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Southeast Franchise Forum

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2019 Franchise Legal Update

Bankruptcy – *Mission Product Holdings, Inc. v. Tempnology, LLC*, 139 S.Ct. 1652 (May 2019)

- Tempnology (Licensor) attempted to use Chapter 11 to reject a trademark license agreement with Mission (Licensee) to effectuate termination of Mission's license rights to use the COOLCORE mark
- Question: Does rejection of a trademark license in bankruptcy terminate a licensee's rights (the First and Fourth Circuits' rule) or simply constitute a breach, which may not preclude the licensee's rights to continue using the trademark (the rule in the Seventh Circuit)?
- The Supreme Court ruled that the Bankruptcy Code section 365(g) unambiguously states that rejection of a license or other "executory contract" constitutes a breach (not rescission) of such agreement.
- ***Takeaways for franchising:***
  - *Mission* applies to franchise agreements: franchisors/franchisee beware
  - Outside of bankruptcy, a licensor's breach does not always terminate a licensee's right to use the licensed mark – the license and/or non-bankruptcy law will govern the licensee's rights
  - Option to include Bankruptcy Code 365(n) into franchise agreement terms – but beware that the debtor (licensor) has no further obligations to perform + franchisee still obligated
  - Check the relevant state laws on termination of franchise agreements

Arbitration – *Henry Schein, Inc. v. Archer & White Sales*, Inc., 139 S.Ct. 52 (January 2019)

- Supreme Court held that under the Federal Arbitration Act (FAA) arbitration is governed by contract -- courts must enforce the parties contract terms
- Parties may agree to have the arbitrator decide whether a dispute is the proper subject of arbitration.
- The FAA contains no "wholly groundless" exception and courts may not rule on the potential merits of the underlying claim that is assigned by contract to an arbitrator.
- ***Takeaways for franchising:***
  - To avoid any ambiguity, if the parties want arbitration to decide ALL disputes, the Franchise Agreement should clearly provide for it, e.g., *"Any dispute as to whether this arbitration clause applies or whether any particular claim is subject to arbitration shall be decided by arbitration in accordance with this Section ___."*

Arbitration: *Anonymous* (2019)

- Franchisor dispute with Franchisee Association on applicability of mandatory arbitration clause that prevented class actions or group dispute resolution – Franchisee Association sought declaratory judgement
- Franchisor filed individual actions against the Franchisee Association's Board of Directors to compel arbitration. Placed each Board member franchisee into default for breaching the Franchise Agreement arbitration dispute resolution clause
- Nearly all of the franchisees withdrew from the declaratory judgment action against the franchisor -- some went forward with individual arbitrations

- ***Takeaways for franchising:***
  - Parties cannot ignore the agreed upon arbitration provisions.
  - By taking action, the Franchisor became the plaintiff with its own breach claims (franchisees paid the franchisor to settle)
  - Arbitration led the parties to a resolution where the participating franchisees agreed to exit the system

Misclassification - *Vazquez v. Jan-Pro Franchising International, 923 F.3d 575* (9th Cir. July 2019)

- Ninth Circuit ruled that the "ABC test" (from *Dynamex*) retroactively applies to franchisor-franchisee relationships. **But on July 23, 2019, the Ninth Circuit granted Jan-Pro's petition for a rehearing on the issue of whether the Dynamex ABC test applies retroactively.**
- Vazquez involved various class actions originating in several states where janitor-franchisees alleged that Jan-Pro's "three-tier franchising model" was employed to result in misclassifying the franchisees as independent contractors instead of employees.
- California Supreme Ct. adopted the "ABC" test, **where a franchisee is presumed to be a employee under California's wage-order laws unless the franchisor can prove ALL of the following:**
  I. The franchisee is free from the control and direction of the hiring entity in connection with the performance of the work, both under the contract for the performance of the work and in fact;
  II. The franchisee performs tasks that are outside of the usual course of the hiring entity's business; and
  III. The franchisee is customarily engaged in an independently established trade, occupation or business of the same nature as the work performed for the hiring entity
- The Court held Jan-Pro could be the plaintiffs' employer under the ABC test, despite its three-tier franchise structure where (1) Jan-pro acts as franchisor, (2) the master owner acts as franchisee, and (3) the master owner acts as franchisor to the unit franchisee

Misclassification - *Vazquez (cont'd)*

- ***Takeaways for franchising:***
  - Court distinguished between a test for employee status in tort cases for joint employer liability vs. wage and hours claims
  - The B prong of the ABC test seems to target franchisors – as long as the franchisee is providing a service for the franchisor ***"even indirectly"*** – the franchisor will fail the ABC test and be deemed an employer
  - No contract is necessary – especially, as in Jan-Pro, where the franchisor revenue is tied back to the "franchisee/employee" services
  - Does the franchisor depend on franchisees to conduct its business?
  - Does the franchisor hold itself out as in the business or does it hold itself out as merely a franchisor?

Misclassification - *Franze v. Bimbo Foods Bakeries Distribution, LLC, No. 17-CV-3556(NSR), 2019 WL 2866168 (S.D.N.Y. July 2, 2019)*

- Summary judgment granted in favor or defendant Bimbo - finding no independent contractor misclassification of bread distributors

- ***Takeaways for franchising:***
  - Court found that customers exerted the most control, non-competition provisions were not enforced, and distributors were not integral to Bimbo's bread making business.
  - Court compared drivers to gig-economy workers because drivers could sell their territories at any time but Bimbo could not
  - Distributors enjoyed independent opportunities for profits and losses, despite not having *sole* control
  - New York is a state that does NOT use the ABC test (yet)

Misclassification: Recent Trends-Settlements

- *Alfred v. Pepperidge Farms* (C.D. Cal.)
  - $22.5 million settlement proposed to resolve claims that Pepperidge Farm denied employment benefits to product distributors in California, Massachusetts, and Illinois by misclassifying them as independent contractors (June 2019)
- *Padavano v. FedEx Ground Package System Inc.* (W.D.N.Y.)
  - FedEx Ground agreed to pay $3.1 million to settle claims that it misclassified drivers as independent contractors and made deductions to their pay that violated New York labor law. (April 2019)
- *Flores v. TFI International, Inc.* (N.D. Cal.)
  - $4.75 million settlement of class and collective action claims brought by delivery drivers against Velocity Express, alleging independent contractor misclassification (April 2019)

Misclassification: Recent Trends-Settlements (cont'd)

- *O'Connor v. Uber* (N.D. Cal.)
  - Uber agreed to a $20 million settlement of California lawsuits challenging the company's classification of drivers as independent contractors and not employees (March 2019)
  - Significantly lower than previous proposed settlements because of effect of arbitration agreements
- *Van Dusen v. Swift Transportation* (D. Ariz.)
  - Knight-Swift Transportation Holdings agreed to a $100 million settlement in a class action lawsuit involving roughly 20,000 drivers claiming improper classification as independent drivers rather than full employees. (March 2019)
- *Roxbury v. Snyders-Lance, Inc.* (M.D. Pa.)
  - Snyders-Lance paid $1.6 million to route drivers alleging misclassification as independent contractors. (November 2017)

Independent Contractor v. Employee: Recent Trends-NLRA

- NLRB decision in *SuperShuttle DFW, Inc.* (January, 2019)
  - Involved shuttle-van-driver franchisees of SuperShuttle at Dallas-Fort Worth Airport
    - The Board found the drivers franchisees not statutory employees under the NLRA
    - "[E]ntrepreneurial opportunity, like employer control, is a principle by which to evaluate the overall effect of the common law factors on a putative contractor's independence to pursue economic gain."

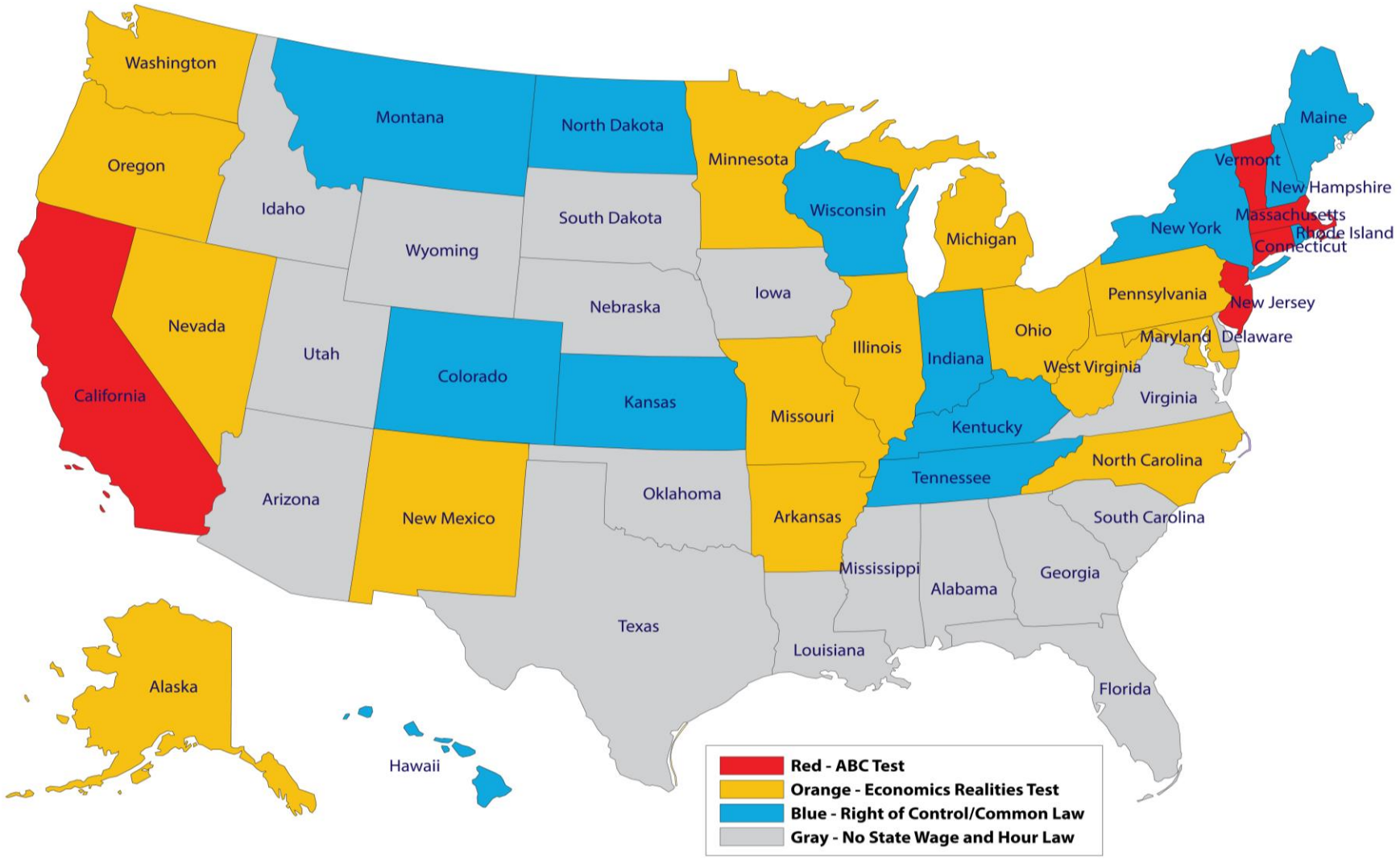
- ***Takeaways for franchising:***

  - NLRB does not apply the ABC test – rather it uses a common law test focusing on the right to control

  - Should be easier than before to show that a worker is an independent contractor under the NLRA

  - Seemingly good news for employers!
    - Decision is limited to NLRA and which workers can unionize

Independent Contractor v. Employee: A Breakdown



No Poaching/No Solicitation: Washington and California Cases

- **WASHINGTON** -- *Stigar v. Dough Inc.* (2:18-cv-00244; E.D. Wash.); *Harris v. CJ Starr LLC* (2:18-cv-00247); *Richard v. Bergey Pullman Inc.*(2:18-cv-00246) – class actions claiming that franchisors (Auntie Anne's, Carl Jr.'s and Arby's) all committed restraint of trade violations by restricting franchisee's from soliciting other franchisee employees. All cases dismissed and settled.
- In March 2019 the Department of Justice (DOJ) chimed in
  - horizontal restraints – "per se" illegal vs. vertical restraints that apply the "rule of reason"
  - agreements among franchisees/among competing entities = per se illegal
  - agreements between franchisors and franchisee = apply rule of reason
- **CALIFORNIA** – *Barker v. Insight Global LLC* (2019 WL 17620 (N.D. Cal. Jan. 11, 2019) invalidated a non-solicitation provision on a regional director prohibited from going after employees/contractors during and 12 months after his employment.
  - Followed illegal restraint of trade ruling in *AMN Healthcare, Inc. v. Aya Healthcare* – 28 Cal. App. 5th 923 (2018) (healthcare employment recruiter non-solicit clause was held invalid).
- ***Takeaways for franchising:*** beware the trend to find restraints of trade if non-solicit/no poaching provisions inhibit employee movement or their ability to do the work they are trained to do

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Marc's practice focuses on intellectual property licensing and franchising in the retail/consumer goods and services areas, fashion/apparel and accessories, and commercial/industrial design, including the drafting, negotiation and enforcement of license and franchise documents and agreements, as well as implementation of branding and commercialization objectives for clients via licensing and franchising. In conjunction with the services above, he counsels clients on creating effective strategies for procuring, protecting and enforcing their global intellectual property assets. He has also participated in and used alternative dispute resolution forums such as arbitration and mediation to enforce intellectual property rights. Marc frequently lectures and writes on intellectual property issues for a variety of intellectual property organizations and publications, including International Trademark Association (INTA), New York State Bar Association (NYSBA) Intellectual Property Section, American Bar Association Forum on Franchising, Association of the Bar of the City of New York Fashion Law Committee, Licensing Industry Merchandisers' Association (LIMA), National Law Journal, IP Strategist and The New York Law Journal, Practical Law, The Licensing Journal.

Marc is listed in the 2019 and the eight years immediately preceding editions of World Trademark Review 1000 – The World's Leading Trademark Professionals. He was recognized as a New York "Super Lawyer" in Intellectual Property by Super Lawyers magazine in 2018 and the eight years immediately preceding, and, for the last seven years, he was named a Top 100 New York Metro "Super Lawyer" in Intellectual Property. Marc has been recognized as an "IP Star" in 2019 and the six years immediately preceding by Managing Intellectual Property magazine. In 2017, he was recognized by Who's Who Legal for Franchising. Marc was named a "Legal Eagle" in 2018 and 2019 by Franchise Times. He was also recommended by Legal 500 US in 2015, 2016, 2017 and 2018 for Copyright and in 2019 for Non-Contentious Trademark Law. In 2013, Marc received the Lexology Client Choice Guide - International 2013 Award and is the sole winner in the Intellectual Property: Copyright category for New York. He was also listed in the 2012 and the four years immediately preceding editions of Chambers USA: America's Leading Lawyers for Business for Intellectual Property: Trademark & Copyright. Chambers noted that Marc has "tremendous business savvy and is tenacious in his work ethic," according to his clients (2012).

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2019 Legislative Update

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Federal Issues

Minimum Wage
Immigration
Elections 2020

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State Issues

HB 324 – Medical Cannabis

HB 479 – Hidden Predator

SB 135 – Workers Comp-$675

HB573 – Min Wage Pre-emp

Business Courts

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Regulatory Issues

Georgia Power Rate Case
Health Inspection-State vs Local
Building Code – State vs Local
Alcohol Three-Tier System

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Mr. McGuire has a general corporate law practice with an emphasis on franchise, M&A and governmental affairs. He has helped companies navigate through local, state, and federal government laws and regulations, and has successfully helped in changing, crafting and passing new laws in many different areas. He has assisted new franchisors starting their business and has assisted mature franchise systems evolve their legal infrastructure to continue to grow their system.

Thank you
Marc & Perry!

See you next month!

Supply Chain / The new reality of warehouse to retail.

9/17/19 the 3rd Tuesday

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