The GPMemorandum

TO: **OUR FRANCHISE AND DISTRIBUTION CLIENTS AND FRIENDS**

FROM: **GRAY PLANT MOOTY'S FRANCHISE AND DISTRIBUTION PRACTICE GROUP**

Maisa Jean Frank, Editor of *The GPMemorandum*

Julia C. Colarusso, Editor of *The GPMemorandum*

DATE: **March 6, 2019—No. 239**

Below are summaries of recent legal developments of interest to franchisors. We have also included at the end of this issue a link to a survey prepared by members of our group that details recently proposed and adopted franchise regulations from around the world.

EMPLOYMENT

FRANCHISEE'S EMPLOYEE PLEADS PLAUSIBLE JOINT-EMPLOYER CLAIM

The United States District Court for the District of New Jersey recently held that Zevin Curtis Ward, an employee of a franchised automotive repair business, sufficiently alleged that franchisor Cottman Transmission Systems acted as his joint employer. *Ward v. Cottman Transmission*, 2019 WL 643605 (D.N.J. Feb. 14, 2019). Ward brought claims of workplace discrimination, retaliation, and creation of a hostile work environment under Title VII of the Civil Rights Act of 1964 and the New Jersey Law Against Discrimination, together with allegations of unpaid overtime under the Fair Labor Standards Act. Cottman filed a motion to dismiss, claiming, among other things, that Ward could not plausibly show that Cottman was Ward's employer or joint employer.

In holding that Ward had adequately pleaded a joint-employer relationship, the court pointed to his allegation that Cottman "instructed" the franchisee who owned the shop "on the methods, procedures, and techniques of operating [the location], including business procedures, evaluation of personnel, hours of operation, [and] inspection." The court further observed that portions of the license agreement

between the franchisee and Cottman supported Ward's claims, including provisions that gave Cottman the power to (1) set the minimum days of the week and hours per week the location was open; (2) set the methods, procedures, and techniques used for work at the shop; (3) inspect the premises, books, and records; (4) meet with the location's employees and customers; and (5) assist the location in finding and evaluating personnel. While recognizing that Ward's complaint was imperfect and not exceedingly specific, the court concluded that he plausibly alleged that Cottman exercised control over the manner and means of his work and had some authority in personnel decisions. Accordingly, Ward's allegations were sufficient to state claims under Title VII and the FLSA, and the court denied Cottman's motion to dismiss.

ARBITRATION

FEDERAL COURT HOLDS OHIO BUSINESS OPPORTUNITY LAW DOES NOT VOID ENTIRE ARBITRATION CLAUSE

A franchise agreement's arbitration clause was not rendered entirely void under Ohio's business opportunity laws the Northern District of Ohio recently held, granting the franchisor's motion to stay the federal court proceedings pending arbitration. *Party Princess Toledo, LLC v. Party Princess USA LLC*, 2019 WL 524186 (N.D. Ohio Feb. 11, 2019). After an Ohio franchisee sued Party Princess for a variety of claims arising under the parties' franchise agreement, Party Princess moved to stay the proceedings pursuant to the agreement's arbitration clause, which specifically designated Denver, Colorado as the venue for any arbitration proceeding. Seeking to avoid arbitration, the franchisee argued the clause was void under Section 1334.06(E) of Ohio's business opportunity laws, which prohibits any provision in a franchise agreement restricting venue to a forum outside of the state.

In a measured application of Ohio's business opportunity laws, the court declined to void the entire arbitration clause and instead severed the choice-of-venue provision setting Denver, Colorado as the place of arbitration. Under Section 1334.06(E), "any provision in an agreement restricting jurisdiction or venue to a forum outside of this state . . . is void." The court interpreted this language as only voiding choice-of-venue *provisions* — all other valid provisions contained in the arbitration clause would remain in effect, including the provision that required arbitration of disputes arising under the franchise agreement.

CALIFORNIA COURT FINDS ARBITRATION AGREEMENT ENFORCEABLE DESPITE PROCEDURAL DEFECTS

A California appellate court reversed the trial court's ruling that an arbitration agreement related to a former Papa John's employee was unconscionable in *Spaulding v. PJCA-2 LP*, 2019 WL 517667 (Cal. Ct. App. Feb. 11, 2019). Plaintiff Jason Spaulding began working in a restaurant operated by defendant Papa John's in 2009, and Papa John's later sold the business to a

franchisee, PJCA-2. PJCA-2 offered to continue to employ Spaulding at the restaurant but required him to review and sign a 40-page new hire package, which included a four-page arbitration agreement. Spaulding signed the arbitration agreement but crossed out the word "voluntarily" and wrote "UD" on the first page to indicate that he was signing the agreement under duress. When Spaulding was fired a year later for violating company policy, he filed multiple employment-related claims against PJCA-2, the manager of the restaurant, and Papa John's. PJCA-2 and the manager moved to compel arbitration, and Papa John's joined in the motion on the grounds that it could enforce the arbitration agreement as an agent or third-party beneficiary.

The trial court denied the motion after determining that the arbitration agreement was unconscionable. Under California law, both procedural and substantive unconscionability must be present in order to render a contract unenforceable. The trial court found that the arbitration agreement was procedurally unconscionable because PJCA-2 did not make someone available to answer questions Spaulding may have had about the agreement, did not attach the rules of the American Arbitration Association that would govern the arbitration of any claims, and presented the arbitration agreement on a take-it-or-leave-it basis. Further, the trial court found the agreement substantively unconscionable because it enabled the arbitrator to limit discovery. The defendants appealed the decision.

In its review of procedural unconscionability, the appellate court was unmoved by some of the trial court's conclusions, finding that there was no evidence that Spaulding had any questions about the arbitration agreement, and noted that the AAA rules were easily accessible on the internet. However, the court agreed with the trial court's conclusion that the arbitration agreement was procedurally unconscionable because Spaulding was unable to negotiate the terms of the agreement and was required to sign it as a condition of his employment. In its review of substantive unconscionability, the appellate court disagreed with the trial court's finding, noting that under existing precedent similar AAA rules governing discovery were not substantively unconscionable. Because there was no substantive unconscionability, the appellate court reversed the trial court's ruling.

CONTRACTS

COURT DENIES FRANCHISOR'S MOTION FOR SUMMARY JUDGMENT IN DISPUTE RELATED TO AREA DEVELOPER'S RENEWAL RIGHTS

The United States District Court for the Northern District of Texas has granted in part and denied in part a motion for summary judgment filed by franchisor Pizza Inn in a dispute with one of its area developers. *Pizza Inn, Inc. v. Clairday*, 2019 WL 499105 (N.D. Tex. Feb. 8, 2019). Pizza Inn entered into two area developer agreements with Clairday that permitted Clairday to promote and develop Pizza Inn franchises in Arkansas. The agreements contained a primary

term of 20 years and provided Clairday the option to renew for two additional five-year periods. The parties renewed the agreements for one additional five-year period but disagreed as to whether Clairday properly exercised his right to renew for the second five-year period. Pizza Inn sought a declaratory judgment that Clairday did not have a right to demand a second renewal of the agreements. Clairday then counterclaimed, alleging violations of the Arkansas Franchise Practices Act and breach of contract and seeking a declaratory judgment that he had the right to renew the agreements for the second five-year period. Pizza Inn moved for summary judgment on its declaratory judgment claim and on all of Clairday's counterclaims.

The court denied Pizza Inn's request for summary judgment on the renewal issue. Pizza Inn first argued that the parties had executed a letter agreement that clearly limited Clairday to one renewal period and extinguished his right to a second renewal. The court disagreed, finding that the letter agreement was ambiguous as to whether it extinguished Clairday's right to renew the area developer agreements a second time. Pizza Inn next argued that Clairday had failed to abide by the terms of the area developer agreements and therefore had forfeited his right to renewal. The court denied Pizza Inn's request for summary judgment on that basis, holding that there was a genuine issue of material fact as to whether Clairday had defaulted. The court also agreed with Clairday that strict compliance with the exercise of an option to renew was not necessary and that, despite providing Pizza Inn notice of renewal two months late, the delay only produced *de minimis* harm and therefore was an improper basis for granting summary judgment.

The court also denied summary judgment on Clairday's declaratory judgment and breach of contract counterclaims because material questions of fact existed as to whether Clairday had breached the agreements. However, the court granted summary judgment to Pizza Inn on Clairday's counterclaims for violations of the Arkansas Franchise Practices Act, concluding that the parties' relationship fell outside the scope of the statute because the area developer agreements did not create a franchisor-franchisee relationship.

AREA REPRESENTATIVES

MAJORITY OF AREA REPRESENTATIVES' CLAIMS PERMITTED TO PROCEED AGAINST FRANCHISOR AND ITS OFFICERS

Ruling on a motion to dismiss in a consolidated action, a federal district court in North Carolina held that several Charlie Graingers area representatives alleged sufficient facts to permit fraud and tort-based claims and other similar claims to proceed against franchisor Charlie Graingers and its individual officers. *Trident Atlanta, LLC v. Charlie Grangers Franchising, LLC*, 2019 WL 441187 (E.D. N.C. Feb. 4, 2019). The area representatives claimed that prior to signing their franchise agreements, Charlie Graingers' officers made multiple representations outside of the company's FDD regarding the amount of support Charlie Graingers provides to its franchisees,

the officers' level of experience, and the success of Charlie Graingers franchised businesses. The area representatives signed a closing acknowledgment and general release of claims in connection with the franchise agreements. The area representatives subsequently filed suit against Charlie Graingers alleging multiple claims, including fraud, intentional misrepresentation, concealment, breach of fiduciary duty, RICO-based claims, and breach of contract.

The court held that the area representatives pleaded numerous and sufficient facts to overcome a motion to dismiss filed by the individual officer defendants with respect to the tort and fraud-based claims, including the claim that the defendants violated North Carolina's Unfair and Deceptive Trade Practices Act. The court rejected the officers' arguments that the claims were barred by the signed general release because the area representatives' claim that they were fraudulently induced into signing the franchise agreements also applied to the execution of the release. In addition, the court found that the release violated the Federal Trade Commission's Franchise Rule because it required the area representatives to waive reliance on representations in the FDD, and therefore should not be enforced. The court also permitted the breach of fiduciary duty claims to proceed, ruling that the area representatives alleged sufficient facts to demonstrate the existence of a relationship of trust and confidence rising to the level of a fiduciary duty, and the officers' breach thereof. The court did, however, dismiss the RICO claims.

STATUTE OF LIMITATIONS

NORTH CAROLINA COURT OF APPEALS AFFIRMS THAT CONTRACTUAL LIMITATIONS PERIOD BEGINS TO RUN WHEN FRANCHISEES SIGNED AGREEMENTS

The North Carolina Court of Appeals affirmed a lower court's dismissal of claims against Family Fare, LLC for violations of the North Carolina Unfair and Deceptive Trade Practices Act and for rescission, fraud, misrepresentation, and breach of the duty of good faith and fair dealing on the grounds that the one-year contractual limitations period contained in the franchise agreements at issue expired prior to the franchisees' filing suit. *Sanghrajka v. Family Fare, LLC*, 822 S.E.2d 789 (N.C. Ct. App. 2019). Sanghrajka operated a convenience store under the ownership and control of Family Fare until November 2013, when Family Fare advised Sanghrajka that the store would be converted to a franchise and that she could continue to operate the store only if she agreed to operate a second location. The parties executed franchise agreements relating to the two stores the following month. When Sanghrajka later attempted to sell her businesses, Family Fare required her to pay an amended transfer fee equaling 50 percent of the then-current franchise fee. Sanghrajka then sued Family Fare in May 2017, and Family Fare filed a motion to dismiss the lawsuit on the grounds that it was not filed "within one (1) year from the occurrence of the facts giving rise to such claim or action," as required by the franchise agreements. The trial court granted Family Fare's motion to dismiss.

The appellate court affirmed the trial court's findings that Sanghrajka agreed to the amended transfer fee when the parties signed the franchise agreements in December 2013 and that the one-year contractual limitations period on Sanghrajka's claims began to run on the date they signed the agreements. Because Sanghrajka did not file the action within one year of signing those agreements, or within the three-year limitations period provided under North Carolina law, her claims were barred. The appellate court also affirmed the lower court's decision not to toll the statute of limitations under the "continuing wrong doctrine," reasoning that any of Family Fare's alleged continual unlawful acts were not separate violations but rather an "ill effect" of their actions in December 2013. Finally, the appellate court affirmed the dismissal of Sanghrajka's claims under the North Carolina Unfair and Deceptive Trade Practices Act on the grounds that Sanghrajka's injury was a result of her "failure to read the documents previously provided to her," and not of any deceptive or unfair tactic Family Fare used in negotiating with her in 2013.

INTERNATIONAL

From time to time Gray Plant Mooty prepares a survey of recently proposed and adopted franchise regulations from around the world. A copy of our February 28, 2019 Update may be found here.

We gather the information from many sources, frequently press reports and translations of actual proposals or laws. Thus we cannot guaranty the accuracy or completeness of our reports. If you have questions, please contact a member of our Franchise and Distribution Practice Group.

GRAY PLANT MOOTY

Minneapolis, MN Office

Elizabeth S. Dillon, co-chair (612.632.3284)
Megan L. Anderson (612.632.3004)
* Eli M. Bensignor (612.632.3438)
Sandy Y. Bodeau (612.632.3211)
Phillip W. Bohl (612.632.3019)
Jennifer C. Debrow (612.632.3357)
Ashley Bennett Ewald (612.632.3449)
John W. Fitzgerald (612.632.3064)
* Hannah H. Fotsch (612.632.3340)
* Olivia Garber (612.632.3473)
Michael R. Gray (612.632.3078)
* Karli B. Hussey (612.632.3278)
Gaylen L. Knack (612.632.3217)

Kirk W. Reilly, co-chair (612.632.3305)
Raymond J. Konz (612.632.3018)
Richard C. Landon (612.632.3429)
Mark S. Mathison (612.632.3247)
* Craig P. Miller (612.632.3258)
Bruce W. Mooty (612.632.3333)
Ryan R. Palmer (612.632.3013)
* Max J. Schott II (612.632.3327)
Michael P. Sullivan, Jr. (612.632.3350)
* James A. Wahl (612.632.3425)
Lori L. Wiese-Parks (612.632.3375)
Quentin R. Wittrock (612.632.3382)

Washington, D.C. Office

Mark A. Kirsch, co-chair (202.295.2229)
Samuel A. Butler (202.295.2246)
* Julia C. Colarusso (202.295.2217)
* Maisa Jean Frank (202.295.2209)
Jan S. Gilbert (202.295.2230)
Peter J. Klarfeld (202.295.2226)
Sheldon H. Klein (202.295.2215)
* Thomas A. Pacheco (202.295.2240)
Iris F. Rosario (202.295.2204)
Justin L. Sallis (202.295.2223)
Frank J. Sciremammano (202.295.2232)
Michael L. Sturm (202.295.2241)
* Erica L. Tokar (202.295.2239)
Stephen J. Vaughan (202.295.2208)
Diana V. Vilmenay (202.295.2203)
Eric L. Yaffe (202.295.2222)
Robert L. Zisk (202.295.2202)
* Carl E. Zwisler (202.295.2225)

**** Wrote or edited articles for this issue.***

For more information on our Franchise and Distribution practice and for recent back issues of this publication, visit the **Franchise and Distribution** Practice Group at http://www.gpmlaw.com/Practices/Franchise-Distribution.

Follow us on Twitter: @GPM_Franchise

GRAY PLANT MOOTY

80 South Eighth Street
500 IDS Center
Minneapolis, MN 55402-3796
Phone: 612.632.3000

600 New Hampshire Avenue N.W.
The Watergate – Suite 700
Washington, D.C. 20037-1905
Phone: 202.295.2200

franchise@gpmlaw.com