

A Failed Exercise: Franchisor Denied Injunction

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Introduction

In *Greco Franchising Inc. v. Franco Milito et al.* 2021 ONSC 3950 (“*Greco*”), the Court analyzed the impact that the Covid-19 pandemic has had on businesses, particularly the personal fitness industries, in the context of a dispute regarding the parties rights and obligations contained in the franchise agreement. Greco Franchising Inc. (the “**Franchisor**”), a fitness studio franchisor, sought an injunction against the corporate franchisee defendant (the “**Franchisee**”) to prevent it from operating a new fitness studio.

Background Facts

The Franchisor operated numerous fitness studios under their “Greco System” with the franchise operated by the Franchisee in Ottawa/Kanata being one of the most successful. The franchise agreement (the “**Agreement**”) was set to expire on September 8, 2021.

Like all fitness studios and gyms, the Franchisee’s location was, and all other Greco System locations were, closed, throughout much of the Covid-19 pandemic. In response to these closures, the Franchisor created an on-line at home program called Greco Method at Home (“**GMAH**”), which Greco offered directly to gym members. The Franchisor received monthly payments for GMAH directly from members and then split the net revenues with franchisees equally, after deducting the franchise fees payable by franchisees. Greco System franchisees, including the Franchisee, were not allowed to offer any programs directly to their own members.

The Franchisor, recognizing that GMAH created fundamental changes to the franchise arrangement, drafted an amended franchise agreement, which the Franchisee refused to sign. The parties entered into negotiations to resolve their dispute; however, no agreement was reached by the parties.

On December 8, 2020, the Franchisee advised its members that it would cease operating as a Greco System franchise and would commence operating under the name TG Athletics. All of the Franchisee’s members who had been enrolled in GMAH cancelled their membership with the Franchisor. On January 8, 2021, the Franchisee sent a letter to the Franchisor purporting to terminate the Agreement alleging fundamental breaches, which it argued frustrated and repudiated the Agreement. The Franchisee alleged four specific breaches:

- (1) That GMAH encroached on the Franchisee's exclusive territory;
- (2) The Franchisor unilaterally setting the price and taking control of the Franchisee's clients was contrary to the Agreement, which stipulated that the Franchisor could only set maximum prices;
- (3) The Franchisor unilaterally changing the payment procedures so that payments received directly from clients meant it was being paid prior to the Franchisee, thereby affecting the Franchisee's cash flow; and
- (4) The Franchisor was offering/promoting services on the internet while not permitting the Franchisee to do so.

Ultimately, when permitted to do so by the Ontario government, the Franchisee opened TG Athletics to its members. The Franchisor took the position that the Agreement was still in force and the Franchisee was in breach of in term non-competition clause set forth in the Agreement.

The Test for an Interlocutory Injunction

To obtain an interlocutory injunction, the Franchisor was required to meet the three-part test outlined in *RJR-MacDonald Inc. v. Canada (Attorney General)* [1994] 1 SCR 311, which consisted of proving:

- (1) There is a serious question to be tried (or, in certain circumstances, the plaintiff has a strong *prima facie* case);
- (2) Irreparable harm will be suffered if the injunction is not granted; and
- (3) The balance of convenience favours granting the injunction.

Lack of a *Prima Facie* Case

The Court held that in this instance the Franchisor was required to establish it had a strong *prima facie* case, for the following reasons: (A) an injunction would likely render moot some of the issues in dispute since it would be impossible to have the issues brought to trial before the Agreement expired in September 2021; and (B) an injunction would close the Franchisee's fitness studio yet again, after over a year of other closures, and the impact on their livelihood was evident.

It was clear to the Court that opening TG Athletics was in contravention of the Agreement. The Court however believed the Franchisee had raised a serious issue to be tried as to whether GMAH and the financial re-structuring of the program resulted in a breach of the Agreement. That the Franchisee also had a serious issue to be tried thus undermined the Franchisor's argument that it had a strong *prima facie* case.

Irreparable Harm to the Franchisee

The irreparable harm and balance of convenience factors were analyzed together and the Court believed that harm would come to both parties. In respect of the Franchisee, an injunction would put it out of business and eliminate any possibility for the Franchisor to be compensated for any claims in the action. In respect of the Franchisor, much of the damage to its goodwill, reputation and membership allegiance had likely already occurred, since the Franchisee's Greco System studio had already closed and had been rebranded, which harm could be compensated by damages. For the remaining harm related to the competition created by the Franchisee's operation of TG Athletics for the remainder of the term of the Agreement, the Court noted that the Franchisor was prepared to allow the Franchisee to operate a fitness studio in the present location, which the Court interpreted as meaning that the Franchisee likely accepted that some competition from the Franchisee was inevitable.

The Court also considered the harm other persons affected by the dispute may suffer, including the impact on the livelihood of TG Athletics' 21 employees and 190 paying members. Further, a court-ordered closure of a fitness studio during a pandemic, for non-health related reasons, would create very poor optics for the public. Ultimately, the Court denied the interlocutory injunction.

Final Decision and Practice Takeaways

There are a number of takeaways from this decision on the relevance of the Covid-19 pandemic to future court decisions. In respect of the impact of the COVID-19 pandemic, throughout the analysis, the Honourable Justice Hackland remained aware of and sensitive to the impact of Covid-19 on the fitness industry, even going so far as to state that he took "notice of the fact that the Covid-19 pandemic has been particularly hard on the personal fitness industry." This statement, together with the fact that the Court was cognizant of the fact that an injunction would prevent the Franchisee from operating after over a year of other closures, seems to indicate that courts are sensitive to the serious negative consequences the pandemic has had on business, and as a result, the courts may be wary to render decisions that are likely to create further hardships. The decision also seems to indicate that the courts are concerned with the public perception of their decisions in the context of the overall administration of justice.

In respect of the legal test for an interlocutory injunction, the *Greco* decision underlies the importance of the party seeking the relief to come to court with "clean hands" and to ensure that the harm was not capable of being compensated by monetary damages.