UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF TEXAS
DALLAS DIVISION

MARY KAY INC. Plaintiff, vs. AMY DUNLAP Defendant.	CASE NO.: 3:12-cv-00029-D

DEFENDANT'S BRIEF IN SUPPORT OF RESPONSE TO PLAINTIFF MARY KAY INC.'S MOTION TO DISMISS HER COUNTERCLAIM COUNTS I AND 2

DATE: March 14, 2012

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COMES NOW the Defendant and for her Response to Plaintiff's Motion to Dismiss Counts 1 and 2 of her Counterclaim, respectfully submits the following brief to the Court.

I. INTRODUCTION

Defendant ("Defendant Amy Dunlap") performed her obligations under the contracts with the Plaintiff ("Mary Kay") by building her business over a period of many years, to become one of Mary Kay's largest distributors, generating a very high volume of sales of Mary Kay products which continues to be enjoyed by Mary Kay to this day.

The actions of the Plaintiff in failing to pay Defendant for the value of the business upon terminating her as a consultant is a deceptive trade practice which is a part of a pattern of deception through the years by Mary Kay, which is the subject Defendant's Answer and Counterclaim, inasmuch as Defendant was to have her "own business" as a National Sales Director ("NSD") of the Plaintiff, which she should have been given an opportunity to sell or transfer, not to have it be forfeited by the Plaintiff upon her resignation as a NSD.

The Plaintiff's actions in restraint of trade violate the letter and the spirit of Texas and federal laws providing for protections of the rights of Defendant to make a living and build her business by competing with Plaintiff as well as of the rights of other former Mary Kay consultants to make a living and build their businesses by competing with the Plaintiff within the direct sales market, particularly in the State of Texas.

II. ARGUMENT AND AUTHORITIES

A. Legal Standard

In her Answer and Counterclaim, Defendant Dunlap has requested relief under § 17.50 of the Deceptive Trade Practices Act (DTPA).[1] The Defendant in Count 1 of her

[1]Texas Statutes, § 17.50 Bus. & Com. Relief for Consumers
§ 17.50 BUS. & COM. Relief for Consumers
(a) A consumer may maintain an action where any of the following constitute a producing cause of economic damages or damages for mental anguish:
(1) the use or employment by any person of **a false, misleading, or deceptive act or practice** that is:

Counterclaim has alleged the Plaintiff has violated § 17.46 of the DTPA which further references two "specifically enumerated" acts or practices. Those enumerated acts or practices referenced in § 17.46 which the allegations of Count 1 of the Counterclaim support as grounds for relief in this case are items (12)[2] and (21).[3] The allegations of Count 1 of the Answer and Counterclaim present a plausible claim for liability of the Plaintiff to the Defendant on her Counterclaim, Count 1, as required in *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007) and *Ashcroft v. Iqbal*, 129 S. Ct. 1937 (2009).

In *Labella v. Charlie Thomas Inc.*, 942 S.W.2d 127 (Tex.App.-Amarillo 1997) the court stated:

"The elements of a DTPA action are: (1) the plaintiff is a consumer,[4] (2) the defendant(s) engaged in false, misleading, or deceptive acts, and (3) these acts constituted a producing cause of the consumer's damages. *Doe v. Boys Clubs of Greater Dallas, Inc.*, 907 S.W.2d 472, 478 (Tex. 1995); Tex. Bus. & Com. Code § 17.50(a)(1). A consumer is defined as 'an individual . . . who seeks or acquires by purchase or lease, any goods or services. . . .' Tex. Bus. & Com. Code § 17.45 (Vernon 1987)."

See also, Amstadt v. U.S. Brass Corp., 919 S.W.2d 644, 649 (Tex. 1996) ("Privity of contract with a defendant is not required for the plaintiff to be a consumer.")[5]

(A) **specifically enumerated in a subdivision of Subsection (b) of Section 17.46** of this subchapter; and
(B) relied on by a consumer to the consumer's detriment;
(2) **breach of an express or implied warranty**;
(3) any **unconscionable action or course of action** by any person; (Emphasis added)

[2]**§** 17.46 BUS. & COM. Deceptive Trade Practices Unlawful
(b) Except as provided in Subsection (d) of this section, the term "false, misleading, or deceptive acts or practices" includes, but is not limited to, the following acts:
… (12) representing that an agreement confers or involves rights, remedies, or obligations which it does not have or involve, or which are prohibited by law;

[3](21) promoting a pyramid promotional scheme, as defined by Section 17.461;

[4] From Defendant's Answer and Counterclaim: "12… By agreeing to acquire her beauty consulting business as an independent contractor, entrepreneur and the owner of her own business as a result of her contracts with Mary Kay, Defendant was a consumer of the Defendant's services as that term is defined under §17.45 of the Texas Business and Commerce Code, having relied on the written and oral representations of Plaintiff that, as an 'independent dealer' she was the owner of her own business."

[5] Although *Amstadt* was cited in the Plaintiff's Brief (pages 3-4) and notwithstanding what Plaintiff described as the elements that must be pled and proven in order "[t]o state a claim," that case did not refer to the specifically enumerated acts as set forth in § 17.46(b) as being a required

In *Concorde Limousines v. Moloney Coachbuilders*, 835 F.2d 541, 544 (5th Cir. 1987) involving a successful DTPA action by a distributor against a supplier, the Court noted the broad remedies allowed under the DTPA:

"DTPA Section 17.50 makes sellers liable to consumers for actual damages where 'a false, misleading, or deceptive act or practice' is 'a producing cause' of those damages.[fn7] As this court noted in *Pope v. Rollins Protective Services Co.*,

> One of the primary reasons for the enactment of the DTPA was to provide consumers with a remedy for deceptive trade practices without the burdens of proof and numerous defenses encountered in a common law fraud or breach of warranty action.[fn8]

In keeping with the DTPA's broad, remedial purpose, Section 17.44 provides:

> This subchapter shall be liberally construed and applied to promote its underlying purposes, which are to protect consumers against false misleading and deceptive business practices, unconscionable actions, and breaches of warranty and to provide efficient and economical procedures to secure such protection.[fn9]"

Defendant Amy Dunlap is a "consumer" and/or a "business consumer" under the DTPA. A "business consumer" is defined as "an individual, partnership, or corporation who seeks or acquires by purchase or lease, any goods or services for commercial or business use. The term does not include this state or a subdivision or agency of this state." § 17.45(10). The claimant must have sought to purchase goods or services and the goods or services must form the basis of the complaint. *Americom Distrib. Corp. v. ACS Communications, Inc.* 990 F.2d 223, 227 (5th Cir.), *cert. denied*, 510 U.S. 867 (1993) (citing *Cameron v. Terrell & Garrett*, 618 S.W.2d 535, 539 (Tex. 1981)). The distributorship arrangement in this case involves the acquisition or, at least the permitted use, of some intangible property rights, such as the Mary Kay trademarks and copyrights,

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element of a statement of a claim upon which relief could be granted. *Amstadt* instead relied on *Doe v. Boys Clubs of Greater Dallas Inc.*, 907 S.W.2d 472, 478 (Tex. 1995) just as did *Labella, supra*) which stated the three elements necessary to be proven by the claimant under the DTPA as:

"(1) the plaintiff is a consumer, (2) the defendant engaged in false, misleading, or deceptive acts, and (3) these acts constituted a producing cause of the consumer's damages. *See* TEX.BUS. & COM.CODE § 17.50(a)(1)."

etc.,[6] and also involves the acquisition of goods[7] or services.[8] *Texas Cookie Co. v. Hendricks & Peralta, Inc.*, 747 S.W.2d 873, 876-77 (Tex.App.-Corpus Christi 1988, *writ denied*). The associated goods and services in this case are not merely incidental to the

[6] *See*, paragraph 7.2 (i) of the INSDA attached as Exhibit "A" to Defendant's Answer and Counterclaim.

[7] From page 1 of the INSDA, "WITNESSETH:
"WHEREAS, Company manufactures and sells cosmetics, toiletries and related products (hereinafter called 'Mary Kay® products') under the registered trademarks 'MARY KAY' and various other trademarks owned by Company; and
WHEREAS, NSD is engaged in business as an independent dealer ('Beauty Consultant') for Mary Kay® products, **purchasing** such products from Company and reselling for NSD's own account to ultimate consumers of NSD's choice and proposes to continue such business; and has also demonstrated exceptional ability as an outstanding Unit and Independent Senior Sales Director, aiding, counseling and inspiring other Independent Beauty Consultants and Unit Independent Sales Directors;"
…[and from Annex 1 to the INSDA] "VII. NSD Product **Purchases**
As a National Sales Director, the NSD shall be eligible to receive a 50% discount off the suggested retail selling price on NSD's **purchase** of any products listed in Section 1 of the Consultant order form which is in effect at the time of the **purchase**." (Emphasis added)

[8] "7.2 NSD shall have, in addition to the other rights and privileges set out in this Agreement, the following rights:
…(ii) **To purchase** or otherwise receive such incentive, promotional items and materials, gifts, products and sales aids as may be made available by Company for NSD's use in furthering the success of Beauty Consultants and Unit Sales Directors within NSD's Sales Group.
(iii) special recognition by Company as a leader and motivator of a Sales Group comprising numerous independent contractors, in an area which may include all of the United States and various foreign jurisdictions and which will include Sales Directors and Beauty Consultants other than individuals personally recruited by NSD, and receipt of various valuable override commissions relating to the Wholesale Purchase Volume and sales activities of such Sales Group;
(iv) personal access to Company-compiled reports and information including comprehensive lists of names, addresses, telephone numbers and detailed records of the purchases and sales activity of various members of the Mary Kay independent sales organization, and data identifying customers for Mary Kay's products and other competitively valuable business information, not generally known nor readily available to competitors or the general public in similar content, detail and form, and, which NSD agrees to treat as confidential and not utilize or disclose for purposes which conflict with the business interests of the Company; and
(v) valuable special recognition at various major Company-sponsored events, national publicity in Company publications and promotional assistance to stimulate sales by NSD's Sales Group and promote NSD's personal image as a successful and dynamic leader, motivator, salesperson and recruiter, designed to enhance NSD's prestige and influence with members of the Mary Kay independent contractor sales organization."

INSDA agreement but are *fundamental*[9] to Defendant Dunlap and her success in her "business" as a National Sales Director and are the basis of her claim that Mary Kay's representation/warranty that she would "own her own business."[10] Because, in a DTPA claim, "the goods or services purchased or leased must form the basis of the complaint," this case falls within the purview of the DTPA. *Id.* (quoting *Melody Home Mfg. Co. v. Barnes*, 741 S.W.2d 349, 351-52 (Tex. 1987))."

A case cited and followed by the *Texas Cookie* case, *Wheeler v. Box*, 671 S.W.2d 75, 78-79 (Tex.App.-Dallas 1984), also dealt with a business arrangement bearing distinct similarities to that which existed in this case:

"In light of the 1977 amendment, changing the definition of "services," we hold that a plaintiff is no longer required to differentiate between goods and services to prove that he is a consumer under the act.

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[9] *Fisher Controls v. Gibbons*, 911 S.W.2d 135 (Tex.App.-Hous. (1 Dist.) 1995) cited by the Plaintiff and dealing with a sales representative of a company in its Brief is not applicable here, but a case cited by the *Fisher* court *is* comparable to the facts of this case--*TX Cookie v. Hndricks/Peralta*, 747 S.W.2d 873, 877 (Tex.App.-Corpus Christi 1988):
"The collateral services which TCC was to provide H & P included a company training program, a confidential operating manual, and what was vaguely referred to in the franchise agreement as a 'unique system,' the characteristics of which are: special merchandising, marketing and specially designed facilities, interior and exterior layout and trade dress; standards and specifications for fixtures and equipment, methods for keeping books and records, inventory control system and training and supervision. . . .These services were clearly an objective of the transaction and not merely incidental to it. Without them, the franchise would have been little more than the right to sell products under the 'Texas Cookie Company' name."

Nor is another case cited by Plaintiff in its Brief, *Hand v. Dean Witter Reynolds, Inc.*, 889 S.W.2d 483, 497 (Tex.App.-Houston 1994) pertinent here. Clearly the "option" which was the subject of the contract at issue in that case is an intangible and not goods or services such as are involved under the facts of this case.

[10] In the case of *Cox v. Dubois*, 16 F. Supp.2d 861, 867-868 (S.D.Ohio 1998) the court described what it is to be an "owner" rather than just a temporary possessor with a few rights:
'"Owner'" is defined in Black's Law Dictionary as 'The person in whom is vested the ownership, dominion, or title of property; proprietor.' Black's Law Dictionary 996 (5th ed. 1979). 'Ownership' is defined in Black's Law Dictionary as: Collection of rights to use and enjoy property, including right to transmit it to others. *Trustees of Phillips-Exeter Academy v. Exeter,* 92 N.H. 473, 33 A.2d 665, 673. The complete dominion, title, or proprietary right in a thing or claim. The entirety of the powers of use and disposal . . . The exclusive right of possession, enjoyment and disposal; involving an essential attribute, the right to control, handle and dispose. Black's Law Dictionary 997 (5th ed. 1979)."

Considering the wording of the contract between the parties, we find that although the parties specifically recognized that the business bargained for was basically a concept, rather than physical property, it also provided that the appellants provide to appellees, an operations manual, word processing programs, and art work and logo including negatives, together with an initial supply of presentation folders. Additionally, the contract provided that appellants would provide a guide and checklist enumerating needed office supplies, equipment furnishings and space requirements, and up to ten days on site assistance and training in Boxes' Dallas office. Additionally, the jury found that certain other services were to be rendered by the Wheelers in connection with the sale of the business.

We hold that the evidence in this case is sufficient to show that appellees were consumers within the meaning of the act. They purchased a business; although the business entity itself was an intangible, it encompassed both tangible personal property and services purchased for use in the function of the business. **Indeed, we would have to adopt a very narrow and strained interpretation, to conclude that the Boxes purchased neither tangible goods nor services."** (Emphasis added)

Plaintiff erroneously cites *Blackmon-Dunda v. Mary Kay*, 05-08-00192-cv 2009 WL 866214, at *6 (Tex.App.-Dallas 4-2-2009) for the proposition that the claim of the former Mary Kay Sales Director was dismissed because she was not a consumer regarding Mary Kay *services*. As the court indicated, its decision denying her DTPA claim was based upon her failure to claim in the trial court below that she was a consumer of services and not just the products sold by Mary Kay.[11] Plaintiff has also cited the cases of *Baker v. Missouri Pac. Truck Lines, Inc.*, 616 S.W.2d 389, 392-393 (Tex. Civ. App.-Houston 1981) and a case which the Plaintiff identifies at page 10 of its Brief as "*Craig*, 1998 WL 466133, at *2-3" which purport to exclude the Plaintiffs in those cases from recovery under the DTPA because they were independent contractors who provided services and therefore were sellers not consumers. These cases may or may not withstand scrutiny under the mainstream of case law cited *supra* and decided under the DTPA, many of which find that business consumers are protected by the DTPA. However they are not comparable to the facts of this case, where Exhibit "A" to the Answer and Counterclaim

[11]"In her pleadings below, appellant argued her DTPA claim was based on her status as a consumer of Mary Kay's products. To the extent appellant failed to raise the issue of her status as a consumer of Mary Kay's *services* in her pleadings, she cannot raise that issue for the first time on appeal. *See* Tex. R. App. P. 33.1(a)(1)." *Id.*

references many important core services which are to be provided *to* Defendant Dunlap *by* the Plaintiff.

B. <u>Mary Kay's conduct in Depriving Defendant of her Right to Sell her "Own Business" is Unconscionable and thus Actionable under the DTPA.</u>

The Court's decision in the case of *Dwight's Dis. Vacuum Cl. City v. Scott Fetzer*, 860 F.2d 646, 649-650 (5th Cir. 1988) described unconscionable conduct for purposes of the DPTA:

"The statute defines unconscionable action as an act or practice which, to a person's detriment:
(A) takes advantage of the lack of knowledge, ability, experience, or capacity of a person to a grossly unfair degree; or (B) results in a gross disparity between the value received and consideration paid, in a transaction involving transfer of consideration.
Tex.Bus. & Com. Code Ann. § 17.45(5). Unconscionable action, by the terms of the statute, then, is an act or practice which either (a) is overbearing and evidences misuse of superior bargaining power or (b) results in a gross disparity between consideration paid and value received.

In *Chastain v. Koonce,* the Texas Supreme Court refined the definition of "unconscionable action." 700 S.W.2d 579 (Tex. 1985). *See also Chandler v. Housholder,* 722 S.W.2d 217, 218-19 (Tex.App.-Eastland 1986, writ ref'd n.r.e.); *Tri-Continental Leasing Corp. v. Law Office of Richard W. Burns,* 710 S.W.2d 604, 609 (Tex.App.-Houston [1st Dist.] 1985, writ ref'd n.r.e.). The court, in considering whether there was evidence to support a jury finding of unconscionability, stated:
Section 17.45(5) is intended to be an objective standard.... The term 'gross' should be given its ordinary meaning of glaringly noticeable, flagrant, complete and unmitigated.
700 S.W.2d at 583. As to subdivision A of section 17.45(5), the *Chastain* court said that '[t]aking advantage of a consumer's lack of knowledge to a grossly unfair degree thus requires a showing that the resulting unfairness was glaringly noticeable, flagrant, complete and unmitigated.' Id. at 584."

The repeated representations that Defendant owned her "own business" which is inconsistent with Section 13 "Assignability" of the Independent National Sales Director Agreement ("INSDA") attached to the Answer and Counterclaim as Exhibit "A," shows a conscious scheme and plan by Plaintiff which was a deceptive act and practice under the

DTPA.[12] Defendant built an organization of consultants in Mary Kay which is still generating substantial sales and income from those sales to the Plaintiff. The forfeiture by Plaintiff of her income stream from those ongoing sales by the organization of consultants that she built is "unconscionable" under the DTPA. Defendant has alleged her right to receive compensation for such a forfeiture in paragraph 13, Count 1 of her Counterclaim. Plaintiff's refusal to allow her to obtain the benefit of the income stream is, at the very least, grossly inconsistent with the last sentence of § 2.210(b).

C. § 17.461 of the DTPA, Pyramid Promotional Schemes is Subsumed in Defendant's Allegations of Count 1 of her Counterclaim by her references to §§ 17.46 and 17.50.

§ 17.461 of the DTPA, Pyramid Promotional Schemes, comes into play in this case by virtue of § 17.46 (21).[13] Exhibit "A" to the Answer and Counterclaim filed by the Defendant, the INSDA, includes Annex I, a "Schedule of Commissions and Bonuses" which shows the method and manner of compensating the NSD, as being a percentage of the monthly *Wholesale Purchase Volume* of the consultants in her "Sales Units,"[14] which are her organization of downline consultants, shows the method and manner of

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[12] "Texas Statutes, § 2.210 Bus. & Com. Delegation of Performance; Assignment of Rights
§ 2.210 BUS. & COM. Delegation of Performance; Assignment of Rights
…(b) Unless otherwise agreed all rights of either seller or buyer can be assigned except where the assignment would materially change the duty of the other party, or increase materially the burden or risk imposed on him by his contract, or impair materially his chance of obtaining return performance. **A right to damages for breach of the whole contract or a right arising out of the assignor's due performance of his entire obligation can be assigned despite agreement otherwise.**" (Emphasis added) Additionally, and also fatal to its validity, the second sentence of Section 13 of the INSDA (Exhibit "A' to the Answer and Counterclaim) lacks mutuality of obligation inasmuch as while it purports to deprive Defendant of her right to transfer her rights under the INSDA, the Plaintiff is not similarly restricted.

[13] "Texas Statutes, § 17.46 Bus. & Com. Deceptive Trade Practices Unlawful:
(21) promoting a pyramid promotional scheme, as defined by Section 17.461…"

[14] Not based upon the amount of actual retail sales made to ultimate consumers:
"**VII. NSD Product Purchases**
As a National Sales Director, the NSD shall be eligible to receive a 50% discount off the suggested retail selling price on NSD's **purchase** of any products listed in Section 1 of the Consultant order form which is in effect at the time of the **purchase**." (Emphasis added)

compensation of the Defendant. In Utah, where many multilevel companies are based and the body of laws governing them is steadily growing, the district court was confronted with money received by participants in a multilevel where the company claimed the distributors involved were ultimate consumers of the company's products and not participants in a pyramid scheme. In that case, *Whole Living, Inc. v. Tolman*, 344 F. Supp.2d 739, 742-744 (D.Utah 2004) the court, in stating that the Federal Trade Commission's positions in respect to pyramid schemes provided it and the other federal courts guidance on such matters,[15] referenced the consequences of a determination that the company's products were primarily being sold to distributors who *were not*, just as alleged by Mary Kay in its Brief in Support of its Motion to Dismiss at page 4 (hereinafter, "Plaintiff's Brief"), the ultimate users/consumers of the products:

"In determining when a multi-level marketing plan is an illegal pyramid scheme, federal and Utah state law apply similar standards… 'The program is unquestionably *not* a pyramid scheme if only the distributor level is taken into account; the participant pays no money to [the company]… This compensation is facially '"unrelated to the sale of the product to ultimate users"' because it is paid based on the suggested retail price of the amount *ordered* from [the company], rather than based on *actual sales* to consumers. On its face, [the company's] program appears to be a pyramid scheme. [The company] cannot save itself simply by pointing to the fact that it makes some retail sales. *See In re Ger-Ro-Mar, Inc.*, 84 F.T.C. 95, 148-49 (1974) (that some retail sales occur does not mitigate the unlawful nature of pyramid schemes), *rev'd on other grounds*, 518 F.2d 33 (2d Cir. 1975). The promise of lucrative rewards for recruiting others tends to induce participants to focus on the recruitment side of the business at the expense of their retail marketing efforts, making it unlikely that meaningful opportunities for retail sales will occur. *Koscot*, 86 F.T.C. at 1181…This compensation is facially "unrelated to the sale of the product to ultimate users" because it is paid based on the suggested retail price of the amount *ordered* from [the company], rather than based on *actual sales* to consumers. On its face, [the company]'s program appears to be a pyramid scheme."

Here, the fact that Mary Kay pays commissions on *Wholesale* Purchase Volume rather than *retail* purchase volume is immaterial as the fact remains that the commissions are

[15] "Texas Statutes, § 17.46 Bus. & Com. Deceptive Trade Practices Unlawful
(c)(1) It is the intent of the legislature that in construing Subsection (a) of this section in suits brought under Section 17.47 of this subchapter the courts to the extent possible will be guided by Subsection (b) of this section and the interpretations given by the Federal Trade Commission and federal courts to Section 5(a)(1) of the Federal Trade Commission Act [15 U.S.C.A. § 45(a)(1)]."

not being paid on sales to "ultimate consumers." In the case of *Stull v. YTB International, Inc.* CIVIL NO. 10-600-GPM (S.D.Ill. 9-26-2011)[16] that court also noted, more recently, the role of the FTC's opinions in the determination of what constitutes an illegal pyramid scheme:

"The meaning of the provisions of the statutes governing pyramid sales schemes invoked by Plaintiffs have not been the subject of extensive judicial construction, but the Court finds guidance (pursuant to the provisions included in the state's anti-pyramid scheme statutes) in the opinions of the Federal Trade Commission ("FTC") and federal courts interpreting the Federal Trade Commission Act ("FTCA"), 15 U.S.C. § 41 *et seq. See, e.g.*, 815 ILCS 505/2 (providing that courts may look to opinions of the FTC in construing the ICFA); *People ex rel. Hartigan v. Unimax Inc.*, 523 N.E.2d 26, 29 (Ill. App. Ct. 1988) (same)…"

"A lawful MLM program is distinguishable from an illegal pyramid scheme in the sense that the "primary purpose" of the enterprise and its associated individuals is to sell or market an end-product with end-consumers, and not to reward associated individuals for the recruitment of more marketers or "associates." *In re Amway Corp.*, 93 F.T.C. 618, 716 (1979) (finding that a MLM program was not an illegal pyramid scheme where so-called "sponsors" did not make money from their recruits' efforts *until a newly-recruited distributor began to make wholesale purchases from his sponsor and sales to consumers*)." (Emphasis added)

D. <u>"Representing that an Agreement Confers or Involves Rights, which it Does Not Have or Involve" is Actionable Under the DTPA.</u>

Texas Statutes, § 17.46 Bus. & Com. Deceptive Trade Practices Unlawful include:

(a) False, misleading, or deceptive acts or practices in the conduct of any trade or commerce are hereby declared unlawful and are subject to action by the consumer protection division under Sections 17.47, 17.58, 17.60, and 17.61 of this code.
(b) Except as provided in Subsection (d) of this section, the term "false, misleading, or deceptive acts or practices" includes, but is not limited to, the following acts:
…
(12) representing that an agreement confers or involves rights, remedies, or obligations which it does not have or involve…

A case in which a representation was determined to give rise to liability under the

[16] http://scholar.google.com/scholar_case?case=17378195018812494774&hl=en&as_sdt=2&as_vis=1&oi=scholarr ; Loislaw Federal District Court Opinions (CCH)

DTPA for a representation that there exists a material benefit in an agreement which it does not actually have or involve,[17] is *Best v. Ryan Auto Group Inc.*, 786 S.W.2d 670, 671-672 (Tex. 1990) in which the Court found the distributor was entitled to recovery:

"Because Best's purchase of the 'dealership' did not include the ability to purchase more inventory from Harley-Davidson, he was effectively out of business. Best then sued Ryan for, among other things, violation of DTPA § 17.46(b)(12)... Here, as the court of appeals conceded, there is evidence "that Ryan misrepresented the status that Best would enjoy as a Harley-Davidson dealership, including the ability to buy parts and vehicles." More specifically, Best testified that Ryan misrepresented to him at the time of sale that he would "be able to buy parts and vehicles as Mr. Ryan had been buying." Clearly, this is some evidence from which the jury could reasonably conclude that Best purchased the dealership with the specific understanding that he would be able to purchase inventory as needed from Harley-Davidson and, therefore, that Ryan's misrepresentation was a producing cause of Best's subsequent damages."

More recently, an allegation of a subsection (12) which specifically enumerates a violation of § 17.46 was used by the Fifth Circuit to pave the way to a trial for the claimant in that case in *Monumental Life Ins. Co. v. Hayes Jenkins*, 403 F.3d 304, 319-320 (5th Cir. 2005):

"Sondra also claims that MLIC and NovaStar engaged in unfair and deceptive practices

[17] From Defendant's Answer and Complaint: "12… Throughout her relationship with Mary Kay, until the very end, she was deceived by the company's continuous, non-stop, orchestrated campaign through speeches at the annual Seminars, business opportunities meetings, CDs, DVDs, cassette/VCR tapes, brochures, letters and emails, representing to her and the other Consultants in her National Sales Director Unit, and throughout the company for that matter, that they were being provided by Mary Kay the business opportunity of owning their own businesses. 13. Mary Kay, among other deceptive practices, has repeatedly represented to Defendendant, its other Independent Beauty Consultants, Unit Independent Sales Directors, and Independent National Sales Directors that their status as such independent contractors affords them the complete ownership of their 'own business' which is a deliberate falsehood inasmuch as the Plaintiff's executives are all well aware of the fact that Mary Kay strictly forbids its Consultants, Sales Directors, and National Sales Directors to sell, transfer or will their 'businesses,' and wrongfully enjoys the fruits of the labors of those independent contractors by forfeiture of their right to receive the 'income stream' or value of it when they die, leave or are terminated by Mary Kay. These trade practices of Mary Kay were misleading, deceptive, and false in that Mary Kay never compensated Defendant for her business when it took it from her without compensation when she resigned as National Sales Director, and would not allow her to sell or will her 'business.'"

under …§ 17.46(b)(12) of the DTPA by representing to potential applicants, in the promotional materials and the application form, that *in every instance* the applicants would enjoy a thirty-day 'risk free' period during which they could (1) examine the policy and accept or reject it, (2) remain covered by the insurance while they considered these options, and (3) owe nothing if they timely rejected coverage. To this end, she maintains that, if enforced, MLIC and NovaStar's monthly billing and notification procedures, coupled with the application and policy provisions that coverage would begin only after the first premium is paid, would render the thirty-day period "meaningless." This is so, asserts Sondra, because in most cases the thirty-day period will have expired (or almost expired) by the time (1) MLIC notifies NovaStar of MLIC's approval of the applicant for mortgage life insurance and (2) NovaStar bills its borrower and receives the premium from its borrower. In an effort to support this argument, Sondra has offered evidence that the thirty-day period runs from the effective date of the policy, rather than the date of payment of the first premium or the date of the insured's receipt of the policy...

We are satisfied that Sondra has raised a genuine issue of material fact as to whether, in violation of § 17.46(b)(12), MLIC and NovaStar represented to her and her husband that the insurance agreement 'confers a right which it does not have,' i.e., a full thirty-day 'risk free' trial period during which they would be fully covered."

In this case, the representation that Defendant would be the owner of her "own business" by entering into her INSDA, when in fact the Plaintiff maintains that a Mary Kay consultant has no right to sell or transfer her rights under her agreement with the company, adequately states a claim for relief under the provisions of § 17.50, by way of a § 17.46(b)(12) representation.

E. <u>Breach of Express Warranty.</u>

The Fifth Circuit has had occasion to pass on the question of whether actionable warranties described under the DTPA § 17.45(2) apply to warrantees relating to services such as the Plaintiff's repeated statements that the Defendant was the owner of her "own business," in the case of *Brooks, Tarlton, Gilbert, ET Al. v. U.S. Fire*, 832 F.2d 1358, 1373-1374 (5th Cir. 1987):

"While the DTPA makes the breach of an express warranty actionable under the Act, '[t]he DTPA does not define the term `warranty.' Furthermore, the act does not create any warranties; therefore any warranty must be established independently of the act.' *La Sara Grain*, 673 S.W.2d at 565; *accord Melody HomeMfg. Co. v. Barnes*, S.W.2d, 30

Tex.Sup.Ct.J. 489, 492 (June 17, 1987). The most accessible definition of 'express warranty' appears in Chapter 2 of the Texas Uniform Commercial Code ("the Code"). *See* Tex.Bus. & Com. Code Ann. § 2.313 (Tex. UCC) (Vernon 1968). Chapter 2 of the Code, however, governs only the sale of goods. *Id.* § 2.102. Under the DTPA, an insurance policy is a service. *McCrann v. Klaneckey,* 667 S.W.2d 924, 926-27(Tex.App.-Corpus Christi 1984, no writ); *Dairyland County Mut.Ins. Co. v. Harrison,* 578 S.W.2d 186, 190 (Tex.Civ.App. —Houston [1st Dist.] 1979, no writ); *McNeill v. McDavid Ins.Agency,* 594 S.W.2d 198, 202 (Tex.Civ.App.-Fort Worth 1980, no writ). Unfortunately, we have been able to find no source which instructs us when, if ever, a seller "warrants" the service it has agreed to furnish.[fn12] We are not prepared to hold, however, that the dearth of law on express warranties in service contracts means that the law only recognizes express warranties when they arise in contracts for the sale of goods. *See Melody Home,* 30 Tex.Sup.Ct.J. at 492 (holding that section 17.45(2) of the Act expresses the legislative intent that providers of services should not escape the requirements of the Act). But the absence of law does, when coupled with the fact that we are faced with an insurance policy, complicate our analysis.[fn13] After reflection, however, we have concluded that for our purposes, the Code's provisions on express warranties are instructive, even if they are not controlling. Therefore, we turn to these provisions."[18]

In *Southwestern Bell Telephone Co. v. FDP Corp.*, 811 S.W.2d 572, 574-575 (Tex. 1991) a case upholding the jury's finding of a violation of 17.50 (a) (2) breach of an express warranty in the sale of advertising service, the court referred first to the common law of warranty, and discussed the UCC definition by way of analogy:

"Because Bell's sale of advertising is predominantly a service transaction, not a sale of goods, the warranty provisions of Article Two of the Uniform Commercial Code ("UCC") do not explicitly govern this case. *See* TEX.BUS. & COM.CODE § 2.102

[18]§ 2.313 BUS. & COM. Express Warranties by Affirmation, Promise, Description, Sample
(a) Express warranties by the seller are created as follows:
(1) Any affirmation of fact or promise made by the seller to the buyer which relates to the goods and becomes part of the basis of the bargain creates an express warranty that the goods shall conform to the affirmation or promise.
(2) Any description of the goods which is made part of the basis of the bargain creates an express warranty that the goods shall conform to the description.
(3) Any sample or model which is made part of the basis of the bargain creates an express warranty that the whole of the goods shall conform to the sample or model.
(b) It is not necessary to the creation of an express warranty that the seller use formal words such as "warrant" or "guarantee" or that he have a specific intention to make a warranty, but an affirmation merely of the value of the goods or a statement purporting to be merely the seller's opinion or commendation of the goods does not create a warranty.

(Tex.UCC). Therefore, we begin this inquiry by examining the common law of warranty. Although it is well-established that express warranties are enforced in service transactions, *see Hawkins v. McGee*, 84 N.H. 114, 146 A. 641 (1929), warranty law has primarily developed in the context of the sale of goods."

F. <u>Count 2 Dealing with an Unreasonable Restraint of Trade should not be Dismissed</u>

In the Plaintiff's Brief, Plaintiff has made a narrowly targeted attack on Defendant's claim, arguing that said Count 2 is defective because it fails to allege "an adverse effect on *competition* in the relevant market" in that it 1) contains no allegations defining the relevant market, showing Mary Kay's market power, the market competitors, or the effect of the non-compete agreement on the price and availability of the relevant products in the relevant area, and 2) "fails to allege that [the] non-compete has an anticompetitive effect on the relevant market as a whole."[19] However, the allegations of paragraph 19 of the Answer and Counterclaim[20] do define the relevant market, that Mary Kay's market power is sufficient to adversely affect the relevant market, in particular the Texas market.

The recent case of another direct sales company's attempts to stop its distributors from

[19]Plaintiff's Brief, at page 12.

[20] "19. The anti-competition covenants on which Plaintiff insists every Mary Kay independent consultant sign, whether an Independent Beauty Consultant, Unit Independent Sales Director, or Independent National Sales Director such as the Defendant herein, are part of a *concerted and effective effort by Plaintiff to vertically restrain trade by tying up and* ***<u>eliminating potential competition from Plaintiff's independent contractors and other direct sales companies</u>*** *much smaller than Plaintiff who sell cosmetic products similar to Plaintiff's line of cosmetic products, <u>particularly in, but not limited to, the Texas market</u>.* Plaintiff is attempting to restrain Defendant by use of its unlawful non-compete agreement from competing with Plaintiff and those other independent contractors with whom Defendant seeks to recruit to assist her in building her current direct sales business. Such restraints by Plaintiff are unreasonable, and *because Plaintiff has exerted such tight control over its independent contractors, particularly as it applies to attempts to do business in the* ***<u>Texas market</u>*** *for cosmetics*, Defendant has been unfairly damaged, and the growth of her business stunted, economically in an undetermined amount but in no event less than $1,000,000.00 in her efforts to build her business in Texas and elsewhere subsequent to resigning as a National Sales Director with Plaintiff." (Emphasis added)

pursuing their chosen path as newly-minted competitors with their former company was put in proper perspective by the court in *Pampered Chef v. Alexanian* 804 F. Supp.2d 765, 787 (N.D.Ill. 7-14-2011). That court also found that Pampered Chef had not established that its non-compete clause is reasonable and served any other purpose than to shield Pampered Chef from competition:

"In sum, Pampered Chef has not made a clear showing that it has some likelihood of succeeding on the merits with regard to the validity of its non-solicitation clause. While under appropriate circumstances Illinois law recognizes clauses that bar the solicitation of employees, Pampered Chef has not shown that its clause is reasonable and necessary. "[N]o other interest has been established in the record beyond plaintiff's desire to shield itself from ordinary competition." *Reliable Fire Equip. Co.,*405 Ill.App.3d at 736, 940 N.E.2d at 175." Id. at 797

The case of *Jayco Systems v. Savin Business Machines Corp.*, 777 F.2d 306, 313, and fn. 20 (5th Cir. 1985) was an appeal from the Northern District of Texas and dealt with a private party bringing an anti-trust lawsuit in federal court:

"To bring a private, treble damage suit under the antitrust laws, a plaintiff must show that it has standing under § 4 of the Clayton Act, 15 U.S.C. § 15.[fn20] The plaintiff must show that it has suffered injury to its 'business or property' of a type the antitrust laws were intended to prevent."…'Private antitrust liability . . . requires the showing of (1) a violation of the antitrust laws, (2) the fact of damage, and (3) some indication of the amount of damage (citations omitted). The requirement of the `fact of damage,' also called `impact,' means that the antitrust violation must cause injury to the antitrust plaintiff.'"

The anti-trust allegations of Count 2 present a plausible claim as required in *Ashcroft v. Iqbal*, 129 S. Ct. 1937 (2009) for "an adverse effect on competition in the relevant market" under *DeSantis v. Wackenhut Corp.*, 793 S.W.2d 670, 688 (Tex. 1990) and *Am. Chiropractic Clinics, P.C. v. Spence,* 1995 WL 731786 (Tex. App. 1995) cited by Plaintiff in its Brief, based upon the multiplicity of unreasonable agreements insisted upon by Mary Kay with every one of its independent contractors, "whether [they are] an Independent Beauty Consultant, Unit Independent Sales Director, or Independent National Sales Director such as the Defendant herein, are part of a concerted and effective effort by Plaintiff to vertically restrain trade by tying up and eliminating

potential competition."[21]

III. CONCLUSION

Counts 1 and 2 of the Defendant's Counterclaim have stated plausible claims under the Texas DTPA for findings of liability of the Plaintiff under the DTPA for deceptive acts and practices, including for a § 17.46(12) representation and a (21) pyramid promotional scheme, as well as for a § 17.50 (2) breach of warranty and (3) unconscionable action or course of action. Additionally a plausible claim has been made by Defendant in her Counterclaim under the Sherman and Clayton anti-trust acts respectively for unlawful anti-competitive actions taken by the Plaintiff. However, if this Court grants a portion or all of the relief requested by Plaintiff in its Motion to Dismiss, Defendant requests leave to amend her Counterclaim to resolve any and all deficiencies in her pleading found by the Court to exist. Defendant also requests any other legal or equitable relief to which she may be entitled.

Respectfully submitted this 14th day of March, 2012.

/s/ David Eisenstein
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[21]Paragraph 19, Counterclaim, Count 2.

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing DEFENDANT'S BRIEF IN SUPPORT OF RESPONSE TO PLAINTIFF MARY KAY INC.'S MOTION TO DISMISS HER COUNTERCLAIM COUNTS I AND 2 has been served on counsel for the Plaintiff as follows:
[X] BY ELECTRONIC TRANSMISSION:
Through the United States District Court's ECF transmission to the following:

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Dated this 14th day of March, 2012

/s/ David Eisenstein
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