

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

SALADWORKS, INC. :
 :
 v. : 05-CV-1928
 :
 MI HO NO :

MEMORANDUM AND ORDER

Norma L. Shapiro, S.J.

July 5, 2005

Plaintiff Saladworks, Inc. ("Saladworks") in this action against its franchisee, Mi Ho No ("Mr. No"), alleges fraud, breach of the franchise agreement, and violations of the Lanham Act, 15 U.S.C. §§ 1114, 1125(a). Saladworks filed a complaint and moved for a preliminary injunction requesting the court to order expedited discovery and effectively terminate Mr. No's franchise. The court granted expedited discovery and held a hearing on the remainder of the preliminary injunction on May 19, 2005.

On May 23, 2005, Saladworks filed an amended complaint and second motion for a preliminary injunction, titled "Emergency Motion for Entry Pursuant to Paragraph XVI.E of the Franchise Agreement", ordering Mr. No to allow Saladworks to enter and exercise complete authority over the business to correct breaches of the franchise agreement regarding health and safety standards. Because of concerns for public safety and the potential for irreparable injury to Saladworks' trademarks and reputation, the

court granted an injunction allowing Saladworks to enter and take control of the business for 45 days while Mr. No retained ownership. See *Saladworks, Inc. v. Ho No*, No. 05-CV-1928, 2005 WL 1417096 (E.D. Pa. June 15, 2005). Now before the court is plaintiff's first motion for a preliminary injunction to enjoin Mr. No from holding himself out as the operator of an authorized Saladworks restaurant, infringing on the Saladworks trademarks, and to order Mr. No to comply with the post-termination provision in the franchise agreement.

The court makes the following findings of fact and conclusions of law under Federal Rule of Civil Procedure 52(a).

Findings of Fact

1. Saladworks is a corporation organized under the laws of the State of New Jersey, with its principal place of business at Eight Tower Bridge, Suite 225, 161 Washington Street, Conshohocken, Pennsylvania.

2. Saladworks, franchising more than 65 Saladworks restaurants in the Delaware Valley, allows franchisees to use its exclusive trademarks, service marks, trade name, and trade dress.

3. Saladworks employs and advertises throughout the Delaware Valley certain trademarks and service marks ("Saladworks Marks") identifying the source, origin, and sponsorship of its facilities, products and services. All right, title, and interest to the Saladworks Marks and the design, decor, and image

of the Saladworks restaurants are vested solely in Saladworks.

4. Mr. No, an individual residing in Pennsylvania, is a franchisee of a Saladworks restaurant at 3728 Spruce Street in Philadelphia ("the Restaurant"). Mr. No also subleases the premises from Saladworks.

5. There is subject matter jurisdiction under 28 U.S.C. § 1331, based on 15 U.S.C. § 1121, for the claims arising under the Lanham Act, 15 U.S.C. § 1114, and § 1125(a). The court exercises supplemental jurisdiction over all state law claims under 28 U.S.C. § 1367.

6. The court has personal jurisdiction over the parties, and venue is proper under 28 U.S.C. § 1391(b).

7. On February 27, 2004, Saladworks entered into a franchise agreement ("the Franchise Agreement") with Mr. No for the operation of the Restaurant. The Franchise Agreement granted Mr. No a license to use the Saladworks Marks in the operation of the restaurant. Plaintiff's Exhibit P-1.

8. Mr. No purchased the franchise from the prior franchisee, Hashad Vyas, for \$200,000 through a Transfer of Franchise Agreement. Saladworks approved the transfer and received a transfer fee of \$17,500. Plaintiff's Exhibit P-3.

9. Contemporaneously with the Franchise Agreement, Mr. No entered into an agreement to sublease the Restaurant premises from Saladworks, the sublandlord and lessee from the owner, the

University of Pennsylvania. Plaintiff's Exhibit P-2.

10. Saladworks first filed a complaint together with a motion for a preliminary injunction and expedited discovery on April 26, 2005 (Doc. No. 2).

11. Saladworks also filed an amended complaint for injunction and damages (Doc. No. 11) on May 23, 2005.

12. After a hearing on the first motion for a preliminary injunction, while a decision was pending, Saladworks filed a second motion for preliminary injunction, titled "Emergency Motion for Entry Pursuant to Paragraph XVI.E of the Franchise Agreement" (Doc. No. 10), on May 23, 2005.

13. Defendant and counsel were served with a copy of the summons and complaint, both motions for preliminary injunctions, and supporting affidavits.

14. The second motion for preliminary injunction sought to allow Saladworks to enter and exercise complete authority over the business on an interim basis under a provision in the Franchise Agreement, while Mr. No would retain ownership of the business. The court granted the second motion for preliminary injunction on June 15, 2005.

15. The term of the Franchise Agreement and the sublease extend from February 27, 2004 to December 31, 2006. The Franchise Agreement and sublease are valid and binding on the parties; Mr. No currently has the right to use the Saladworks

name and Saladworks Marks.

16. The Franchise Agreement defines certain acts as events of default. For certain defaults, the Franchise Agreement requires Saladworks to give the franchisee notice of the default and thirty days to cure the default before termination of the Franchise Agreement based on the default. Franchise Agreement, Paragraph XVI.A.

17. The Franchise Agreement requires the franchisee to pay to Saladworks a weekly Continuing Services and Royalty Fee equal to five percent of gross sales. Franchise Agreement, Paragraph X.A.

18. The Franchise Agreement requires Mr. No to contribute three percent of gross sales to an Advertising and Development Fund. Franchise Agreement, Paragraph IX.B.

19. The Franchise Agreement requires Mr. No to maintain and preserve for a period of three years full, complete, and accurate books, records, and accounts in accordance with a standard accounting system prescribed by Saladworks. Franchise Agreement, Paragraph XI.A.

20. The Franchise Agreement requires Mr. No to supply to Saladworks on or before the fifteenth day after the end of each calendar quarter an activity report, a profit and loss statement, a balance for the last preceding calendar quarter, and weekly gross sales for the preceding calendar week. Franchise

Agreement, Paragraph XI.B.

21. The franchisee's failure or refusal to comply with any provision of the Franchise Agreement, or any mandatory specification, standard, or operating procedure prescribed in the Manual or otherwise in writing, followed by the failure to correct such failure within thirty days (or failure to provide proof acceptable to Saladworks that the franchisee has made all reasonable efforts to correct such failure and will continue to do so until a cure is effected, if such failure cannot reasonably be corrected within thirty days) after written notice of such failure to comply is delivered to the franchisee is an act of default. Franchise Agreement, Paragraph XVI.C.2.

22. Saladworks presented the testimony of Saladworks Chief Executive Officer and President John Scardapane ("Scardapane"), and Vice President of Operations Paul Steck ("Steck").

23. Saladworks introduced evidence that Mr. No's restaurant suffered from numerous health and safety problems, including rodent contamination including rodent feces; improper food handling, storage, and preparation increasing the risk of bacterial growth and contamination; unsanitary and dirty equipment (such as cutting boards and lettuce spinners); unsafe food temperatures; storage of insecticide near paper products; the absence of sanitization test strips; improper rotation and dating of food products; fermentation of salad dressings; and

general disarray and uncleanliness.

24. The court, granting the second emergency motion for entry, found that Saladworks was likely to succeed on the merits of its claims regarding the health and safety conditions, that the potential irreparable harm to Saladworks outweighed the harm to defendant resulting from the injunction, and that the public interest in health and safety would be protected by the injunction.

25. At the hearing for the first motion for preliminary injunction, Saladworks also introduced evidence to show Mr. No was defrauding Saladworks of royalty payments and advertising fees due Saladworks under the Franchise Agreement.

26. Scardapane and Steck visited the Restaurant in March, 2005, and posed as customers to observe the operation of the cash registers. Scardapane testified that he observed several instances of sales being rung up and immediately voided out. May 19 H.T. at 36.

27. Scardapane testified that he ordered a meal at the Restaurant. He testified that when the cashier calculated a subtotal for the sale on the register, he gave her money for the purchase, and the cashier voided out the sale so that the sale total was never entered into the net sales total on the register. May 19 H.T. at 36.

28. Saladworks requested tax returns, accounting records,

bank account information, sales tax records, and other business records. Saladworks alleges that Mr. No failed to produce any of the requested records or documents as required under the Franchise Agreement. May 19 H.T. at 47.

29. Saladworks' conducted an audit of the cash registers at the Restaurant. Saladworks alleges that the audit showed numerous, repeated, and frequent instances of voided sales. Plaintiff's Exhibit P-9.

30. Saladworks sent several notices to cure, addressing Mr. No's failures to submit timely sales reporting forms, cash register tapes, payments of royalties and advertising fees, and for violations of quality, service, and cleanliness standards. Plaintiff's Exhibit P-6.

31. On April 19, 2005, Saladworks sent Mr. No notice of termination of the Franchise Agreement for his failure to cure the previously noticed defaults. Plaintiff's Exhibit P-6.

32. Mr. No presented the testimony of James Moody ("Moody"), an employee of the Restaurant who was recently promoted to interim manager.

33. Moody testified that the previous manager left open the cash drawer of the register while making sales, and computed sales prices on a calculator. June 2 H.T. at 64.

Discussion

To support a preliminary injunction, the moving party must

prove a reasonable probability of success on the merits and irreparable injury if the preliminary relief is not granted pending final adjudication on the merits. See *American Greetings Corporation v. Dan-Dee Imports, Inc.*, 807 F.2d 1136, 1140 (3d Cir. 1986). The district court must also consider the potential harm to the party opposing the preliminary injunction as well as the public interest. *Id.*

Saladworks alleges Mr. No has defrauded Saladworks of royalty payments and advertising fees due Saladworks under the Franchise Agreement. Saladworks had also argued that it would suffer harm to its Marks and reputation as a result of Mr. No's poor operation of the Restaurant. This latter concern has been removed by the injunction already granted.

Concerning plaintiff's claims for payment of overdue royalties and fees, we need not analyze the probability of success on the merits, because Saladworks would suffer no irreparable harm from the denial of its motion. The injunction already granted to Saladworks allows it to exercise complete control of operations, while Mr. No retains ownership. This allows Saladworks to protect its marks and reputation, and protects the public interest by ensuring the health safety of the restaurant.¹ Plaintiff's only remaining interest in additional

¹ Saladworks is required to submit a weekly status report to the court to show it is properly operating the Restaurant.

equitable relief is purely pecuniary; this is insufficient justification for a preliminary injunction. See *In re Arthur Treacher's Franchisee Litigation*, 689 F.2d 1137 (3d Cir. 1982)(trial court erred in granting preliminary injunction ordering franchisee to pay money damages for past-due royalties).

In contrast, granting this injunction would cause substantial harm to defendant. Mr. No paid \$200,000 for the franchise, and he retains the right to own and operate the business for seventeen months (provided he can comply with plaintiff's operational standards following its interim takeover). Plaintiff's proposed injunction would take away his business entirely and deprive Mr. No of all profits he would otherwise enjoy under the remainder of his tenure. This harm substantially outweighs the potential harm to plaintiff from denying its injunction.

Because plaintiff's only remaining damages are monetary, all claims relating to the failure to pay amounts owed under the Franchise Agreement are properly left for trial, after a full adjudication of the merits of plaintiff's claims.

Conclusions of Law

1. The court has jurisdiction over the parties and the subject matter.
2. Saladworks will not be irreparably harmed by the denial of the preliminary injunction because any potential harm to its

Marks and reputation was cured by the previously granted injunction; all other harm is purely monetary.

3. The financial harm to defendant from plaintiff's total and permanent takeover of the Restaurant would be substantial, and outweighs any potential irreparable harm to plaintiff.

4. Plaintiff's first motion for a preliminary injunction will be denied to the extent not already granted.

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v.

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ORDER OF PRELIMINARY INJUNCTION

AND NOW, this 5th day of July, 2005, upon consideration of the verified amended complaint, the first motion for preliminary injunction and supporting memoranda of law of plaintiff, Saladworks, Inc. and all responses thereto, and after hearings on May 19, 2005 and June 2, 2005, in accordance with the attached memorandum, it is hereby **ORDERED** that plaintiff's first motion for preliminary injunction (Doc. No. 2) is **DENIED** to the extent not already granted.

/s/ Norma Shapiro
Norma L. Shapiro, S.J.