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Extreme circumstances: injunctive relief still difficult to obtain in franchise context

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The Supreme Court of Newfoundland and Labrador decision in *MTY Tiki Ming Enterprises v Azmy Enterprises Inc*, 2018 NLSC 169 reminds franchisors of the uphill battle in enforcing post-termination restrictive covenants by way of injunction.

Background

The plaintiff, MTY Tiki Ming Enterprises Inc. (MTY), is the franchisor of the Extreme Pita chain of restaurants.[1] MTY's franchise agreement with the defendant franchisee expired in August 2016. The franchisee continued to pay rent to MTY and operate the location post-expiry, but alleged that it did not do so as an Extreme Pita franchise as it did not use the franchisor's products or menu. MTY ultimately took the location back in September 2017. In November 2017 the franchisee began operating another pita concept restaurant (Stuff-It Pita) on the same street in suburban St. John's.

The franchise agreement contained a post-term non-compete clause that restricted the franchisee from operating a competitive business within the territory or within 20 kilometres of any other Extreme Pita locations, for a period of 12 months following termination.

One of the main issues in this case was whether or not the franchise agreement had ever been extended. The court held, at least for the purposes of this proceeding, that the agreement had not been extended. The 12-month restrictive covenant had therefore almost run its course by the time the application was brought.

Analysis

To determine whether the Supreme Court of Newfoundland and Labrador (the Court) should grant an interlocutory injunction it applied the three-part analysis set out by the Supreme Court of Canada in *RJR—MacDonald Inc. v Canada (Attorney General)*[2]:

1. There must be a serious issue to be tried;
2. The applicant must show it will suffer irreparable harm if the relief is not granted; and,
3. The balance of convenience must favour the granting of the interlocutory injunction.

In applying the first part of the test, the Court found that the elevated threshold of establishing a strong *prima facie* case should apply. Referring to *R. v. Canadian Broadcasting*

Corp.[3] the Court held that, in the circumstances of this case, the practical effect of granting the injunction would be akin to a final determination of the issue given that the franchisee would be required to shutter its business. However, the Court held that MTY failed to demonstrate a *prima facie* case for two primary reasons: (1) the geographic restriction was ambiguous; and (2) MTY had failed to bring any evidence to show that the proprietary interest that the restrictive covenant was intended to protect would actually be protected. The Court did, however, indicate that MTY would have met the lower threshold of qualifying as a "serious issue" to be tried.

The Court further held that MTY failed the second part of the test in that it had not been able to demonstrate that it had suffered or would suffer any irreparable harm. MTY failed to establish any financial loss, reduction of market share, damage to goodwill, or that the public would associate the Stuff-it Pita restaurant with the Extreme Pita brand. While MTY had demonstrated many similarities between the Extreme Pita and Stuff-It Pita concepts, including the names, marketing materials and menu offerings, these findings alone were not sufficient to establish harm.

In the final part of the test, the Court held that the balance of convenience favoured the franchisee. The key reasons given for its finding were: (1) the lack of evidence that the franchise agreement had been extended, and that, even if it had been extended, the protected period had almost run its course; (2) the lack of evidence of damage to the franchisor's goodwill, reputation, trademarks or of any harm to any other existing franchisees; and (3) the investments made by the franchisee in its new business and the consequential losses that it would suffer should it be required to shut down.

Key takeaways

There are a few key takeaways for franchisors from this decision. First, any franchisor coming to the court seeking injunctive relief must always put its best foot forward and come adequately prepared. A court will not want to take any action that will have serious effects on the investments and livelihood of other parties without clear reason. MTY's evidence, in particular the confusing record surrounding the term of the franchise agreement, the geographic scope of the restrictive covenant and its failure to show harm, fell short.

Second, the initial dispute with regard to whether or not the franchise agreement had been renewed or extended also underscores the need for franchisors to ensure that they maintain clear processes in documenting franchise renewals and extensions. More importantly, those processes must also be followed so that no franchisee can continue operating after its agreement has expired without clear evidence of extension or renewal terms.

Finally, the decision serves as a reminder to franchisors that a statement in a franchise agreement to the effect that the franchisor shall be entitled to injunctive relief should the franchisee breach a post-term restrictive covenant is insufficient for obtaining such relief. In order to succeed in enforcing a restrictive covenant post termination, franchisors will require compelling evidence of irreparable harm.

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[1] *MTY Tiki Ming Enterprises v Azmy Enterprises Inc, 2018 NLSC 169*

[2] [1994] 1 SCR 311

[3] 2018 SCC 5