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FRANCHISING: THE EVOLVING RELATIONSHIP BETWEEN FRANCHISORS AND FRANCHISEES

YOUR PRESENTERS



- **Gregg Rubenstein, Partner, Nixon Peabody**
- Practice is focused on franchise and distribution, trade secrets, and employment matters
- Actively litigates and arbitrates franchise cases throughout the country
- Was selected by *Franchise Times* as a 2012 “Legal Eagle” and is a member of the team selected by *U.S. News* as “Law Firm of the Year” in Franchise Law two years in a row



- **Robert M. Einhorn, Managing Partner, Zarco, Einhorn, Salkowski & Brito, P.A.**
- Practices in the area of Franchise, Dealership, Intellectual Property, and Hospitality
- Frequent Speaker at the ABA’s Annual Franchise Forum and other Franchise Industry Events
- 2012 Lawyer of the Year for Franchise Law, South Florida’s Best Lawyers; “Legal Eagle” by Franchise Times Magazine, 2008-2012

PRIVATE EQUITY'S EVOLVING ROLE IN FRANCHISING

- Private equity firms have played an ever increasing role over the last ten years.
- Examples include: Roark Capital, Sentinel Capital Partners, Pouschine Cook Capital Management, Harvest Partners and many others.
- Private equity firms invest both as franchisors and as franchisees.
- Private Equity's presence tends to make franchising more "professional."
- This should benefit both franchisors and franchisees, but may make entry into the market more difficult for those without private equity backing.

SELECT PRIVATE EQUITY PORTFOLIOS

Roark Capital



Sentinel Capital



Pouschine Cook Capital



THE AFFORDABLE CARE ACT

- An Overview of the Act
 - Individual Mandate
 - Insurance Exchanges
 - Medicaid Expansion
 - Employer Mandate
- Supreme Court Decision
 - *National Federation of Independent Business, et al vs. Sebelius*
- Impact on Small Businesses
 - Deter Growth
 - Reduce Staff/Hire More Part Time Workers
 - Raise Prices
 - Practical Effect Unknown

VICARIOUS LIABILITY: WHO IS LIABLE FOR ALLEGED DISCRIMINATION CLAIMS?

- Growing line of cases have attacked traditional separation between franchisor and franchisees for employee discrimination claims.
- Cases focus on required dress policies, control over operations and policies provided by franchisors to assist franchisees.
- How much control is too much control? Can franchisor's "help" in a situation later "hurt" its position?
- If franchisors face potential liability anyways, will they seek to exert more control?

VICARIOUS LIABILITY: WHO IS LIABLE FOR ALLEGED DISCRIMINATION CLAIMS?

- *Myers v. Garfield & Johnson Enters., Inc.* – Court refused to dismiss harassment claim against franchisor despite no allegation franchisor knew of alleged harassment or participated in it. Plaintiff allowed to proceed on basis that franchisor was: (1) “joint employer;” (2) vicariously liable; and (3) ostensible or apparent employer.
- *EEOC v. Papin Enters., Inc.* – Suit brought by EEOC against Subway and its franchisee for religious discrimination. Claim based on employee being dismissed at franchisor’s insistence for violating no facial jewelry policy by wearing a nose ring. Court refused to dismiss case against Subway because its retained ultimate right to issue waiver from policy requirements and franchisor had injected itself into decision making process.

GROWTH OF INDEPENDENT FRANCHISEE ASSOCIATIONS

- Franchise Associations
 - Independent Franchise Associations vs. Franchise Advisory Councils
 - Purpose
 - Why Created
 - Growing voice of its membership
 - The Coalition of Franchisee Associations (CFA) “brings together some of the largest and most reputable independent franchisee associations to form an organization with a mission to leverage the collective strengths of franchisee associations for the benefit of the franchisee community.”
 - Asian American Hotel Association (AAHOA) “one of the fastest-growing organizations in the industry, with more than 11,000 members owning more than 20,000 hotels that total \$128 billion in property value”
 - Advocacy of the Associations
 - Universal Franchisee Bill of Rights
 - Legislative Efforts
 - Impact on Franchise Systems

THE ABILITY TO AVOID CLASS ACTION CLAIMS

- The past few years have seen an increase in franchisees bring claims either as class actions or through franchisee associations.
- These claims tend to “increase the stakes” dramatically versus claims by a single franchisee.
- Two U.S. Supreme Court cases, *Stolt-Nielsen* and *Concepcion*, have given franchisors a way to avoid class claims if they select arbitration as their dispute resolution venue.
- More recent decisions, however, suggest ways for class or class-like claims to be brought in arbitration.
- How will franchisors weigh possibility of having to litigate “high stakes” claims in arbitration with no appeal right with ability to prevent claims being brought at all.

FRANCHISE RELATIONSHIP LEGISLATION

- **Current Types of Franchise Regulations**
 - **Pre-Sale and Post-Sale Regulations**
 - Federal vs. State Legislation
 - No Federal Relationship Laws
- **Franchise Relationship Legislation**
 - **MA-Fair Franchising Act, Senate Bill 01843 (2011)**
 - 90 days notice for termination
 - 90 day written notice of non renewal by franchisor
 - Franchisor liable for encroachment damages
 - **CA-The Level Playing Field for Small Businesses Act of 2012**
 - Contractual agreement to operate in "Good Faith"
 - Notice and cure periods
 - Franchisors would owe a duty of competence to franchisees
 - Dispute resolution alternatives
 - Reasonable transfer of ownership qualifications
 - Penalties for false and deceptive claims made in association with the sale of a franchise
 - **Vermont, House Bill 694 (2012)**
 - **Arizona**

PRIVACY REGULATIONS

- The federal government and states are adopting an ever increasing number of regulations addressing data privacy. For example, California law regarding privacy of emails – Who is responsible?
- Many of the customer loyalty programs in the hospitality sector (and elsewhere) are subject to these regulations.
- This raises many issues concerning who will be responsible for ensuring that programs comply with regulations. Will franchisor insistence on safeguards increase potential for vicarious liability?
- Who owns the data? If the franchisor owns the data, is it responsible for complying with regulations? What about where data is entered by or maintained by franchisees?
- How will be costs be allocated amongst the parties?

MENU LABELING REQUIREMENTS

- Who is responsible for keeping up-to-date on menu labeling requirements instituted on state or city basis?
- Who bears cost of creating compliant menus? Who bears costs for testing required to gather required information? Can franchisors effectively push cost down?
- Who is liable for inaccuracies in menu labels? Can franchisees effectively demand indemnification from franchisors, especially for likely class action claims?
- How will results of menu labeling affect product sales? Will they force systems to develop new products that can more effectively compete in the marketplace?

OTHER CURRENT TRENDS

- **Refranchising**
 - Sale of corporate stores
- **Growth of Multi-Unit Operators and Area Developers**
 - “Biggest growth trend in today’s franchise industry”
 - **Benefits of Multi-Unit Ownership**
 - Franchisor
 - Franchisee
- **Territorial Protection**
 - Offered less and less
 - Impacting franchise sales and relations
- **Franchisor Incentives**
 - Purchase of Franchises
 - Purchase of Required Equipment and Systems
- **Green Initiatives**