced, under California law. (IJL Mem. P. & A. 2-3.)

Counterclaimants argue (1) the choice of law provision should not be enforced, and (2) they state claims under California and New York law. (Opp'n 5, 14.)

A. Choice of Law

Both parties agree that California choice of law analysis should govern the enforcement of the choice of law provision. (IJL Mem. P. & A. 8; Opp'n 5-6.) California uses the test set forth in Nedlloyd Lines B.V. v. Superior Court to determine whether to enforce a choice of law provision. 3 Cal. 4th 459 (1992). This test draws heavily on section 187 of the Restatement Second of Conflict of Laws ("Restatement"). Id. at 464-66.

Under Nedlloyd, California will apply the law indicated by the choice of law provision where: "[1] the chosen state has a substantial relationship to the parties or their transaction," or where "[2] there is any other reasonable basis for the parties' choice of law." Id. at 466. "If neither of these tests is met, that is the end of the inquiry, and the court need not enforce the parties' choice of law." Id. at 466.

Where either test is met, the court proceeds to the second step and "determine[s] whether the chosen state's

law is contrary to a fundamental policy of California." Id. at 466. Once the party who seeks application of the choice of law provision demonstrates a substantial relationship, the party who would avoid the choice of law provision bears the burden of showing that the California law embodies a fundamental policy. See id. at 471.

Where "there is a fundamental conflict with California law," the court proceeds to the third step and "determine[s] whether California has a materially greater interest than the chosen state in the determination of the particular issue. If California has a materially greater interest than the chosen state, the choice of law shall not be enforced, for the obvious reason that in such circumstance we will decline to enforce a law contrary to this state's fundamental policy." Id. at 466 (internal citations and quotations omitted).

1. Substantial Relationship

Applying the Nedlloyd test here, the court must first determine "whether the chosen state has a substantial relationship to the parties or their transaction . . . ." Nedlloyd, 3 Cal. 4th at 466. This requirement is easily satisfied: Plaintiff has a substantial relationship with Nevada because IJL is a Nevada limited liability company. (Countercl. ¶ 3; see Nedlloyd, 3 Cal. 4th at 467.)

2. Fundamental Policy

As a substantial relationship exists, the court next "determine[s] whether the chosen state's law is contrary to a *fundamental* policy of California" or that of a third state. Id. at 466, 467 n.5. Where enforcement of the choice of law provision would run counter to a fundamental policy of California or a third state, then the court must refuse to enforce the choice of law provision if it finds that "California has a 'materially greater interest than the chosen state in the determination of a particular issue . . . .'" Id. at 466.

There is no bright-line definition of a "fundamental policy." Restatement § 187 comment g. A fundamental policy must be "substantive," and "may be embodied in a statute which makes one or more kinds of contracts illegal or which is designed to protect a person against the oppressive use of superior bargaining power." Id.

Here Counterclaimants' fourth claim is based on the California Franchise Investment Law ("CFIL"), or, in the alternative, on the New York Franchise Sales Act; their seventh claim is based on California Business and Professions Code section 17200. (Countercl. ¶ 72, 75, 88-93.) The CFIL has been found to embody a fundamental California policy, while the Courts have split over the question of whether section 17200 does.

The CFIL protects franchisees against franchisors who may have superior bargaining power. See Cal. Corp. Code § 31001 (CFIL enacted to address losses suffered by franchisees due to franchisor failure to provide complete information); Restatement comment g (fundamental policies may "protect a person against the oppressive use of superior bargaining power"). The California legislature described the provisions and intent of the CFIL as follows:

> It is the intent of this law to provide each prospective franchisee with the information necessary to make an intelligent decision regarding franchises being offered. Further, it is the intent of this law to prohibit the sale of franchises where the sale would lead to fraud or a likelihood that the franchisor's promises would not be fulfilled, and to protect the franchisor and franchisee by providing a better understanding of the relationship between the franchisor and franchisee with regard to their business relationship.

Cal. Corp. Code § 31001. At least two courts have read the CFIL as constituting an important protection for franchisees. America Online, Inc. v. Superior Court, 90 Cal. App. 4th 1, 11 (2001) (CFIL "enacted to protect the statute's beneficiaries from deceptive and unfair business practices"); Cottman Transmission Systems LLC v. Kershner, 492 F. Supp. 2d 461, 467-70 (E.D. Pa. 2007).

In Cottman, a Pennsylvania district court found that California and New York's protections of franchisees

"express[ed] a clear policy to provide a heightened degree of protection to prospective franchisees regarding misrepresentations about a franchise system." 492 F. Supp. 2d at 467. Here, the Court finds that the CFIL and New York laws express fundamental policies because Counterclaimants are franchisees who claim the need for protection against a franchisor's misrepresentations and other unfair practices.

The authorities are more conflicting as to whether section 17200 embodies a fundamental policy of California. The language of the statute, which forbids unlawful, unfair or fraudulent business practices, hews close to the spirit of a fundamental policy as described in Restatement 187 comment g. Cal. Bus. & Prof. Code § 17200. The Restatement comment defines a fundamental policy as one that "makes one or more kinds of contracts illegal or which is designed to protect a person against the oppressive use of superior bargaining power." Courts have differed on whether section 17200 embodies a fundamental policy, depending on the underlying violation. See Cardonet, Inc. v. IBM Corp., 2007 WL 518909, *5 (N.D. Cal.)[1] Here Counterclaimants allege

[1]For example, the Cardonet court at *5 noted that section 17200 was found to embody a fundamental California policy when applied to a dispute about a covenant not to compete in Application Group, Inc. v. Hunter Group Inc., 61 Cal. App. 4th 881, 907-08 (1998). In a different dispute cited by the Cardonet court,

(continued...)

that all of IJL's actions constituted illegal trade practices in violation of section 17200. (Countercl. ¶ 90.)

To recap, IJL has demonstrated a substantial relationship with Nevada law, satisfying the first step in the Nedlloyd test. As Counterclaimants seek to avoid application of the choice of law provision, under Nedlloyd, Counterclaimants bear the burden of demonstrating that section 17200 embodies a fundamental policy. See Nedlloyd, 3 Cal. 4th at 471. Neither IJL nor Counterclaimants cite any authority to support their positions on this question. (IJL Mem. P. & A. 9, Reply 6-7; Opp'n 6.) As Counterclaimants bear the burden here, and fail to state with any precision which actions or violations they seek to address with the section 17200 claim, the Court declines to find that section 17200 embodies a fundamental policy in California as used here.

---

[1](...continued)
Nibeel v. McDonald's Corp. 1998 WL 547286 *11 (N.D. Ill. 1998), section 17200 was not found to embody a fundamental policy because the protections afforded by California law and those of the state selected by the choice-of-law clause were similar. Mere differences between California law and that of the state selected by the choice-of-law provision, however, do not transform the California law into one embodying a fundamental policy. MediaMatch v. Lucent, 120 F. Supp. 2d 842, 862 (N.D. Cal. 2000). Counterclaimants' seventh claim cannot neatly be categorized because they allege that all of IJL's actions violate section 17200. (Countercl. ¶ 90.)

In sum, the Court finds that the law on which Counterclaimants base claim four embodies a fundamental California policy, but that the laws on which Counterclaimants base claim seven do not embody such a policy.

3. Materially Greater Interest

Having determined that the California franchise law expresses fundamental policy, the Court considers whether California or New York have materially greater interests than Nevada in enforcing their laws. The Cottman court considered a similar situation and found that California and New York had materially greater interests than did Pennsylvania, the state identified in a choice-of-law clause, in enforcing its laws.

In Cottman, the franchisor was headquartered in Pennsylvania and sought to enforce a choice of law clause requiring application of Pennsylvania law. Cottman, 492 F. Supp. 2d at 467-68. The facts here are similar to those before the Cottman court; Counterdefendant IJL is incorporated in Nevada but resides in California while Counterdefendants Daniel Dolan and Irene LaCota reside in California. (Countercl. ¶¶ 3-5.) Counterclaimants reside in New York. (Id. ¶¶ 1-2.) Nevada's interest here in enforcing its laws, compared to the interests of California and New York, therefore seems equivalent to

Pennsylvania's interest in Cottman. There, the franchisor was headquartered in Pennsylvania and sought to enforce Pennsylvania law; here, the franchisor is incorporated in Nevada and seeks to enforce Nevada law. (Countercl. ¶¶ 2-5); see Cottman, 492 F. Supp. 2d at 467-68.[2] IJL fails to support its position that California and New York do not have materially greater interests in enforcing their laws. (IJL Mem. P. & A. 9; Reply 7.) This Court therefore declines to enforce the choice of law provision as to claim four.[3]

B. Fourth Claim

IJL argues Counterclaimants' claim under the CFIL fails because the franchise was located in New York, not California, and California Corporations Code section 31105 therefore bars it. (IJL Mem. P. & A. 4; Cal. Corp.

---

[2]"There is no franchise disclosure law in Nevada, and, thus, to enforce the choice of law provision in this case would defeat the strong fundamental policy of California's law." Cottman, 492 F. Supp. 2d at 468 citing Chong v. Friedman, 2005 WL *4 (Cal. Ct. App.) (unpublished).

[3]Other courts have refused to enforce the same choice of law provision using different reasoning. See Order Denying Counterdefendants' Motion to Dismiss, Mar. 8, 2007 (It's Just Lunch Int'l LLC v. Nichols, Case No. ED CV 06-01127-SGL); It's Just Lunch Int'l LLC v. Polar Bear Inc., 2004 WL 3406117 (unpublished). These authorities read Restatement section 187 to allow an allegation of fraud regarding the contract *as a whole* to prevent enforcement of the choice of law claim. This Court reads Restatement section 187 to require an allegation of fraud regarding the choice of law claim itself to obtain the same effect. As Counterclaimants do not allege fraud in the inclusion of the choice of law claim, (see Counterclaim ¶¶ 58-66), the choice of law analysis above is necessary.

Code § 31105.) Section 31105 of the California Corporations Code provides:

> Any offer, sale, or other transfer of a franchise, or any interest in a franchise, to a resident of another state or any territory or foreign country, shall be exempted from the provisions of Chapter 2 (commencing with Section 31110) of this part, if all locations from which sales, leases or other transactions between the franchised business and its customers are made, or goods or services are distributed, are physically located outside this state.

Counterclaimants' franchise is located out-of-state and Counterclaimants allege claims under section 31110 and 31111 in their fourth claim. (Countercl. ¶¶ 73-74.) Thus, on its face, section 31105 appears to require dismissal of the fourth claim. A closer reading of section 31105, however, reveals that such a superficial reading of the statute is flawed.

Section 31105 only precludes claims under Part 2, Chapter 2, of the California Corporations Code. Counterclaimants, however, rely on sections *outside* of Part 2, Chapter 2, including sections 31201 and 31220. (Countercl. ¶ 77.) Accordingly, insofar as IJL relies on the provisions of section 31105, the dismissal of Counterclaimants' fourth claim is unwarranted.

Finally, IJL contends the Court should dismiss the CFIL claim on the basis of the parol evidence rule. (IJL

Mem. P. & Am. 5-6.) According to IJL, the Franchise Agreement signed by Counterclaimants contains an enforceable integration clause (Compl. Ex. 1 ¶ 19(f); Ex. 2 ¶ 19(f)), and application of the parol evidence rule will bar the evidence necessary to sustain Counterclaimants' allegations of violations of the CFIL.

This argument lacks merit. Counterclaimants have alleged that IJL made unregistered earnings claims, including fraudulent statements, in connection with offering and selling of a franchise, and that this violated franchise laws. (Countercl. ¶¶ 71, 73-74.) The fourth claim, which addresses franchise laws, incorporates the paragraphs of the second claim (for fraud and deceit). (Countercl. ¶¶ 71-72.) The second claim alleges that It's Just Lunch and Dolan made fraudulent statements orally and/or in writing about the actual or potential level of income or sales for franchise locations before the franchise agreements were signed. (Countercl. ¶¶ 58-60, 74.) These statements include that certain locations would be profitable, that the franchise system as a whole was profitable, and that a location had never been closed. (Countercl. ¶¶ 58-66, 71-72.) Read together, the Counterclaim alleges that IJL made specific fraudulent oral statements about earnings in conjunction with the offer and sale of a franchise.

Defendants rely on the parol evidence rule to compel dismissal of the seventh claim. The rule barring reliance on parol evidence when the parties enter into a contract with an integration clause does not apply where fraud is alleged sufficiently. See Cal. Code Civ. P. § 1856(g); see also Polar Bear, WL 3406117. Here, as discussed above, Counterclaimants have alleged fraud in connection with the sale of franchises. The Court now turns to whether those allegations were made with sufficient detail.

Fraud allegations must "be specific enough to give defendants notice of the particular misconduct so that they can defend against the charge and not just deny that they have done anything wrong." Vess v. Ciba-Geigy Corp. USA, 317 F.3d 1097, 1106 (9th Cir. 2003) (internal quotations omitted). To meet this standard, the pleading must allege "the who, what, when, where, and how of the misconduct charged." Id. (citations and quotations omitted). A plaintiff alleging fraud under state law before a federal court must plead with sufficient particularity to satisfy Fed. R. Civ. P. 9(b). Id. at 1103. A plaintiff must set forth "what is false or misleading about a statement and why it is false." Id. at 1106 (citations and quotations omitted). Counterclaimants have met this standard because they have identified who (IJL and Dolan), when (prior to the

franchise agreements), how (over the telephone and face to face), and which specific fraudulent statements were made in conjunction with the sale of a franchise. (See Countercl. ¶¶ 59-60, 71-74.) They have also shown what is false about these statements by giving the true facts about the franchise system at paragraph 60 of the Counterclaim.

C. Seventh Claim

The seventh claim is based on California Business and Professions Code section 17200 and alleges IJL engaged in illegal, fraudulent, and unfair business practices in connection with its dealings with its franchisees. (Countercl. ¶¶ 88-93.) Defendants' primary basis for arguing that the seventh claim should be dismissed is its contention that Nevada law governs the dispute between the parties. As the court enforces the choice of law clause as to section 17200, it grants the Motion to Dismiss the seventh claim, without leave to amend.

IV. CONCLUSION

For the reasons set forth above, the Court denies the Motion as to fourth claim and grants the Motion as to the seventh claim, without leave to amend.

Dated: October 21, 2008

Virginia A. Phillips

VIRGINIA A. PHILLIPS
United States District Judge