December 10, 2013

Supreme Court Bolsters Enforceability of Forum Selection Clause

But Public Policy Factors May Still Allow Franchisees to Avoid Transfer

The U.S. Supreme Court decided unanimously in a December 3 decision that forum selection clauses will be enforced in "all but the most exceptional cases" when a party seeks a transfer to a contractually prescribed federal venue in a motion pursuant to 28 U.S.C. 1404(a). When the parties' agreement prescribes a nonfederal venue and is therefore beyond the scope of a transfer motion, the Court held that the party seeking to enforce the forum selection clause may do so through application of the doctrine of forum non conveniens. Although the Court's decision in *Atl. Marine Constr. Co., Inc. v. U.S. District Court,* 571 U.S. ___ (2013) resolves an important question concerning the appropriate procedure?- and the relative burdens?- applicable to efforts to enforce a forum selection clause, parties to franchise agreements may continue to be subject to varying state substantive law that precludes enforcement altogether as a matter of public policy.

Background of the Case

Atlantic Marine arose in the context of a construction dispute. Atlantic Marine, a general contractor from Virginia working on a project in Texas, entered into an agreement with J-Crew, a local Texas subcontractor. The parties' agreement contained a forum selection clause mandating that any dispute between them must be litigated in either Virginia state court or the U.S. District Court for the Eastern District of Virginia. Following a payment dispute, J-Crew, in violation of the forum selection clause, filed suit in federal court in Texas. Atlantic Marine moved to dismiss, claiming venue in the Western District of Texas was "wrong" under 28 U.S.C. 1406(a) or "improper" under Federal Rule of Civil Procedure 12(b)(3). Alternatively, Atlantic Marine moved to transfer the action to the Eastern District of Virginia under 28 U.S.C. 1404(a).

The district court denied the motions, and the U.S. Court of Appeals for the Fifth Circuit rejected Atlantic Marine's petition for a writ of mandamus. *In re Atl. Marine Constr. Co.*, 701 F.3d 736 (5th Cir. 2012). The circuit court held venue was neither improper nor wrong under the federal venue statute, 28 U.S.C. 1391. Instead, Atlantic Marine was limited to seeking a transfer under Section 1404(a). The circuit court further reasoned that dismissal was appropriate under Rule 12(b)(3) only when the parties' forum selection clause dictated an arbitral, foreign or state court forum. Applying transfer jurisprudence to the case at hand, the circuit court determined the district court did not abuse its discretion by placing the burden on the movant and treating the forum selection clause as only a "significant factor" in analyzing the public and private interest factors. In its decision, the circuit court recognized a split in authorities regarding the question of whether an action filed in contravention to a forum selection clause is subject to dismissal.

The Supreme Court's Decision

The Supreme Court began its analysis by rejecting Atlantic Marine's argument that dismissal of J-Crew's action was appropriate under either Section 1406(a) or Rule 12(b)(3). "Whether venue is 'wrong' or 'improper' depends exclusively on whether the court in which the case was brought satisfies the requirements of federal venue laws, and those provisions say nothing about a forum-selection clause." Like the circuit court, the Supreme Court held the forum selection clause may be enforced through a motion to transfer under Section 1404(a). However, the Supreme Court disagreed with the weight that should be accorded to the clause as part of the transfer analysis.

Putting it plainly, the Supreme Court held that "[w]hen the parties have agreed to a valid forum-selection clause, a district court should ordinarily transfer the case to the forum specified in the clause." Rather than being merely a "significant factor," the Supreme Court reasoned that "[o]nly under extraordinary circumstances unrelated to the convenience of the parties should a ?1404(a) motion be denied." According to the Court, the presence of the forum selection clause changes the usual calculus employed on a transfer motion by (a) withholding any weight to plaintiff's choice of forum; (b) removing consideration of the parties' private interests such as inconvenience; and (c) eliminating application of the original venue's choice-of-law rules.

Applying these principles to the case before it, the Supreme Court reversed, holding that the district court erred in placing the burden on Atlantic Marine to prove transfer was appropriate. Rather, a party acting in violation of a forum selection clause "must bear the burden of showing that public-interest factors overwhelmingly disfavor transfer."

Although not expressly at issue in the case, the Supreme Court also addressed the circuit court's holding that dismissal under Rule 12(b)(3) was an appropriate remedy when the clause points to a nonfederal forum. The Court rejected that conclusion, reasoning that a proper venue under federal venue laws cannot become improper simply because the forum selection clause identifies a nonfederal forum. Instead, the Court resolved this question by directing application of the forum non conveniens doctrine. Since Section 1404(a) was merely a codification of the doctrine of forum non conveniens for cases subject to transfer within the federal system, the Court held that the doctrine remained available for those residual cases where a nonfederal forum best serves the litigation convenience of the parties.

Applicability to Franchise Agreements

Forum selection clauses are a staple of franchise agreements. Franchisors seeking uniform treatment of common disputes and consistent construction of the system's critical contractual provisions typically include forum selection and choice-of-law provisions in their agreements. And, without doubt, forum selection clauses directing disputes to local courts afford franchisors the additional convenience of conducting the litigation in a location close to witnesses and documents.

The Supreme Court's decision in *Atlantic Marine* will, in most cases, bolster franchisors' efforts to enforce such forum selection clauses. However, the Court left open the possibility that, in an "exceptional case," the public interest factors may defeat a transfer application. For franchisees, one such factor may be the forum state's public policy invalidating a forum selection clause. Accordingly, the nearly impenetrable rule of enforceability announced in *Atlantic Marine* may be tempered where the forum state protects franchisees against litigation outside the local jurisdiction. *See, e.g.*, *Kubis & Persyzky Assocs., Inc. v. Sun Microsystems, Inc.,* 146 N.J. 176 (1996) (holding that forum selection clauses can materially diminish franchisees' rights guaranteed by the New Jersey Franchise Practices Act); Iowa Code ? 537A.10.3(a) (nullifying provisions in franchise agreements restricting jurisdiction to a forum outside Iowa); *S & G Janitschke, Inc. v. Cottman Transmission Sys.,* No. 05-2896, 2006 WL 1662892 (D. Minn. June 8, 2006) (upholding Minnesota state regulations that treat waiver of a franchisee's right to choose forum as unfair and inequitable).

Franchisors and franchisees must therefore look beyond the guidance provided by *Atlantic Marine* in analyzing the enforceability of a forum selection clause and consider state substantive protections that may serve to nullify such provisions as a matter of public policy.