

**FRANCHISE AGREEMENT DRAFTING**

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## INTRODUCTION

A marketer knows that it is much easier to sell a product in which he or she has conviction, and the same applies to awarding franchises. A franchisor is not merely marketing a system, but also a relationship. It is essential to a successful franchise system that a franchisor has conviction both in the core system elements and in the structure of the relationships it is creating. The franchise agreement is the foundation for those relationships.

The best franchise agreement is one that correctly mirrors the business philosophies and strategies of the company that adopts it. For this reason, there is no one “right way” to draft a franchise agreement. The authors’ goal is to outline a variety of elements for the franchise practitioner’s consideration as they work through the sometimes complex task of creating or revising a document that is suitable to the client, the industry and the applicable franchisee profile.

Part I focuses upon the preliminary work counsel must perform in identifying the client’s key business objectives and vulnerabilities. Practical advice on the actual drafting process follows in Part II, including specific text examples. Part III identifies some of the more common flashpoints in standard franchise agreements, with suggestions for balancing marketability and related business risks. It is hoped that counsel involved in revisions to a franchise agreement currently in use in an active franchise system will appreciate the experience-based guidance offered in Part IV for obtaining franchisee buy-in on contract changes. Part V addresses traditional subject areas within a franchise agreement which are often the source of franchise disputes and resulting drafting considerations.

## I. IDENTIFYING THE KEY BUSINESS OBJECTIVES AND AREAS FOR POTENTIAL EXPOSURE

### A. Get to Know the Franchisor's Business

Like any agreement, a good franchise agreement should clearly express the parties' rights and obligations. It should also reflect their business objectives and provide a framework to manage the risks inherent in the franchising business model consistent with those objectives. Although some aspects of being a franchisor or being in a particular kind of business are constant, that does not, for example, make an agreement that works for one restaurant franchisor entirely suitable for the next, or for a franchisor in another industry. Before the drafting process begins, the lawyer needs more than just a good form, the lawyer needs to do some homework about the client and the business.

#### 1. Start by Reviewing the Record

There may be a wealth of written information about the franchisor that could foster an understanding of the business. Here are some examples:

- The franchisor's written business plans
- Its advertising, customer brochures, marketing materials
- Its web site
- News media and trade journal articles on the franchisor
- 10-K or private placement memorandum, if applicable

#### 2. Make Site Visits

The written record will not always convey a complete picture of how a business operates. There is no substitute for first hand experience, which can be acquired in various ways such as patronizing the business to see things through the customer's eyes, taking a tour of an outlet or other physical plant to observe operations first hand and visiting the company offices to get a sense of the corporate culture. Even if no additional insight is gained from site visits, most clients appreciate a lawyer who will step out of the office and into their world. Having a better client relationship alone will make easier the task of learning the client's needs and objectives.

#### 3. Research the Market and the Competition

Knowledge about the market for the client's goods and services and the competition will usually produce a more effective agreement. Looking at market conditions and trends and what competitors are doing can help

identify particular objectives and risks for the client's business. It will also help you in framing a response to Item 1 UFOC requirements.

#### 4. Consider the Competition's UFOCs

If the client's competitors offer franchises, some potential business objectives and areas of exposure can be identified by reviewing their franchise offering circulars. Offering circulars of all California-registered franchisors can be obtained online by accessing the Department of Corporations Cal-EASI search engine at: <http://www.corp.ca.gov/caleasi/caleasi.htm>. For franchisors not registered in California, hard copies of UFOCs can be obtained from other state regulatory agencies, usually for a per page copy charge, and from services like FranData and Franchise Help for a flat fee.

Regardless of the business the client is in, the client's primary objective is to sell franchises. A clearly drafted and comprehensive franchise agreement will not serve the client well if its material provisions are not competitive with those offered by other franchisors who are targeting the same pool of potential buyers. Most prospective franchisees are not intent on owning a specifically branded business. They are searching for a viable business of a general type in a particular investment range and will shop for the best deal. All else being equal, the client may not succeed in franchising if its initial fees and royalty rates are higher or if other key terms are more burdensome relative to those offered by comparable franchisors.

### B. Facilitating the Franchisor's Decision-Making Process

Ultimately, the franchisor must determine what it wants to accomplish in its franchise agreement, what risks it is willing to take and how to manage them. Unless the client's decision maker is a seasoned franchise veteran, the lawyer will probably have to educate the client about the basics -- what the franchise agreement should cover, the different approaches to those subjects and the trade offs of selecting one approach over another. At the end of the process, the client should have an understanding of the issues and a comfort level that the agreement supports its franchising agenda.

#### 1. Intake Interview

As with any new client, you should conduct an intake interview. Even if you are familiar with the business or have an existing client relationship, getting the franchisor to describe the business fundamentals and how franchising fits into the business plan can reveal key information you might

not otherwise discover about the business objectives and potential areas of exposure. Ask the franchisor for an overview of the business, its strengths and weaknesses, and what differentiates it from competitors. Ask why the client wants to enter into franchising and how that fits in with their overall business plans. Ask the franchisor about its expectations for franchising, the perceived benefits and why they believe that franchising offers more advantages than other forms of expansion. The client's expectations may or may not be realistic. Will franchising be the main focus or a supplemental channel of distribution? Ask where and how the client expects to make a profit from franchising and the services they intend to provide to franchisees. Also ask if a franchising-specific business plan, taking into account the costs of franchising, has been prepared and the degree to which success of the plan depends on franchise sales income exceeding costs during periods in which royalty or other income may be low. It is also important to ask about specific business vulnerabilities, like dependence on particular suppliers, as well as the franchisor's long-range plans and exit strategy. If the franchisor has begun franchising, it is imperative to learn the existing franchisee/franchisor dynamics and the franchisor's perception of its role in the relationship. Experienced franchise counsel can prove to be a critical (in both senses of the word) resource for clients new to the realities of franchising.

## 2. Agreement Checklist/Questionnaire and Client Review Meeting

A written checklist or questionnaire covering the elements of a typical franchise program and subjects to address in the franchise agreement is a valuable information gathering tool. A sample checklist is attached in Schedule 1. Even sophisticated clients who are familiar with franchising may find that reviewing a checklist prompts them to consider new issues or alternative approaches.

Many clients will not be inclined to study a written checklist and provide complete and thoughtful written responses. In any case, this list and any client responses to it should be reviewed with counsel to make sure the client understands the issues and clearly communicates the objectives.

The authors' recommended approach is to give the checklist to the client first as "food for thought" and then meet with the client to review the checklist, making notes to refer to during the drafting process. In this meeting, the lawyer can field questions and further explain each subject and the alternatives for handling different issues in the agreement. This meeting provides an opportunity for the client to express its objectives and concerns, consider all the variables and arrive at clear decisions. It will probably take several hours to work through all of the issues, but the time

will be well spent and should result in a product that is more satisfying to the client.

### C. Anticipate and Plan for Problems and Business Innovations

As in most continuing commercial relationships, a franchise includes a variety of risks. Moreover, because franchises are typically granted for periods of five to 10 years or more with renewal options, there is the additional prospect that the relationship and the business itself may need to adapt to survive over the long term. A soundly drafted franchise agreement will include provisions for managing liability as between the parties and to third parties, and allocate the foreseeable risks of conducting the business. It will also allow for innovation that may be needed to meet competition and exploit opportunities that may arise in the future.

#### 1. Risks Associated With Franchise Model of Doing Business

Exposure to the franchisor can come in a variety of forms, including vicarious liability for the franchisee's acts and omissions, nonpayment by the franchisee of amounts due the franchisor or third parties, and franchisee claims against the franchisor (e.g., franchise law violations, breach of contract, fraud, violation of covenant of good faith and fair dealing). Refer to Part V for a discussion of some of the more common friction points in the franchisee/franchisor relationship.

Standard franchise agreement provisions for limiting the kinds of vulnerabilities described above often include:

- Indemnification and insurance requirements appropriate to the business
- Limitation/disclaimer of warranties for goods, computer programs and Web-based services provided by the Franchisor or affiliates
- Monetary caps on liability
- Liquidated damages clauses, e.g., for breach of nondisclosure provisions
- Disclaimers of success or profitability and franchisee acknowledgments that no such promises were made
- Dispute resolution clauses requiring mediation before litigation or arbitration; use of an ombudsman program like the one offered through the IFA or internal franchisee and franchisor representatives
- Personal guaranties by individual owners of franchise entity obligations
- Requirement that franchisee provide franchisor a general release of known and unknown claims upon transfer or renewal of the franchise, on award of an additional franchise or at other points

Planning for damage control should also include a realistic assessment of potential exposure in the context of the client's specific business. In that way, you can better safeguard against and appropriately allocate those risks in the franchise agreement. It helps to review how the client's business works and what sorts of events might cause disruption to it, including a frank discussion with the client about how it might address the problems and what a reasonable outcome would entail for both the franchisor and franchisee.

## 2. Other Business Challenges

There are many areas of vulnerability common to franchising a business that may warrant special attention in the drafting process. Here are a few problem areas and suggestions for how to address them. Part II includes additional drafting tips and sample provisions to help illustrate means of addressing several of these key subject areas.

### a. Site Selection and Pre-Opening Issues

For some businesses and in some market conditions, finding suitable locations for the franchise is difficult. In addition to site selection obstacles, other events that can derail franchise openings include the franchisee's failure to obtain financing or to complete successfully the franchisor's training program. What happens then?

Most franchise agreements give the franchisor the option to terminate in these cases, which could lead to litigation if the franchisee loses not only the time and effort spent on trying to start the business, but the franchise fee as well. One approach to minimize this risk is to provide for a termination option (exercisable by either party or by the franchisor or franchisee, depending on the control desired), whereby the initial franchise fee would be refunded in whole or in part, conditioned on the franchisee executing a release of any claims against the franchisor, returning all proprietary material, and honoring applicable post termination commitments, such as confidentiality and/or non-solicitation requirements. Even when the franchise agreement disclaims franchisor responsibility for site selection and other pre-opening matters, a franchisee seeking redress could sue alleging misrepresentations or franchise law violations. A termination and refund option lets the franchisee recover some or all of its investment, and assuming a release is obtained, limits the franchisor's exposure to claims that might otherwise result from the aborted franchise venture.

Some franchisors simply defer signing the franchise agreement until a viable site is identified and the requisite financing is secured. Using this approach, it is common to use a preliminary agreement so that the

parties have an operative document to work under but are not bound to the franchise agreement if the venture fails in the initial stages.

Some terms to include in a preliminary agreement are: payment of a deposit to be credited to the franchise fee and that may be refundable under specific conditions; a designated territory or area in which the franchisee will look for a site; confidentiality covenants; a time period by which the franchise agreement must be signed or the deposit agreement expires, and acknowledgments by the franchisee that UFOC and agreement delivery requirements have been met and proper holding periods respected.

#### b. Supply Chain Issues

Supplier relationships often create vulnerabilities in the franchising context. This is particularly true if the franchisor designates suppliers, acts as a buyer for redistribution to the franchise system, negotiates terms with suppliers for the franchisees or if the franchisor or an affiliate is a significant supplier, and particularly if the economic model contemplates that a major portion of the franchisor's revenues will be dependent on sales of goods or services to the franchisees.

Franchisees may want the supplier selection process to put the greatest emphasis on providing the lowest price. Franchisors may give equal or higher priority to other factors, like quality control, payment terms, administrative costs, cooperation in marketing and research and development and/or rebates to the franchisor or affiliates or, candidly, income to the franchisor or an affiliate. To avoid misunderstandings that may arise from such differing expectations, the franchise agreement should include express provisions about how suppliers may be selected and reserve complete discretion to the franchisor in this regard, or clearly define any limits on that discretion. The agreement could also disclaim franchisor fiduciary duties relative to supplier relationships and include acknowledgements that rebates or other consideration may lawfully flow to the franchisor, if that is the intent. If the franchisor or an affiliate is a supplier of specific products or services, consider providing then current pricing information with a clearly reserved right to adjust prices, subject to whatever limitations the franchisor/affiliate is willing to entertain, if any. Clear disclosure in the franchise agreement and the UFOC of "lock-in" arrangements whereby the franchisee must obtain items from only the franchisor or an affiliate may also mitigate potential "tying" or other anti-trust claims by the franchisee.

Additional trouble spots include supply constraints, price increases and other supply chain events that negatively affect franchisees. Of course

price and availability will be influenced by supply and demand. Other factors can also cause suppliers to unilaterally change direction to the detriment of franchisees or the franchise system. They can raise prices and tighten credit terms. They can make previously limited goods widely available to competitors or constrain distribution channels by terminating relationships with existing purchasers. They may go out of business leaving the franchise system scrambling for alternative sources. Consider counseling the franchisor to implement supplier agreements, which may help balance these risks with supplier indemnifications, complaint monitoring tools and/or financial reporting requirements that can provide early warning of a supplier in operational or financial trouble. Where the system is dependent on third party suppliers for key goods or services, consider including franchise agreement language that disclaims or limits the franchisor's responsibilities for continuity of supplier relationships, supplier imposed pricing or payment terms and related matters that are beyond the franchisor's control.

#### c. System Attrition and Location Control

Even successful franchise systems can be vulnerable to loss of established franchisees. Some franchisees may elect not to renew at expiration, transfer to new owners, or terminate the agreement, regardless of whether it permits termination by the franchisee. Various reasons exist for franchisee attrition, but most are based on financial considerations. Perhaps the franchisee thinks a better return on investment could be found elsewhere or that the brand and other benefits are not worth the fees being paid.

Franchise agreement provisions cannot independently increase the real or perceived value of the franchise or restore a failing franchise relationship. However, there are some franchise agreement provisions and ancillary agreements that could limit the exposure to these events, such as:

- Inclusion of a franchisor right of first refusal to be exercised on any transfer of the franchise, its assets or where the transfer would change the controlling interest in the franchisee entity. One drafting tip, to deal with offers designed to circumvent the franchisor's right of first refusal, is to include language that permits the franchisor to excise from the offer to purchase any assets or terms included in the original offer that are unrelated to the operation of the franchise, and that allows the franchisor to pay the cash equivalent of any non-cash consideration.

- Inclusion of rights to purchase the franchised business on termination, non-renewal or expiration for any reason, with a method for valuation that would survive judicial scrutiny, if contested.
- If the franchisor does not lease or sublease the premises to the franchisee, use of a collateral assignment of lease form, accepted in writing by the landlord, that permits the franchisor to assume the lease on enumerated events, e.g., termination, non-renewal, the franchisee's uncured default under the lease or otherwise.
- If the franchisor is the primary tenant on the lease for the franchisee's premises, consider a sublease over an assignment. Although subleasing may negatively affect the franchisor's financial statement, it at least provides a better means for the franchisor to assert its rights to possession. An assignment leaves the franchisor with secondary liability to the landlord for the franchisee's default but without the rights to bring an unlawful detainer or similar proceeding that would be available to the holder of a leasehold interest as a sublessor.
- Geographically and temporally reasonable noncompetition agreements
- Reasonable liquidated damages clauses for premature termination by the franchisee

### 3. Drafting for Changing Needs of the Business

Considering the life of a typical franchise agreement, some modifications in the business will probably be required to keep pace with the demands of a changing marketplace. Factors that can drive adaptation include, among others, the entry of new competitors, changes in the target market for the goods and services, evolving consumer expectations, new legal regulations, and innovative technology.

It is common to provide for the franchisor's ability to modify the franchise system via changes to the operations manual. However, if certain kinds of modifications are foreseeable, addressing them in the agreement should reduce the possibility of conflict over what changes were anticipated and should be permitted. Refer to Part II, C. 2. for specific examples of provisions for facility upgrading.

In the drafting process, the lawyer and client might ponder the following questions to provide for the needed flexibility in the agreement: What is the current business climate for the client's type of goods and services? Is

the market stable or in flux? How might it evolve and how might the business need to adapt to maintain or grow market share and keep up with competition? Who are the customers, could the customer base be different in the future and how might their needs and demands change over time? What are competitors doing and is that going to influence the direction of the client's business? Is it likely that new ways of delivering the goods and services would be required? What sorts of technological improvements might the franchisor want to make as it grows the business (e.g., Intranets, centralized reservations or customer service, unified point of sale systems)?

The foregoing factors may influence how to draft for a range of issues, including whether to grant and how to define territory rights, the extent of renewal rights, and whether to impose sales quotas. System-wide modifications may be more clearly addressed in the agreement with some knowledge of market trends and technology needs for the client's business. Some provisions to consider drafting include those that permit or require use of or participation in a national accounts program, debit card payment systems, gift card and warranty programs, delivery of goods and services by traditionally over-the-counter businesses, and the addition of related product lines and services.

## II. THE DRAFTING PROCESS

### A. Plan the Process

Just as the content and coverage of franchise agreements may vary by industry and by attorney, so does the drafting process. As stated in the Introduction, there is no one "right way" to draft a franchise agreement. The goal is to create a document that clearly establishes the parties' rights and obligations, defines the relationship and addresses the elements specific to the business, all while balancing the need for flexibility that must be attendant to a contract that in many situations may be one to two decades in length. A well thought-out and thorough drafting process is key to achieving this goal. Attorneys have different drafting styles and approaches and franchisors have different company structures and levels of attention and resources devoted to the franchise process. This section attempts to provide some tips and best practices for how to approach the drafting of a franchise agreement, whether it is the first program for a company just beginning to franchise or a rewrite of an existing document.

#### 1. Seek Experienced Assistance

The franchise agreement is a complex document that must take into account the various nuances of franchise laws, particular aspects of the franchisor's business and system and the culture and relationship a company has, or wishes to develop, with its franchisees. For these

reasons, it is important to draft with a healthy background in contract drafting and franchise law and a good understanding of the franchisor's business. Simply put, a good franchise lawyer is a key element a good franchise agreement and is well worth the investment of time and money. If you are new to franchising and in-house, hire a quality transactional franchise lawyer to assist you with the process. If in private practice, be sure to work with an experienced mentor to help guide the way. An experienced transactional attorney may have the wherewithal to draft an excellent contract, but may not foresee some of the areas of conflicts with franchisees that can be avoided with proper drafting. Similarly, an attorney with years of franchise litigation experience but no extensive experience in contract drafting may unknowingly include (or fail to include) provisions that do not clearly and adequately address the contemplated business model and its effects on the relative rights and obligations of the franchisor and franchisee.

## 2. Assemble Models and Tools

As with drafting most types of contracts, it is common practice to start with a "form" document. Start with a well-drafted franchise agreement that is appropriate for the industry so as to cover the unique areas of the business. For instance, the terms of a home-based service franchise will vary significantly from the terms of a restaurant franchise. Also, make sure the agreement suits your style of writing and is well organized so that the provisions are presented logically throughout the text. Your firm may have examples, and you can find offering circular and franchise agreement examples by using the following resources (this list is not exhaustive, and note that some services may require a fee to obtain the documents).

- [www.franchise.org](http://www.franchise.org). The International Franchise Association's official website offers articles on franchising available for download and contains a comprehensive list of other publications for purchase.
- <http://www.abanet.org/forums/franchising/home.html>. Similar to the IFA's site, this site for the American Bar Association's Forum on Franchising offers publications for purchase and numerous articles to download free of charge.
- [www.corp.ca.gov](http://www.corp.ca.gov). California is the first state to provide online access to franchise documents. Log on to the Department of Corporation's home pages and click on the "Cal-EASI" link (currently <http://www.corp.ca.gov/caleasi/caleasi.htm>) to search and view uniform franchise offering circulars (franchise agreements are often listed as a separate exhibit).
- [www.frandata.com](http://www.frandata.com). FRANdata is one of the companies that offer franchise documents for purchase. Unlike the California website,

Fradata can provide access to most franchise programs, even those that are not registered in California.

A critical first step in drafting a good franchise agreement is to get to know the franchisor's business. If time and resources permit, schedule a visit to the franchisor's home office – this helps the attorney become acquainted with the organization as well as the business, which can prove invaluable for getting appropriate and complete details that are necessary for a clear and comprehensive franchise agreement – not to mention what it does to improve the attorney-client relationship. To help alleviate some of a franchisor's anxiety and avoid some frustrations that may be attendant to tackling the process of drafting a franchise agreement, establish a timeline by which to gather information from the client, provide drafts, receive feedback and discuss revisions, incorporate the agreement into the offering circular and, ultimately, file with the appropriate state authorities.

### 3. Gather the Business Terms

Many attorneys provide the franchisor with what is known as a “Franchise Questionnaire” or “Franchisor Checklist” to gather basic data about the company and the franchise offering, as discussed in Part I. The answers to this series of questions presents a picture of the franchisor's system and gives concrete details regarding specific deal terms that you can easily incorporate into a form document. Refer to Schedule A for a sample checklist. Once you receive the client's responses, you will need to discuss the answers with the franchisor and not simply rely on what is on paper. Further, it is important to discuss the answers with the appropriate person in the organization. Often a franchisor has an individual designated to be responsible for “Franchising,” but his or her focus may be on sales and development, and not on other aspects that must be discussed and understood when drafting the agreement, such as training, operations, finance, retail-level marketing and purchasing. If possible, request that you meet and have discussions with numerous people within the franchise organization to get an accurate assessment of what needs to be described in the franchise agreement. Refer to Part I for additional suggestions on how to approach the fact-gathering process.

#### B. Applying the Business Model to “Standard” Franchise Provisions

Certain provisions are common in a majority of franchise agreements and the franchisor will look to the attorney for guidance about what to include. Do not, however, let the franchisor skim over these provisions, as even the most routine provision may or may not be appropriate for an industry or a particular business, for whatever the reason.

For instance, all franchise agreements are likely to include a section on trademark standards and requirements. The common subheadings for this section include: trademark ownership, trademark use, restaurant/store/unit identification, litigation and changes or modifications to the trademarks. A comparison of numerous franchise agreements would show that the language used throughout this section varies little from franchise agreement to franchise agreement. Remember, however, that the trademark or service mark is at the heart of any franchise system and although the language used is largely the same from agreement to agreement, there are specific details that need to be discussed with the franchisor. For instance, the attorney must verify the owner of the trademarks (the franchisor? its parent? an affiliate?). Other provisions need to be discussed with the client to determine preferences. For instance, a franchisor may wish to give the franchisee a length of time in which to comply with trademark changes, due to the costs involved, whereas others will require an immediate change. The authors' suggestion for "standard" franchise agreement provisions is to draft sample language to review with the client and modify to tailor to the franchisor's business and approach.

Several other provisions for which you can have common language and then modify accordingly after a discussion with the franchisor include:

- **Definitions Section.** Certain definitions, such as Trademarks and Gross Sales, often will be standard. Other definitions will be unique to the franchise system and will require substantial input from the franchisor. For ease of reading the franchise agreement, at least by non-lawyers, the definitions section may be best placed at the back of the agreement, particularly if the section is lengthy.
- **Renewal Provisions.** The conditions a franchisee must meet to renew a franchise agreement are often numerous, but many industries share the same criteria, including signing a new franchise agreement, becoming current on payments, meeting current system standards, providing a release, etc.
- **Default and Termination.** Agreements typically provide for a process by which a franchisor may terminate the franchise agreement. Events of default, notice required and cure rights are detailed in this section. Clients will look to the attorney to assist with the provisions addressing these issues, particularly if it is a new franchisor that has not yet dealt with a default or termination situation.
- **Boilerplate.** Typically one of the last sections of the franchise agreement, it contains straightforward provisions common in all franchise agreements, including "severability," "notices," "references" and "authority." Take care when drafting "boilerplate" provisions; as described further below, they can be a trap for the less experienced drafter and can be of critical importance in litigation.

Bear in mind that because a particular term may be common in an industry does not necessarily mean that it will not be contentious. Refer to Part V for various terms which have been the subject of franchisee/franchisor disputes.

### C. Attorney as Educator – Addressing the Sensitive Issues

Another category of franchise agreement provisions can be summarized as those provisions that address sensitive issues – those terms defining rights and obligations that may cause tension between the franchisor and franchisee or be a target for liability. For the following provisions, particularly for start-up franchisor clients, the franchise attorney has the role of educator.

Similar to the suggestion above regarding standard franchise agreement language, the authors' tip is to prepare sample language and then consult with the client to determine which details are vital to the franchisor's business. It is important that you and the franchisor feel comfortable with the document, and that you and persons within the franchise organization are able to deliver a rationale for the franchise agreement and each of its provisions, particularly those that might be objectionable to a franchisee (or prospective franchisee) or her counsel. It also is essential that the franchisor's sales team understands and can explain the rationale for including such provisions, as this explanation often can prove decisive. The team's understanding will be beneficial to the sales process, as well as throughout the franchisor/franchisee relationship.

#### 1. Territory Terms

If you are new to franchising and have not yet heard of "Scheck," this paper will be the first of many mentions. Scheck v. Burger King Corp., 756 F. Supp. 543, (S.D. Fla. 1991); Bus. Franchise Guide (CCH ¶ 9760. The Scheck decision and its progeny are often cited, discussed and debated, and have resulted in franchise attorneys significantly expanding the territory protections and limitations set forth in the franchise agreement. The territory terms in a franchise agreement should address the franchisor's reservation of rights as well as the franchisee's territory protection. Even if the franchise agreement specifically states that a franchisee has no territorial protection, the development and operational activities in which the franchisor is entitled to engage should be delineated.

Well drafted territory provisions will clearly address questions such as the following:

Should the franchisee be given any territorial or similar rights? What rights does the franchisor have or should it reserve regarding expansion of locations (franchised or company-owned) and other methods of distribution? Is a right-of-first-refusal in favor of the franchisee a

reasonable balancing of the interests of the franchisee and the franchisor? Can the franchisor conduct, or franchise others to conduct, businesses that operate under a different trademark? Or offer goods or services to different classes of customers (retail, wholesale, governmental, etc.)? Or through alternative channels of distribution, such as kiosks, within other businesses, on airports, casinos, campuses or military bases, through mail order or the internet?

The answers to these questions are very particular to the industry and to the individual business. The authors suggest avoiding the use of the word “exclusive.” The term is inherently ambiguous and often carries a connotation of greater weight than what is commonly intended by the franchisor. Instead, use a term such as “designated” and take care to clearly describe in full detail what is intended with any grant of protected territory. It is important that any designated territory rights be specifically delineated in the franchise agreement.

The following sample clauses address the questions above. As with any sample language provided throughout this paper, please note the need to carefully consider the specific business model, industry and unique issues at hand and adapt the language accordingly before incorporation into any franchise agreement.

*Nonexclusivity; Our Reservation of Rights.* The license is limited to the right to develop and operate one Restaurant at the Authorized Location located in the Designated Area, and does not include (i) any right to sell products and Menu Items identified by the Trademarks at any location other than the Authorized Location, except for authorized catering and delivery services as noted in subparagraph X, or through any other channels or methods of distribution, including the internet (or any other existing or future form of electronic commerce), (ii) any right to sell products and Menu Items identified by the Trademarks to any person or entity for resale or further distribution, or (iii) any right to exclude, control or impose conditions on our development of future franchised, company or affiliate owned restaurants at any time or at any location. You acknowledge that the consumer service area or trade area of another ABC restaurant may overlap with your Designated Area.

You also acknowledge and agree that we and our affiliates have the right to operate and franchise others the right to operate restaurants or any other business within and outside the Designated Area

under trademarks other than the ABC Trademarks, without compensation to any franchisee, except that our operation of, or association or affiliation with, restaurants (through franchising or otherwise) in the Designated Area that compete with ABC restaurants in the video entertainment oriented, fast casual restaurant segment will only occur through some form of merger or acquisition with an existing restaurant chain (except as otherwise provided for in this subparagraph). Outside of the Designated Area, we and our affiliates have the right to grant other franchises or develop and operate company or affiliate owned ABC restaurants and offer, sell or distribute any products or services associated with the System (now or in the future) under the Trademarks or any other trademarks, service marks or trade names or through any distribution channel or method, all without compensation to any franchisee.

We and our affiliates have the right to offer, sell or distribute, within and outside the Designated Area, any frozen, pre-packaged items or other products or services associated with the System (now or in the future) or identified by the Trademarks, or any other trademarks, service marks or trade names, except for Prohibited Items (as defined below), through any distribution channels or methods, without compensation to any franchisee. The distribution channels or methods include, without limitation, grocery stores, club stores, convenience stores, wholesale, hospitals, clinics, health care facilities, business or industry locations (e.g. manufacturing site, office building), military installations, military commissaries or the internet (or any other existing or future form of electronic commerce).

You acknowledge and agree that certain locations within and outside the Designated Area are by their nature unique and separate in character from sites generally developed as ABC restaurants. As a result, you agree that the following locations ("Special Sites") are excluded from the Designated Area and we have the right to develop or franchise such locations: (1) military bases; (2) public transportation facilities; (3) sports facilities, including race tracks; (4) student unions or other similar buildings on college or

university campuses; (5) amusement and theme parks; and (6) community and special events.

2. Modernization requirements (timeline and expenditures)

Franchise Agreements typically require franchisees to remodel the business premises as a condition to certain events, such as renewal or transfer. However, a franchisor may wish to have the ability to require modernization or remodeling *during* the initial term of the agreement, particularly in franchise agreements that grant an initial term of significant duration. Language such as the sample text below affords the franchisor some flexibility to make changes or upgrades it feels necessary to the business, while giving the franchisee some comfort by way of capping the required expenditures and defining the timeline involved.

*Modernization or Replacement.* From time to time as we require, you must effect items of modernization and/or replacement of the building, premises, trade dress, equipment and grounds as may be necessary for your Restaurant to conform to the standards for similarly situated new ABC restaurants. The maximum cumulative amount (the "Maximum Modernization Amount") that you may be required to spend during the initial term of this Agreement is established as follows:

You will be required to spend no more than \$XXX during the initial 10 years of this Agreement and \$XXX during years 11-15. If we do not require you to spend \$XXX during the first 10 years of the Agreement, we may require you to spend the remaining amount, in addition to the \$XXX, during years 11-15. If we do not require you to spend \$XXX during the first 15 years of this Agreement, we may require you to spend the remaining amount up to \$XXX during years 16-20.

Notwithstanding the prior paragraphs, we will not require you to make any modernization expenditures during the first three years of this Agreement. Thereafter, however, you must complete to our satisfaction any changes we require within 24 months from the date you are notified of any required changes.

Each and every transfer of any interest in this Agreement or your business governed by Paragraph X or renewal covered by Paragraph X is expressly conditioned upon your compliance with these

requirements at the time of transfer or renewal without regard to the Maximum Modernization Amount.

The Maximum Modernization Amount does not include any required expenditures for equipment or leasehold improvements necessary to prepare new product offerings. Furthermore, you must perform general, continued maintenance and refreshing of the Restaurant premises whenever necessary as set forth in subparagraph X and at a cost not included in the Maximum Modernization Amount.

You acknowledge and agree that the requirements of this subparagraph are both reasonable and necessary to insure continued public acceptance and patronage of ABC restaurants and to avoid deterioration or obsolescence in connection with the operation of the Restaurant. If you fail to make any improvement as required by this subparagraph or perform the maintenance described in this subparagraph, we may, in addition to our other rights in this Agreement, effect such improvement or maintenance and you must reimburse us for the costs we incur.

Part V of this paper addresses sensitive issues in addition to the ones above and provides drafting approaches to consider.

#### D. Know What Not to Include

Arguably just as important as knowing what to include in a franchise agreement is knowing what *not* to include. Unnecessary, ambiguous and superfluous language makes the goal of having a clear franchise agreement all the more difficult to achieve.

##### 1. Excess Language in the Recitals

Keep the franchise agreement recitals simple and advise the franchisor not to include any unnecessary detail. Fraud claims based on a franchise agreement's recitals rarely succeed. Nonetheless, it is prudent to bear in mind that the purpose of a franchise agreement is not to serve as a sales tool. Although it may be tempting to extol the "uniqueness" of the system or the ability of franchisees to achieve "maximum results," it is best to steer clear of this type of language.

## 2. Judicial Use of the Word “Discretion”

A more recent trend among franchise attorneys is to minimize the use of, or advise against using, the word “discretion” in franchise agreements. Three key reasons contribute to this position. First, the use of discretion is often superfluous, as a franchisor intends to mean that the right to do something is absolute. It is clearer to simply claim something as an absolute right. Second, using discretion inconsistently can lead to unintended interpretations of an agreement’s terms. Finally, courts have applied the common law standard of “good faith and fair dealing” to situations in which the franchise agreement clearly states that the franchisor may act in its “sole discretion.” In Carvel Corp. v. Baker, the court held that the covenant of good faith limits the exercise of discretion in the franchisor’s decision to expand distribution to supermarkets. 79 F. Supp. 2d 53, 65-66 (D. Conn. 1997); Bus. Franchise Guide (CCH) ¶ 11,208.

To avoid an uncertain interpretation and perhaps unintended consequences, consider removing any unnecessary references to discretion and adding language that clarifies the drafter’s motivation for, or proposed construction of, specific term choices.

*Interpretation of Rights and Obligations.* The following provisions apply to and govern the interpretation of this Agreement, the parties’ rights under this Agreement, and the relationship between the parties:

*Our Rights.* Whenever this Agreement provides that we have a certain right, that right is absolute and the parties intend that our exercise of that right will not be subject to any limitation or review. We have the right to operate, administrate, develop, and change the System in any manner that is not specifically precluded by the provisions of this Agreement, although this right does not modify any express limitations set forth in this Agreement.

*Our Reasonable Business Judgment.* Whenever we reserve discretion in a particular area or where we agree to exercise our rights reasonably or in good faith, we will satisfy our obligations whenever we exercise Reasonable Business Judgment in making our decision or exercising our rights. Our decisions or actions will be deemed to be the result of Reasonable Business Judgment, even if other reasonable or even arguably preferable alternatives are available, if our decision or action is intended, in whole or significant part, to promote or benefit the

System generally even if the decision or action also promotes our financial or other individual interest. Examples of items that will promote or benefit the System include, without limitation, enhancing the value of the Trademarks, improving customer service and satisfaction, improving product quality, improving uniformity, enhancing or encouraging modernization and improving the competitive position of the System.

### 3. Legalese, Passive Voice, and Verbosity

Legalese, passive voice and verbosity can all detract from the goal of having a clear, concise and easily readable franchise agreement. The complexity of the franchise relationship certainly can result in lengthy terms and provisions; however, it is prudent to use plain English wherever possible and be candid about the franchisee's requirements. There is a common tendency to want to soften requirements. Some franchisors might prefer to say, "you shall be required to..." rather than, "you must..." It is the authors' experience, however, that franchisees generally prefer knowing clearly where each party stands. Clouding over obligations with modifiers may serve only to create room for dispute. Further, the UFOC Guidelines specifically require the offering circular be drafted in plain English. Although a state is unlikely to comment on the franchise agreement, it is wise to have consistency throughout the UFOC and its various exhibits.

### 4. Control Over Day-to-Day Business

Throughout the document, be sure to carefully assess the franchisor's controls over the franchisee so as to limit the franchisor's risk. Placing too much control over a franchisee's business may, at best, lead to resentment from franchisees over a sense of micromanagement, and, at worst, can expose the franchisor to legal liability in the form of a vicarious liability claim. Consider carefully the controls a franchisor desires and discuss options for how to address the issues, while best protecting the franchisor. For instance, a restaurant franchisor may want the right to approve general managers at a franchisee's location, stemming from a negative personnel experience. However, a better approach is to indicate that a general manager must meet the franchisor's then current qualification requirements. Also, a franchise agreement can contain language that expressly disclaims a certain level of control. Sample provisions include:

Any required standards exist to protect our interests in the System and the Trademarks and not for the purpose of establishing any control or duty to take control over those matters that are reserved to you.

You acknowledge that you are an independent business and responsible for control and management of your Restaurant, including, but not limited to, the hiring and discharging of your employees and setting and paying wages and benefits of your employees. You acknowledge that we have no power, responsibility or liability in respect to the hiring, discharging, setting and paying of wages or related matters.

#### 5. Unnecessary or Inappropriate Provisions

While specificity may be the key to a better territory provision (as noted in a previous section), some subject areas lend themselves to drafting with a broader brush. This may be the case for some topics that are the subject of specific, detailed descriptions in the offering circular. For example:

*Training.* You must, at your expense, comply with all of the training requirements we prescribe for the Restaurant to be developed under this Agreement. The Control Person, the Unit General Manager and at least one of your assistant managers must attend training and complete training to our satisfaction. The training requirements may vary depending on our assessment of the experience of the Control Person, the Unit General Manager and the assistant managers or other factors specific to the Restaurant. In the event you are given notice of default as set forth in subparagraphs A and B and the default relates, in whole or in part, to your failure to meet any operational standards, we have the right to require as a condition of curing the default that you, the Control Person, the Unit General Manager and the assistant managers, at your expense, comply with the additional training requirements we prescribe. Any new Control Person or Unit General Manager must comply with our training requirements immediately after being appointed by you. Under no circumstances may you permit management of the Restaurant's operations by a person who has not successfully completed to our reasonable satisfaction all applicable training we require.

Contrast the foregoing paragraph with a typical training disclosure in Item 11 of the UFOC, which may be several pages in length, including charts and footnotes. Using Item 11-type specificity in the Franchise Agreement could tie the franchisor's hands in the event it wished to revise some aspects of its training program.

Another example of such a contrast is the Approved Suppliers disclosures in Item 8, which are not only lengthy, but also must meet strict and detailed requirements. It is common for the franchise agreement, however, to state simply the following:

*Approved Supplies and Suppliers.* We will furnish to you from time to time lists of approved supplies or approved suppliers. You must only use approved products, services, inventory, equipment, fixtures, furnishings, signs, advertising materials, trademarked items and novelties, and other items or services (collectively, “approved supplies”) in connection with the design, construction and operation of the Restaurant as set forth in the approved supplies and approved suppliers lists, as we may amend from time to time. Although we do not do so for every item, we have the right to approve the manufacturer, distributor and/or supplier of approved supplies and in some instances, require that you use designated sources or suppliers. Along with a number of other approval criteria, to be an approved supplier, the supplier must have the ability to provide the product and/or service, on a national basis, to at least 80% of the then existing Restaurants. You acknowledge and agree that certain approved supplies may only be available from one source, or a limited number of sources, and we or our affiliates may be that source or among that limited number. All inventory, products, materials and other items and supplies used in the operation of the Restaurant that are not included in the approved supplies or approved suppliers lists must conform to the specifications and standards we establish from time to time.

Another way to maintain flexibility is to cross reference the operations manual throughout the franchise agreement. System standards and requirements that are likely to evolve over time are best treated in an operations manual, which can be revised as necessary. Too much detail in the agreement may be cumbersome and present barriers to system-wide change. For an in-depth discussion on the interplay between manuals and the franchise agreement, see Maslon, et. al. *Franchise Agreement Drafting*, IFA’s 38th Annual Legal Symposium (May 8-10, 2005).

#### E. Evolving the Agreement with the System

The franchise agreement, particularly in its first few years, should evolve as the franchisor experiences issues that arise in the sales process or present obstacles

to the franchisor/franchisee relationship. Even for mature franchise systems, case law developments often warrant a reassessment of an existing franchise agreement provision. Keep a list throughout the year of case law updates, recommended new approaches to standard terms, issues arising in the sales process and problems occurring in the franchise relationship. Consult with the various departments within the franchise company and determine the challenges over the past year. Circulate a draft of revisions to the appropriate persons at the franchisor for review and comment, and plan on using the franchise registration renewal process as a tool to improving your franchise agreement. As the franchise system matures, consider whether bringing franchisees into the process is appropriate, as further discussed in Part IV.

### III. BALANCING MARKETABILITY AND RISK IN THE FRANCHISE AGREEMENT

A few concepts may be so rock solid or promising that it scarcely matters what the agreement provides; people will buy the franchise. Also, it may be true that some prospective franchisees never read the franchise agreement or consult an attorney for its review. But a typical franchise agreement can only go so far in favor of the franchisor before scaring away prospective franchisees--likely the more qualified ones with enough business savvy to recognize an unfavorable deal when they see it. For most companies, the franchise agreement must roughly reflect the actual bargaining power between the parties or selling it will be difficult. The challenge is how to provide reasonable protection for the franchisor without alienating prospective franchisees.

#### A. Common Points of Tension Between Marketability and Risk

Here are some common flashpoints where the legitimate interests of the franchisor and franchisee may collide, and some proposals for how they might be resolved.

##### 1. Protected Territory Versus Market Penetration

Franchisees want strong territory rights to safeguard their ability to grow the business in their market area and protect against encroachment from other outlets or channels of distribution that the franchisor may establish. Franchisors are reluctant to award absolute exclusivity. Tying up territories reduces the options for growing their businesses and may leave them and their franchisees exposed to a competitor subsequently entering the market, "locking up" advantageous locations and eventually establishing a dominant market share and degree of consumer awareness. Franchisees may not develop the market for the goods and services in the territory up to the franchisor's expectations. Some may resist adapting changes that are needed to retain and grow market share. Even successful franchisees are not always positioned to respond to what the market demands, including new ways of delivering goods and services

or more complex customer requirements or willing to take the risks associated with opening additional units. In addition, protected territories may make it harder to sell the franchise company, if that is part of the franchisor's business plan, and lack of clarity as to franchisee's territorial rights may be even more fatal to a possible acquisition.

To keep all their options open, some franchisors choose not to award any type of territory protection. This approach may not be realistic, particularly if competing franchisors award territory or marketing rights. There are several compromises that offer each party some assurance that their business will not be stymied in the future.

- Rather than granting a larger geographic territory, the franchisor can offer the franchisee a right of first refusal or an option to acquire additional franchises in a defined market area. A drafting tip is to condition the exercise of the rights on the franchisee remaining in good standing and being able to demonstrate adequate financing and other qualifications necessary to be a multi-unit operator.
- If a protected territory is granted, its continuation could be based on the franchisee achieving certain sales goals with a provision that, if those levels are not reached by specified dates, the protection is reduced or withdrawn. Implementing a rational means of establishing these goals and enforcing them can, however, prove quite difficult, so caution must be exercised. In addition, the wisdom of placing another unit in the territory of an underperforming franchisee is questionable if the market cannot support both.
- Retaining territory rights can also be conditioned on the franchisee continuing to follow the system as it is modified over time, for example, by offering new goods or services as may be required in the future.

Sometimes the issue is not about more locations, but about the need to deliver goods or services to particular customers in different ways, for example, under a national accounts contract or by direct sales, or through a different brand. The franchise agreement could provide that franchisees may participate in national account business in their markets at agreed rates. With other kinds of encroaching sales, the franchisor could use a percentage of the revenue to compensate the franchisee (either by making unrestricted payments or paying for additional advertising or other assistance). Similarly, an agreement could provide that the franchisee's rights extend only to the licensed brand.

However you choose to approach the subject of territory protections, clarity is key. Refer to Part II, C. 1, for illustrative provisions.

## 2. Post Termination Noncompetition Covenants

Franchise agreements without post-termination noncompetition agreements are the exception to the rule. Perhaps it is no wonder, then, that there is a fair amount of case law on the topic. (Refer to Part V, F. for a case law discussion.) While part of the system, franchisees may favor having these covenants as insurance against unfair competition by former franchisees continuing in the same business without payment of royalties or advertising dollars to the system. Yet the same franchisees probably want the option to continue doing business under a different name and mark should they exit the system. Conversion franchisees and multi-unit developers in particular may resist post-termination noncompetition clauses because of their desire to protect substantial pre-existing business investments and/or goodwill, and also simply because they can wield greater bargaining power.

Post-termination noncompetition agreements are difficult and expensive to enforce in the best of cases, and, in some states like California, they are enforceable only in limited instances. If location control is paramount, the agreement might instead focus on strengthening ways to secure the location after termination or nonrenewal, as described above. One method to provide for an orderly exit by franchisees wishing to terminate the agreement before expiration is to provide for payment by the franchisee of a termination fee calculated under a pre-determined formula. This type of provision is common in some franchise agreements, such as those used by hotel chains.

## 3. Personal Guaranty

Requiring owners of a franchise entity to guaranty the franchisee's payment and performance of all franchise agreement obligations is standard practice among franchisors. A well-drafted guaranty will also bind the owner to all of the franchisee's covenants, such as those dealing with confidentiality and noncompetition.

Resistance to a personal guaranty frequently arises when dealing with high net worth franchisees. Other forms of security for payment could be an option, for example, a pledge of stock, letter of credit or security interest in the assets of the franchised business. In any case, the absence of a personal obligation may diminish the sense of commitment to the system and accountability to the franchisor.

## 4. Negotiated Changes

Requests for negotiated changes to franchise agreements may come from the pioneer franchisees of a new system, renewing franchisees of an established system, or high net worth or conversion franchisees, among others. Sometimes there are legitimate reasons for treating franchisees differently; for example, a separate conversion addendum can be used with conversion franchisees, who understandably may be unwilling to sign a post-term noncompete, if they are already involved in the same industry or business as is the subject of the franchise. However, negotiated changes can dilute uniformity of the system and create administrative headaches. They may also create resentment among other franchisees who were not granted concessions, as well as legal issues in certain states.

The California Franchise Investment Law imposes unique disclosure obligations relative to negotiated changes, Cal. Corp. Code §31109.1. Five state franchise laws make discrimination in the terms offered to franchisees unlawful unless it can be justified under statutory tests, see: Haw. Rev. Stat. §482E-6(C); 815 Ill. Comp. Stat. §705/18; Ind. Code § 23-2-2.7-2(5); Minn. R. 2860.4400.B; Wash. Rev. Code §19.100.180(2)(c). On the other hand, in Virginia, if the franchisor does not afford the franchisee an opportunity to negotiate on all provisions other than those that might impair the uniform image and quality standards of the franchise, the franchisee may void the agreement within 30 days of its execution under Va. Code Ann. §13.1-565(b).

One way to manage negotiated changes is for the franchisor to identify circumstances in which modifications to the standard deal are warranted, such as offers to conversion or renewing franchisees, and create addenda for those cases. Franchisors can also mute charges of favoritism or unfair discrimination if there is a clear rationale for the modifications.

At the same time, franchisors should not have an expectation that “special deals” with franchisees will remain confidential. Good advice may be recommend to the franchisor that it to only agree to changes from the standard form when the business rationale can be justified to other franchisees who did not receive such benefits and who purchased at about the same time. The “political” consequences of not adopting such a policy may be unpleasant.

## 5. Renewal Options

To be fair and marketable, the initial term and any renewals of the franchise should provide a sufficient time for the franchisee to recoup its investment in the business and enjoy a reasonable return on that investment. Beyond that, there may be differences in what seems

appropriate from the perspective of each party. Cases involving renewal related issues appear at Part V, E., below.

Franchisees may seek options to renew well beyond the franchisor's ability to predict its business direction. Inexperienced franchisors can be short sighted in this regard, viewing generous renewal rights as a selling point that comes at little or no present cost to them. A prudent lawyer will caution the new franchisor that unlimited or unreasonable options to renew may constrain efforts to implement needed efficiencies in its distribution chain and dramatically limit its exit strategies. Similar cautions apply to ambiguous requests for renewals on "terms no less favorable" than those contained in the original franchise term, which can seriously impede a franchisor's ability to evolve its system through franchise generations.

## B. General Strategies to Enhance Marketability While Managing Risk

### 1. A Spoonful of Sugar

Providing incentives and tradeoffs to compensate for franchise agreement terms that prospective franchisees find objectionable may help the parties get to "yes". For example, if the agreement imposes aggressive sales goals, the franchisor could include a sliding scale royalty to reward franchisees with lower rates for attaining higher sales. Or, as noted above, if the agreement does not award an exclusive territory, it could provide for options or rights of first refusal in a defined market area, perhaps even with a provision for payment of less than then-current initial franchise fees, on the theory that an existing franchisee has a greater chance of success in meeting growth targets for the additional unit.

### 2. Avoid Excess; Retain Essentials

The ideal franchise agreement is not a two-page document or a 60-page tome. Legal certainty and brand protection should not be sacrificed on the altar of franchise sales, nor should sales be stifled by an overreaching, needlessly complex agreement. Striking a balance requires the drafter and franchisor to prioritize and adopt a realistic approach.

Drafters can use common sense and various drafting devices to limit wordiness and strengthen agreements. Some tips: Do not try to cover every remote contingency or express the same thing 10 different ways or in 20 different places. Use defined terms and cross-reference provisions to avoid repetition of concepts and promote consistency. Ask, "Is this clause really necessary? Is it redundant? Are these details more appropriate for an operations manual?"

Another tip is to delete or tone down provisions that raise enforcement issues. Franchise agreements sometimes include a host of franchisee-intimidating remedial rights that are rarely invoked and may be of doubtful utility in a given system. The employment of these rights also can spawn litigation. Refer to Part V of this document for illustrations.

Examples of such remedial provisions could include:

- Provisions granting the franchisor a security interest in the franchisee's assets where the only debts secured are future royalties and advertising fees, and where banks and purchase-money lenders have higher priority and will demand subordination.
- Provisions granting to the franchisor a power of attorney or authority to act on behalf of the franchisee, such as removal of signs after termination or signing of legal documents that are contrary to the franchisee's interests.
- Provisions for franchisee consent to entry of judgment.
- Jury trial waivers, waivers of rights to recover consequential or punitive damages, and waivers of rights to pursue claims as a class action.
- Options to purchase that permit the franchisor to cherry pick franchisee assets or buy at other than fair market value on termination or nonrenewal.
- Provisions whereby the franchisor can assume management of the franchised business on certain events, which may not provide for an accounting to the franchisee.
- Provisions for accelerating the entire future royalty stream upon termination or nonrenewal regardless of the underlying cause and without reduction for present value or possible replacement of the franchised location.

Anecdotal evidence suggests that numerous franchisors rarely rely on many of these provisions. Where enforcement efforts are attempted, they can rapaciously consume legal fees and produce negative results. For example, some California courts are refusing to uphold provisions for jury trial waivers and other limits on franchisee remedies based on lack of mutuality or unconscionability.

Deleting or toning down these sorts of potentially problematic provisions does not sacrifice much if enforceability is questionable or too expensive for the client to pursue. The goal is to draft for reasonableness, fairness and mutuality of obligations as to issues that do not compromise system standards and integrity. At the same time, it is vital not to compromise essential legal protections of the brand, such as the ability to dictate quality standards, control the brand's image and require additional training as needed.

#### IV. OBTAINING FRANCHISE SYSTEM BUY-IN

##### Building System Support

As mentioned in Part II, a key to a good franchise agreement is starting with a good form, using a recent, well-drafted franchise agreement appropriate for the industry and business. A good franchise agreement not only clearly identifies the rights and obligations of the franchisor and franchisee, it also becomes a defining element of the franchise relationship. An overreaching agreement that places every fathomable restriction on a franchisee may be reflected in a franchisor/franchisee relationship of distrust and tension. Even if franchisees sign a one-sided document, it is not uncommon that as the franchisees mature and know the business, resentment grows regarding the controls placed on the franchisee community.

Getting franchisee buy-in for the agreement and any changes sought to be implemented does wonders for the franchisor/franchisee relationship. Here are six tips to help accomplish that objective.

- Know the Audience. Who is the ideal franchisee prospect? How is the ongoing franchisor/franchisee relationship? As mentioned earlier, the franchise agreement should not be relied on as a sales tool. It can, however, send a message about the company's culture and philosophy. After all, it is one of the first comprehensive documents a prospect reviews about the business and franchise offering. Speak to the franchise development and field staff to determine which elements of an existing agreement are proving to be confusing and/or unintended impediments to System goals.
- Work with the System's Advisory Board. Work with a franchise advisory council ("FAC") during the drafting process. If no FAC is in place, designate key franchisees to assist in the review process. Ask for input and suggestions, not negation or approval. Keep the focus on the System rather than individual agendas and complaints.
- Research Competitors. Particularly with the boom in franchise brokers, it has become a common practice for franchisee prospects to "shop" franchise agreements. Use the resources referenced earlier in this paper to research other

franchise agreements and determine strengths to emulate and weaknesses to avoid in an evolving industry/marketplace.

- Don't Tinker. Minimize changes and make only those necessary based on changes to the business/system or those dictated by best practices (such as those resulting from franchise case law developments).
- Communicate with the System When Appropriate. If you make significant changes to the franchise agreement, consider communicating those changes to the entire franchise system, particularly if the franchisees have requested this communication. Making changes to the franchise agreement without making them known to the franchise community may foment a climate of distrust. Most franchisees will encounter a time in which they will be required to sign the "then-current form" of the franchise agreement (renewal, transfer, pursuant to an area development agreement, etc.). If a franchisor informs the franchisees of changes to the agreement at the time the change is made, it may ease the process of entering a term under the new franchise agreement.
- Use Plain English. Simpler, shorter and more user friendly provisions are benefits not only to attracting prospective franchisees, but also for the people in the field responsible for selling, understanding, explaining, and sometimes enforcing the agreement. Clarity in document language can allow the franchise development team to focus on explaining the business, not the legal obligations. Identify terms which are essential to the company and its operations (including its long-term strategic goals, which may include sale or merger) and those that can be sacrificed to achieve a shorter, friendlier document.

## V. FRANCHISOR-FRANCHISEE LITIGATION AND WAYS TO MINIMIZE FRANCHISOR EXPOSURE.

The Franchisor-Franchisee relationship is by its nature prone to litigation. There is, of course, no guarantee that even the most competent franchisee will be successful. Nevertheless, unsuccessful franchisees, correctly or incorrectly, may target their frustrations against their franchisor. Other franchisees may feel that they have an unconditional right either to renewal of the franchise on favorable terms or to compete with their franchisor, positions that will often be contested by franchisors. Below we address some of the most common areas of dispute between franchisors and franchisees, how to minimize franchisor exposure in the event of litigation, as well as issues related to dispute resolution.

### A. Lack of Franchisor Support

#### 1. The Issue

One of the benefits to any franchisee is the support it receives from its franchisor. This support may come in many forms, including site selection, initial and ongoing training, marketing of the brand, making arrangements for proprietary products, economies of scale in the purchase of goods and services, conducting research regarding ways to improve performance and/or the strength of the brand, and even a supposed “duty” on the part of the franchisor to grow the business and add additional franchisees. The duties of the franchisor in this regard are generally governed by the franchise agreement. When franchisees fail, they often claim that the franchisor did not do enough to support them, notwithstanding that successful franchisees in the same system generally received the same level of support. Often these claims of lack of assistance occur many years after the alleged lack of assistance took place, thereby creating issues as to adequacy of proof.

## 2. Case Law regarding Lack of Franchisor Support

Though these types of cases are very often not amenable to summary judgment, TCBY successfully moved for summary judgment in JRT, Inc. v. TCBY Systems, Inc., 52 F.3d 734 (8<sup>th</sup> Cir. 1995). In that case, the franchisee failed to present any evidence demonstrating, among other things, that (i) the franchisor was required to find and place the franchisee in a profitable site; (ii) the franchisor’s ad campaign was inadequate; (iii) the franchisee was entitled to an exclusive area; or (iv) there was a contract right to a reasonable opportunity to succeed.

Claims arising out of an alleged lack of support may also include claims of fraud. For example, in A.J. Temple Marble & Tile v. Union Carbide Marble Care, Inc., 618 N.Y.S.2d 155 (1994), the franchisee claimed that the franchisor’s “proprietary chemicals” were actually relabeled off-the-shelf compounds and that franchisor’s training staff was unqualified. The franchisee also argued that the franchisor misled the franchisee to believe that it would have the right to use the Union Carbide mark and that the franchisor concealed a pre-existing plan to dispose of the franchise system if the system failed to meet certain financial goals. The franchisor moved to dismiss arguing that the claims were barred because the documents contained a merger clause, the franchisee signed a release of claims and the franchisee’s assertions were inconsistent with the written literature. The court denied the motion.

In Century 21 Real Estate Corp. v. CLTM Associates, LTD., 2003 U.S. Dist. LEXIS 1863 (N.D. Ill. 2003), a Century 21 franchisee claimed inadequate support as a defense to a suit for unpaid royalties. The franchisee claimed that Century 21 failed to list the franchisee in the franchisor’s directory or on its website and failed to provide a proper support staff. In addition, the franchisee complained that Century 21

wrongfully supported the Coldwell-Banker system (a competitor brand) after Century 21's parent company acquired Coldwell-Banker. The franchisee's complaints were enough to defeat Century 21's summary judgment motion, which was based on a claim for lost royalties and other amounts due. The court found there were questions of fact as to whether the franchisee owed the monies in light of the franchisor's alleged failure to provide support.

### 3. Suggested Ways to Minimize Franchisor Exposure re Support Issues

A franchisor may seek to limit claims of lack of support by requiring in the franchise agreement (i) that the franchisee must notify the franchisor in writing within a set amount of time after a failure to provide adequate support; and (ii) that a failure to so notify the franchisor within the prescribed time operates as an acknowledgement by the franchisee that all support has been provided.

Also, the franchisor may want to shift any contractual responsibility regarding support to the franchisee. The franchisor may require, for example, that the franchisee must complete certain training within a certain period of time. That way, it is the franchisee's responsibility to seek out support from the franchisor.

Alternatively, a franchisor may wish to set forth in the franchise agreement that the franchisor may provide support, but it is not obligated to do so. The franchise agreement may further limit the franchisor's support obligations by stating that if the franchisor has provided support, the franchisor may provide continuing support in the sole discretion of the franchisor.

Finally, the franchisor may also elect to require the franchisee to execute a separate acknowledgement or statement in which he/she indicates, in his own handwriting, that no representations regarding support have been made other than as contained in the UFOC, the franchise agreement and other listed documents.

## B. Earnings Claims

### 1. The Issue

When a franchisee experiences a lack of financial success, it might bring an action claiming that the franchisor misrepresented the franchisee's earnings potential. The claim might be based on statements contained in the franchisor's UFOC, marketing materials, correspondence, or other written materials. A franchisee might also base such a claim on oral

misrepresentations, perhaps supported by other franchisees' testimony that they received similar oral misrepresentations.

## 2. Case Law regarding Earnings Claims

The franchisor successfully moved for summary judgment against a franchisee who alleged misstatements as to earnings in Healy v. Carlson Travel Network Assoc., Inc., 227 F. Supp 2d 1080 (D. Minn. 2002). The franchisee claimed that the franchisor's agent misled him into believing that he "could expect to do \$1.2 million in business his first year, \$2 million his second year and \$3 million his third year." The Court granted summary judgment in favor of the franchisor because such representations of expected earnings are not actionable under Illinois franchise law on the theory that they are not representations of present material fact. Furthermore, in the franchise closing checklist, the franchisee specifically disclaimed that he had been given or relied on "any oral or written promises, representations or assurances of any specific actual, projected or pro forma sales, profits, earnings or break even point" for his or any other franchise.

However, in Carousel's Creamery, LLC v. Marble Slab Creamery, Inc., 134 S.W.3d 385 (Tex. App. 2004), the franchisee alleged that its franchisor was liable for negligent misrepresentation of earnings and was able to overturn a directed verdict. The franchisee had submitted evidence demonstrating that the UFOC misrepresented the value of the franchise because the figures were based on a company-owned store, which was more profitable than other restaurant franchises because it did not have any labor costs and because it catered corporate events, which generated more profits than in-store sales.

Earnings claims may also be based upon a failure to comply with statutory requirements, as opposed to misstatements or misrepresentations. The court in Kinship Inspection Service, Inc. v. Newcomer, 605 N.W.2d 579 (Wis. App. 1999), reversed the dismissal of the franchisees' Wisconsin franchise law claims. The court held there was sufficient evidence to establish a violation because the franchisor had failed to include in the UFOC projected earnings and historical financial data for the franchise. Instead, the franchisor had provided financial data in documents separate from the UFOC. In Wisconsin, as in the Item 19 instructions generally, franchisors are required to register and insert in their UFOC any statement of projected franchisee earnings and a statement describing the data upon which the projections were based.

Deceptive practices as to earnings claims led the FTC to seek and obtain a permanent injunction to halt deceptive practices in the sale of Minuteman print shop franchises and Speedy sign-making franchises in

FTC v. Minuteman Press Inter., Inc., 53 F. Supp. 2d 248 (E.D.N.Y. 1998). Specifically, the FTC demonstrated that the franchisors falsely represented to prospective franchisees that they would achieve specific gross sales levels and that one third of their gross sales would be profit. The franchisors also made earnings claims concerning gross sales and profit levels without having contemporaneous substantiating documentation and without providing earnings claims documents. Finally, the franchisors made earnings claims to prospective franchisees in contradiction to the express statement in franchisors' general disclosure documents that they did not make earnings representations.

### 3. Suggested Ways to Minimize Franchisor Exposure re Earnings Claims

One common way for a franchisor to seek to protect against a claim that there has been a misrepresentation as to earnings is to make no earnings representations in the UFOC. However, this leaves open the possibility that the franchisee still may assert that the franchisor made oral misrepresentations regarding earnings. Moreover, at least one state regulator has expressed the opinion that a statement in a UFOC that the franchisor is making no claims as to earnings is to be given no weight in the context of a state enforcement action. A more effective approach may be for franchisors to simply set forth a range of earnings of its franchisees. Whichever approach the franchisor chooses, it should consider establishing procedures to instruct, train and educate sales personnel and brokers against making improper earnings claims. The franchise agreement should also emphasize the fact that, realistically, no franchisor can accurately predict the results to be obtained by any franchisee, or a company-owned store for that matter, and that every franchise system will, inevitably, have successes and failures.

The franchisor may consider creating an acknowledgment or statement for a prospective franchisee to complete immediately prior to, or concurrent with, the signing of the franchise agreement. The acknowledgment should cover earnings claims, as well as support claims. Following is such an example:

- No oral, written, visual or other promises, agreements, representations, options, rights-of-first-refusal, statements or otherwise (collectively, the "representations"), expanding upon or inconsistent with the Offering Circular, the Franchise Agreement, or any related franchise documents, have been made to or with me/us with respect to any matter, including, but not limited to, marketing, site location and/or development, operations, support services, training, financial results, exclusive rights or protected territory, or otherwise.

I/we have not relied in any way on any such representations, except as follows:

\_\_\_\_\_  
(If none, the Prospective Franchisee should write NONE in his/her/their own handwriting.)

Prospective Franchisee's Initials: \_\_\_\_\_

- No oral, written, visual or other claim, guarantee, statement or representation that stated or suggested any specific level or range of actual or potential sales, costs, income, expenses, profits, cash flow, or other financial data about franchised or non-franchised units, or from which such information might be ascertained, (collectively, "financial results"), was made to me/us by the Franchisor, its affiliates or any agents/representatives/salespersons, or any other person. Except as may have been contained in Item 19 of Franchisor's Offering Circular and its related exhibits, I/we have not seen or relied on charts, tables, spreadsheets or mathematical calculations to demonstrate actual or possible results based on a combination of variables, such as multiples of price and quantity to reflect gross sales, or otherwise. I/we have not relied in any way on any such financial results except for information (if any) in Item 19 of the Franchisor's Offering Circular and as detailed in the space provided below.

I/we have not relied in any way on any such representations, except as follows:

\_\_\_\_\_  
(If none, the Prospective Franchisee should write NONE in his/her/their own handwriting.)

Prospective Franchisee's Initials: \_\_\_\_\_<sup>1</sup>

Such an acknowledgment may also be helpful in the case where a franchisee raises procedural unconscionability in an attempt to avoid enforcement of terms contained in a franchise agreement, whether the

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<sup>1</sup> The author wishes to recognize *Holmes & Lofstrom, LLP* for its contribution of certain suggested contract provisions.

terms involve earnings, support, arbitration, jury trial waivers or punitive damages.

## C. Trademark Issues

### 1. The Issue

Perhaps the most valuable asset of any franchise is its brand. It is common for franchisors to assert trademark infringement claims against terminated franchisees. This type of litigation is well documented and beyond the scope of this paper. Even when there is no termination, however, the brand/trademark must be protected from infringers in order to maintain its value. Sometimes, disputes arise between franchisors and franchisees as to responsibility for protecting the marks or as to liability for infringing upon a competitor's marks. Disputes may also arise in the context of re-branding or substituting different proprietary marks for the marks originally licensed to the franchisee under the franchise agreement.

### 2. Case Law regarding Trademark Issues

What of the case where a franchisee is infringing a third party's mark and the third party sues the franchisor for infringement? The Eleventh Circuit in Mini Maid Serv. Co. v. Maid Brigade Sys., Inc., 967 F.2d 1516 (11<sup>th</sup> Cir. 1992) found that a franchisor does not have a duty to supervise a franchisee's improper use of trademarks and will not be held liable for infringement by a franchisee. The case involved a claim brought by a competitor of the franchisor in the home cleaning service industry. A franchisee of the defendant acquired the assets of a former franchisee of the plaintiff, including a telephone book listing bearing the plaintiff's trademark. The plaintiff requested that the defendant franchisor Brigade stop its franchisee from using the telephone number. The franchisee, however, ignored its franchisor's requests to stop using the number. The District Court entered a directed verdict on a vicarious liability theory because the defendant failed to exercise "reasonable diligence" to prevent its franchisee from violating the trademark laws. The Eleventh Circuit reversed, finding that although there was a duty for a licensor to supervise a licensee's use of the licensor's own trademark, there is no duty for a licensor to supervise a licensee's appropriation of other marks. In order to prevail, the plaintiff had to have shown that the defendant franchisor somehow knowingly participated in the infringement.

### 3. Suggested Ways to Address Trademark Issues

Franchisors may include in their franchise agreements information identifying the trademarks they are licensing to franchisees. The agreement should make it clear that the franchisee may use the trademark

only in the ways authorized by the franchisor. With respect to protection of the mark, the franchise agreement should state that the franchisee must promptly notify the franchisor of any known or suspected trademark infringement or challenges to the franchised mark. The franchisor should also state that it has the right, but not the obligation, to take action against possible infringers and to otherwise protect the mark. The franchise agreement may contain an indemnity agreement wherein the franchisee agrees to defend and indemnify franchisor against any claims, which allege that the franchisee has infringed upon marks not licensed under the franchise agreement.

Other language may include:

- Franchisee agrees to ensure that all advertising and promotional materials, signs, decorations, stationery, business forms, and other items bear the Marks in the form, color, location, and manner prescribed by Franchisor. Franchisee will use best efforts to uphold the reputation and goodwill of Franchisor and its affiliates.
- Franchisee agrees to promptly notify Franchisor of any suspected unauthorized use of the Marks, any challenge to the validity of the Marks, or any challenge to Franchisor's ownership of, Franchisor's right to use and to license others to use, or Franchisee's right to use, the Marks. Franchisee acknowledges that Franchisee has the sole right to direct and control any administrative proceeding or litigation involving the Marks, including any settlement thereof. Franchisor has the right, but not the obligation, to take action against uses by others that may constitute infringement of the Marks. Franchisor agrees to defend Franchisee against any third-party claim, suit or demand arising out of Franchisee's use of the Marks. Franchisee agrees to execute any and all documents and do such acts as may, in the opinion of Franchisor, be necessary or advisable to protect and maintain the interests of Franchisor and Franchisee in the Marks. Except to the extent that such litigation is the result of Franchisee's use in a manner inconsistent with the terms of this Agreement or of Franchisee's infringement of the marks of others not licensed under this Agreement, Franchisor agrees to reimburse Franchisee for his or her out-of-pocket cost in doing such acts.
- Franchisee agrees to defend Franchisor against any third-party claim, suit or demand arising out of Franchisee's unauthorized use of the marks of others not licensed under this Agreement. Franchisee agrees to reimburse Franchisor for its out-of-pocket cost in doing such acts.

- During the term of this Agreement and after its expiration or termination, Franchisee agrees not to directly or indirectly contest the validity of, or Franchisor's ownership of, or right to use and license others to use, the Marks.
- Franchisee's use of the Marks does not give Franchisee any ownership interest or other interest in or to the Marks.
- Any and all goodwill arising from Franchisee's use of the Marks shall inure solely and exclusively to the benefit of Franchisor, and upon expiration or termination of this Agreement, no monetary amount shall be assigned as attributable to any goodwill associated with Franchisee's use of Franchisor's System or the Marks.
- The license of the Marks granted hereunder to Franchisee is nonexclusive, and Franchisor thus has and retains the rights, among others: (a) to use the Marks itself in connection with selling products and services (including products and services that Franchisee will offer and sell); (b) to grant other licenses for the Marks, including to licensees outside of the System; and (c) to develop and establish other systems using the Marks, similar marks, or any other marks, and to grant licenses thereto without providing any rights therein to Franchisee.
- Franchisor reserves the right to substitute different marks for use in identifying the System and the businesses operating thereunder.

#### D. System-Wide Change

##### 1. The Issue

In order to adapt to changes in the business environment, whether from internal or external forces, the franchise system must be able to effectuate system-wide change. External forces include governmental and regulatory changes, changes in demands of customers and increased competition against the franchise system. Internal forces include a change in ownership of the franchisor, major litigation and significant decreases in the franchisee community's performance and satisfaction levels. One type of system-wide change, which is currently gaining attention, is re-branding. Re-branding is often deemed necessary when there is a merger or acquisition, or when there has been a strategic change in the franchise system's approach to the consumer market. When declining performance follows re-branding, franchisees may blame the franchisor for imprudent re-branding and argue that the re-branding was not permitted. At other times, re-branding is not a business judgment, but rather is forced upon the franchisor. For example, if the franchisor

itself loses trademark rights (or for whatever reason never had them), it has little choice but to re-brand, if it cannot secure the rights.

## 2. Case Law regarding System-Wide Change

Several states have passed statutes that prohibit a franchisor from “substantially changing the competitive circumstances of a dealership agreement without good cause.” See, e.g., Wis. Stat. § 135.03 (2006). These states include: Wisconsin, Minnesota, Arizona, Oregon, Indiana and Montana. However, even if the franchisor is subject to scrutiny under the “substantial change in competitive circumstances” analysis, a franchisor may avail itself of various arguments to defend a system-wide change. Courts have read economic necessity and the right of a manufacturer to implement non-discriminatory system-wide changes into their analysis. See, *infra*, East Bay Running Store, Inc. v. NIKE, Inc., 890 F.2d 996 (7<sup>th</sup> Cir. 1990) (held NIKE’s new policy prohibiting sale of certain shoes by internet, mail or phone was not a substantial change in competitive circumstances where the policy applied to all retailers nationwide and was not an underhanded attempt to drive dealers out of business); Re/Max North Central, Inc. v. Cook, 160 F. Supp. 2d 1004 (E.D. Wis. 2001) (when a franchisor makes a system-wide non-discriminatory change, the franchisor does not violate Wisconsin law even if the change significantly harms a particular franchisee’s profitability).

System-wide changes, including re-branding, often turn on the issue of whether or not the action is undertaken in good faith. In Unified Dealer Group v. Tosco Corporation, 16 F.Supp.2d 1137 (N.D. Cal. 1998), the Court considered whether the PMPA permitted franchisor Tosco, which was the franchisor for “Union 76” gas stations, to re-brand “BP” gas stations as “Union 76” stations when Tosco obtained the BP assets. The court held that the decision to re-brand was in good faith in the normal course of business. See *also* Johnson v. Arby’s, Inc., CCH ¶ 12,018 (E.D. Tenn. 2000) (franchisor could require the franchisee to construct a free-standing building as part of a system-wide change undertaken in good faith).

Re-branding not undertaken in good faith is actionable, however. In Cromeens, Holloman, Sibert, Inc. v. AB Volvo, 349 F.3d 376 (7<sup>th</sup> Cir. 2003), Volvo terminated the Samsung franchisees because Volvo claimed that it had discontinued Samsung branded excavators. The Circuit Court found that a question of fact existed as to whether Volvo discontinued the Samsung brand in good faith or whether Volvo terminated the franchisees because Volvo, in actuality, simply re-branded the Samsung excavators with the Volvo brand.

Although franchisees will often assert breach of the implied covenant of good faith and fair dealing, such a claim may not be used to rewrite or override the express terms of a contract. Stone Motors Co. v. General Motors Corp., 293 F.3d 456 (8<sup>th</sup> Cir. 2002); see also Clark v. America's Favorite Chicken Co., Bus. Franchise Guide (CCH) ¶ 11,147 (5th Cir. 1997) (a franchisor who owned two competing fast-food chicken restaurants was able to implement a system-wide change because the franchise agreement *specifically stated* that the franchisor reserved the right to open competing franchises under different marks). Many courts, however, treat the implied covenant as a supplement to the written contract that protects the reasonable expectations of the parties when one party has broad discretion in interpreting a contract term. Ford Motor Co. v. Meredith Motor Co., Bus. Franchise Guide (CCH) ¶ 11,941 (D.N.H. 2000); Emmet Bonfield v. AAMCO, 708 F.Supp. 867 (N.D.Ill. 1989) (arbitrary changes in complete disregard of a franchisee's success are actionable).

### 3. Suggested Ways to Minimize Franchisor Exposure re System-Wide Change

The franchise agreement should unequivocally state that the franchisor reserves the right to make system-wide changes and should enumerate as many system-wide changes as possible, including the right to change the mark under which the franchise systems operates. By setting forth various kinds of system-wide changes, the franchisor should increase its chances of defeating a good faith and fair dealing claim, since the implied covenant cannot alter an express term. Furthermore, the chances that a system-wide change will be viewed as an action taken in good faith will be increased if the franchisor makes its system-wide changes on a non-discriminatory basis. The agreement should also provide that the franchisee must comply with whatever system-wide changes are implemented, including using only marks designated by the franchisor, and no others. For example:

- We reserve the absolute right to make system-wide changes. We shall use our judgment in exercising such discretion based on our assessment of the interests we consider appropriate and will not be required to consider your individual interests or the interests of any other particular franchisee(s). You, we and all other franchisees have a collective interest in working within a franchise system with the flexibility to adjust to business conditions, including but not limited to the competitive environment, new regulatory developments and emerging business opportunities. Therefore, you and we agree that the ultimate decision-making responsibility for the System must be vested in us. So long as we act in compliance with the requirements of this Agreement, we will have no liability for the exercise of our

discretion in making any system-wide change in accordance with the provisions of this Agreement.

- Franchisor reserves the right to substitute different marks for use in identifying the System and the businesses operating thereunder.

## E. Renewal Issues

### 1. The Issue

Franchisor-franchisee disputes are not limited to the context of a failed franchise operation. The franchise relationship, defined by the franchise agreement, is for a set term. Typically, the franchise agreement will address the possibility of a renewal of the franchise. In addition, state or federal statutes may permit non-renewal only under limited circumstances. Successful franchisees will typically wish to continue the relationship beyond the term of the agreement. For many reasons, franchisors may wish to end the relationship at the conclusion of the term, or they may wish to continue the relationship on different terms than those in the original franchise agreement. In addition, franchisors often also require a general release as a condition of any renewal, something that might complicate the renewal process. Litigation may result whenever a franchisee wishes to renew but the franchisor is either disinclined to renew at all or wishes to renew on terms more favorable to the franchisor than those in the original franchise agreement, or conditioned upon a release.

### 2. Case Law regarding Renewal Issues

In Vaughn v. General Foods Corp., 797 F.2d 1403 (7<sup>th</sup> Cir. 1986), the franchisees argued that the releases they signed in connection with renewal were unenforceable. They claimed that there was a lack of consideration, they were the product of economic duress and they were induced by fraud. In rejecting the arguments, the Seventh Circuit stated: "It is clear that there was adequate consideration since each of the releases was given in exchange for making, renewing, extending or modifying the terms of the franchise agreements. Moreover, the agreements were mutual." For this court, mutuality was an important consideration.

Franchisors often condition renewal on the franchisee executing the "then current" franchise agreement at the time of renewal. In Bradley v. Harris Research, Inc., 275 F.3d 884 (9<sup>th</sup> Cir. 2001), *infra*, the Ninth Circuit approved a renewal provision that required the franchisee to execute a "then current" franchise agreement which contained an arbitration provision requiring arbitration in Utah. The franchisee executed the "then current" franchise agreement under protest, asserting it was a contract of

adhesion and lacked mutuality. Although not the main issue in the case, the Ninth Circuit affirmed the requirement that the then-current franchise agreement be signed as a condition to renewal (and, as discussed below, required arbitration in Utah).

In Tatan Management v. Jacfran Corp., 270 F. Supp. 2d 197 (D.P.R. 2003), the court found that the franchisor had good cause not to renew the franchise agreement because the franchisees never submitted their renewal fee, they refused to perform agreed-upon renovations and they were in default of their obligations. The court, however, questioned the validity of conditioning renewal on requiring the franchisee to execute (1) the “then current standard form of franchise agreement” and (2) a unilateral release. The court observed: “The Court has doubts as to the lawfulness of requiring the execution of the then-current standard form of the franchise agreement and the execution of a release. The first condition potentially runs contrary to [the Puerto Rico dealer law] by allowing the principal to unilaterally alter the terms of the agreement, while the execution of the release seems to clash with [the Puerto Rico dealer law] provision that the rights provided under the statute cannot be waived.”

In Re/Max North Central, Inc. v. Cook, 160 F. Supp. 2d 1004 (E.D. Wis. 2001), the franchisor sought to require its franchisee to agree to a system-wide change as a condition to renewal. More specifically, the franchisee previously had an exclusive real estate franchise and the franchisor wanted to limit it to residential real estate in the renewal, permitting the franchisor to sell commercial real estate in the territory. The court held that such a system-wide change, which was a condition of renewal, was permissible under Wisconsin franchise law.

The Petroleum Marketing Practices Act and some state franchise acts explicitly forbid conditioning renewal of the franchise agreement on a release of claims under the act at issue or any state law. See, e.g. 15 U.S.C. § 2805(f)(1) (forbids conditioning renewal on a release of any claim, federal or state); Mich. Comp. Laws § 445.1527(b) (forbids a release of claims arising under the Michigan franchise law). In Franchise Management Unlimited Inc. v. America’s Favorite Chicken, 561 N.W.2d 123 (Mich. App. 1997), the franchisor conditioned the transfer of the franchise upon a release of claims. The Court found that it was acceptable to condition the transfer of the plaintiff’s franchise to a new owner upon a release of claims because the release at issue specifically preserved any claim arising under the Michigan franchise law.

### 3. Suggested Ways to Minimize Franchisor Exposure re Renewal Issues.

Often renewal provisions state that renewal will be offered to franchisees on the same terms as the then-current franchise agreement. The renewal clause may contain, among other stipulations, the following:

- Renewal is conditioned upon you executing our then-current form of franchise agreement and related documents, as are then customarily used by us to award Franchises (with modifications to reflect the fact that the successor franchise agreement may have limited successor franchise rights as contemplated by this Agreement); provided that, 1) we will not be required to provide you any training or other “start-up” services, 2) you will not be required to purchase start up equipment and inventory, and 3) you will not have to pay another initial franchise fee but will need to pay a successor franchise fee.

As always, one must be cognizant of the various jurisdictions at play. As described above, some have limitations about conditioning renewal upon a release and some courts have expressed concern where the franchisor requires a unilateral release.

## F. Non-Compete Issues

### 1. The Issue

Sometimes, a franchisee may attempt to avoid its obligations to its franchisor by establishing its own competing business. In many cases, this occurs after the franchisor has expended its resources in training the franchisee. Accordingly, many franchise agreements contain an in-term noncompete provision and many also contain a post-term noncompete obligation. Depending on the jurisdiction, post-term noncompete provisions may be of limited enforceability, however. In any case, the franchisor can and should restrict the franchisee from soliciting customers away from the franchise.

### 2. Case Law regarding Noncompete Issues

#### a. Post-Term Covenants Not to Compete

In contrast to cases addressing in-term covenants not to compete (which are generally enforced), the case law on post-term covenants is substantial. Whether or not they are permissible varies from state to state. A number of states (such as, perhaps most notably, California) have statutes that specifically limit these covenants. See Cal. Bus. & Prof. Code §§ 16600 et seq. (invalidating all covenants not to compete, except where exempted by statute); Burns Ind. Code Ann. §§ 23-2-2.7-1 et seq. (restricting

geographic and time limitations of covenants not to compete); Tex. Bus. & Com. Code § 15.50 (providing criteria for enforceability of covenants not to compete).

Where lawful, post-term covenants not to compete are generally enforceable only if they are “reasonable.” What is reasonable, however, varies from state to state, as does a court’s willingness to unilaterally revise agreements to make them reasonable and thereby enforceable. Generally, reasonableness will depend on three principal factors:

(i) Duration: A reasonable duration should be, at most, the time (a) it would take the franchisor to establish a new franchisee in the territory in question, and (b) the value of proprietary information to dissipate.

(ii) Geographical limitations: Unlike in-term noncompete covenants, post-term covenants cannot be geographically unlimited. However, properly drafted geographic limitations can restrict post-term competition in the vicinity of distant members of the franchise system. Armstrong v. Taco Time Int’l, Inc., 635 P.2d 1114 (Wash. App. 1981) (in-term and post-term noncompete modified by Court to prohibit competition in franchise territory and within the franchise territory of any other franchisee); Casey’s General Stores, Inc. v. Campbell Oil Co., 441 N.W.2d 758 (Iowa 1989) (following Armstrong, Iowa Supreme Court made similar modifications to noncompete).

(iii) Type of business activity: The narrower the type of business activities that are restricted, the more likely it is that the restriction will be considered reasonable. The restriction should be only so broad as is necessary to protect a franchisor’s legitimate business interests. “Legitimate business interests include protection of trade secrets, confidential information, and good will.” Boulangier v. Dunkin’ Donuts, Inc., 815 N.E.2d 572 (Mass. 2003) (the Court observed that a noncompete in a *franchise agreement* was more akin to a sale of a business noncompete, than to an employment noncompete). See also Hobbs v. Pool, 1987 Ark. App. LEXIS 2111 (1987) (prohibition on “catfish preparation” too broad because it was not limited to restaurant operations); Giampapa v. Carvel Corp., Bus. Franchise Guide (CCH) ¶ 11,442 (D.N.J. 1998) (covenant regarding ice cream store upheld).

b. In-Term Covenants Not to Compete.

There are relatively few decisions dealing with in-term covenants not to compete. Most courts that have addressed in-term covenants not to compete have refused to apply a reasonableness standard and have generally enforced them as written. See, e.g., McDonald's Sys., Inc. v. Sandy's, Inc., 195 N.E.2d 22 (Ill. App. 1963) (providing that in-term covenants will be upheld, irrespective of their geographic scope); Deutschland Enter., LTD v. Burger King Corp., 957 F.2d 449 (7<sup>th</sup> Cir. 1992) (franchisor successfully terminated a Wisconsin franchisee for operating a competing Hardee's in Michigan).

In-term covenants can also prevent competition in other, related businesses in certain circumstances. For example, Dairy Queen successfully terminated a franchisee, which leased a portion of its location to a drive-through coffee business. In the Matter of Arbitration between Shikka West Coast Co. and American Dairy Queen Corporation, Bus. Franchise Guide (CCH) ¶ 12,776 (AAA Mar. 23, 2004).

However, it is not without precedent for an in-term covenant not to compete to be disregarded or modified by a court. Armstrong v. Taco Time Int'l, Inc., supra, 635 P.2d 1114 (Wash. App. 1981) (in-term covenant not to compete was modified according to the same reasonableness limitations the court applied to the post-term covenant). Florida also appears to apply the same reasonableness standard to in-term covenants that it applies to post-term covenants. Fla. Stat. § 542.335(1).

c. Limits on Solicitation of Customers.

A franchisor may also limit competition by a franchisee by placing limits on solicitation of the franchisor's customers.

In American Express Financial Advisors, Inc. v. Yantis, 358 F. Supp. 2d 818 (N.D. Iowa 2005), the franchisor, who operated a financial services franchise, sued a franchisee who terminated his relationship and began to work for a competitor soliciting customers and employees of his former franchisor. The franchisor obtained a preliminary injunction under the franchise agreement and Iowa law. The court held that the franchise agreement's restrictive covenants were permissible in the franchisor/franchisee context because they were reasonably necessary for the protection of the business. "Covenants not to compete," the court said, "are unreasonably restrictive unless they are tightly limited as to both time and area." The one-year, countywide restriction was held to be reasonable and enforceable.

Similarly, in H & R Block Tax Serv., Inc. v. Circle A Ent., Inc., 693 N.W.2d 548 (Neb. 2005) and H & R Block Eastern Tax Serv., Inc. v. Vorpahl, 255 F. Supp. 2d 930 (E.D. Wis. 2003), the courts found a covenant enforceable and prevented former franchisees of H & R Block from soliciting or servicing clients of their former franchisor. The Nebraska Supreme Court observed that the covenant was enforceable even as against clients for whom the franchisees performed no services because the franchise agreement was akin to the sale of a business. The covenant was not injurious to the public interest, and it was reasonable “in both space (45 miles) and time (1 year) so that [it was] no greater than necessary to achieve its legitimate purpose.”

### 3. Suggested Ways to Address Non-Compete Issues

#### a. Post-Term Covenants Not to Compete

Keeping in mind that under certain circumstances, courts may find them unenforceable, any post-term covenant not to compete should specify (i) prohibited activities; (ii) time limitations; and (iii) geographical limitations. The provision should be written to facilitate a re-writing of the provision in the event a court finds any part of the provision unreasonable. Some courts will “blue pencil out” an unreasonable term, leaving the rest alone. Others will “blue pencil” a modification. Others still will not “blue pencil” at all; they will either enforce the entire provision or strike it. A clear contractual provision inviting a court to revise any otherwise unenforceable provisions, at least in this area, may be helpful in some cases. In a similar vein, a franchise agreement may restrict post-term competition by restricting the solicitation of customers, requiring the franchisee’s return of customer lists, and requiring the assignment of leases to franchisors.

It may be helpful to set out in the franchise agreement (i) that the franchisee understands that a noncompete provision is necessary to protect the franchisor from unfair competition arising from the use of the franchisor’s training, proprietary information, etc. in competition with the franchisor; and (ii) that the franchise and the entire system benefit from preventing one franchisee from opening a competing business, which might affect existing franchisees. The agreement may also provide that the franchisee recognizes that the franchisor would not enter into a franchise agreement under which the franchisor discloses proprietary information to the franchisee, without the promise that the franchisee will not use the information to compete with the franchisor. Such provisions are legitimately

designed to protect the trade secrets of the franchisor and may have greater enforceability in California.

b. In-Term Covenants Not to Compete

For in-term covenants, even though the “reasonableness” limitations set forth above with respect to post-term covenants are not strictly required in many jurisdictions, the franchise agreement should nevertheless incorporate reasonable limitations for in-term covenants.

As noted above, some in-term noncompete issues arise in the context of the franchisee conducting a separate business at the premises. To prevent use of the premises or equipment by the franchisee for any other business, the franchisor may wish to address this issue in the franchise agreement. The agreement then should provide that the franchisee shall not use the premises to conduct any business other than the franchised business or use any of the assets of the franchised business in connection with any other business.

c. Solicitation of Customers

The franchise agreement may provide that a franchisee agrees to not:

- Encourage, assist, participate, induce, or attempt to induce any customer or prospective business or customer to terminate an agreement with franchisor, franchisor’s affiliates, or any franchised business under the system.
- Solicit any customers that franchisee contacted, serviced or learned about while operating under this Agreement to open an account other than an account with franchisor or to sell any products or services other than through franchisor with franchisor’s written approval and consent.

G. Dispute Resolution Provisions

1. The Issues

Franchise agreements commonly require alternative dispute resolution, or “ADR”. ADR provisions create a number of legal issues. First, it is crucial that the franchise agreement make clear which ADR procedures are to be followed. Once that hurdle is cleared, the parties may be expected have conflicts over such items as the precise manner of ADR (e.g., arbitrator

selection), the venue of the ADR proceeding (i.e., can a franchisor require a franchisee to travel to another jurisdiction for the proceeding?), the choice of law to govern the ADR proceeding, evidence which can and cannot be considered in any ADR proceeding, the effect of integration clauses, and the reviewability of any award rendered in an ADR proceeding. Other issues involve the measurement of damages, the availability of class-wide relief, the effectiveness of pre-dispute waivers (e.g., of jury trials, types of relief, and punitive damages), and provisions respecting limitations periods for claims.

Perhaps the most important suggestion to be made to transactional lawyers contemplating the drafting of dispute resolution provisions is to solicit the input of franchising-experienced litigators who ultimately may have to try such cases. Not only are their insights and real-life experiences particularly valuable, lessons about how to avoid adverse consequences are often learned only after having litigated inadequate contractual provisions.

## 2. Case Law regarding Dispute Resolution Issues

### a. Availability of Arbitration

Section 2 of the Federal Arbitration Act (“FAA”) provides that both pre-dispute and post-dispute arbitration agreements within its broad scope “shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.” See 9 U.S.C. § 2. Section 2 applies in state court and preempts conflicting state laws, including state franchise laws.

In Southland Corp. v. Keating, 465 U.S. 1 (1984), the franchisees sued 7-Eleven for violation of the California franchise laws, among other things. 7-Eleven moved to compel arbitration under the franchise agreement. The California Supreme Court held that the arbitration agreement was unenforceable because it was an invalid “condition, stipulation or provision purporting . . . to waive compliance with any provision of [the California franchise law].” The United States Supreme Court reversed the California Supreme Court, holding that the FAA applied in state court and preempted the California ant-waiver provision as applied to arbitration clauses.

To avoid FAA preemption, courts will rely on the “save upon such grounds as exist in law or in equity for the revocation of any contract” language of Section 2. For example, in Aral v. Earthlink, Inc., 134 Cal. App. 4<sup>th</sup> 544 (2005), a California court recently held that a requirement that a California consumer arbitrate in Georgia was unconscionable, stating “a forum selection clause that

discourages legitimate claims by imposing unreasonable geographical barriers is unenforceable under well-settled California law.” The court decided that whether the forum selection clause was unconscionable was a “gateway” issue for the court, not the arbitrator, thereby avoiding FAA preemption. The Court in Aral, relied upon (1) Green Tree Financial Corp. v. Bazzle, 539 U.S. 444 (2003), for the proposition that courts are to determine certain “gateway” matters, such as the validity and scope of the arbitration agreement and (2) Discover Bank v. Superior Court, 39 Cal. 4<sup>th</sup> 148 (2005), for the proposition that under California law, the question of whether grounds exist for the revocation of the arbitration agreement based on grounds that exist for the revocation of any contract (including unconscionability and contrariness to public policy) is such a “gateway” matter for the courts to decide. It is notable that Aral was a consumer case, arguably different than arbitration in a commercial context, such as franchising.

In the U.S. Supreme Court’s most recent decision on arbitration and FAA preemption, the Court held that an arbitration provision was enforceable even if the contract as a whole was illegal under state law as usurious. Buckeye Check Cashing, Inc. v. Cardegna, 2006 U.S. LEXIS 1814 (Feb. 21, 2006). Justice Scalia writing for the Court reasoned that regardless of whether the action is brought in federal or state court, a challenge to the validity of a contract as a whole, and not specifically to the arbitration clause within it, must go to the arbitrator, not the court.

Arbitration was successfully compelled in Jensen v. Quik Int’l, 820 N.E.2d 462 (Ill. 2004) even though the franchisor allowed its registration with Illinois state authorities to lapse just before signing the franchise agreement containing the arbitration provision. When the franchisee sought to rescind the franchise agreement, the franchisor moved to compel arbitration, and the franchisee argued that the arbitration provision of the franchise agreement was not enforceable because the franchisor was not registered as a franchise in Illinois when the franchise agreement was executed. The Court held that the provision was enforceable and that the legislature had not intended registration to be a condition precedent to an enforceable franchise agreement.

#### b. Forum Selection

When determining the enforceability of a forum selection clause in a franchise agreement, there is an important distinction between judicial forum selection clauses and arbitral forum selection clauses: Judicial forum selection clauses are generally

enforceable, unless state franchise law is to the contrary. The Bremen v. Zapata Off-Shore Co., 407 U.S. 1 (1972) (forum selection clauses are “presumptively valid”). Arbitral forum selection clauses are generally enforceable and the FAA preempts any contrary state law.

Judicial forum selection clauses in the following states will not be enforced to require a franchisee to litigate outside the franchisee’s home state: California, Connecticut, Illinois, Indiana, Iowa, Louisiana, Maryland, Michigan, Minnesota, New Jersey, North Carolina, North Dakota, Rhode Island, South Carolina, and Wisconsin. In a case involving the California statute, the Ninth Circuit rejected a franchisor’s claim that the franchise agreement’s provision for a Pennsylvania forum prevented the California franchisee from suing in California. Jones v. GNC Franchising, Inc., 211 F.3d 495 (9th Cir. 2000). See also Kubis & Perszyk Assoc., Inc. v. Sun Microsystems, Inc., 680 A.2d 618 (N.J. 1996) (held enforcement of forum-selection clauses in franchise agreement undermined protections of the N.J. franchise law and were presumptively invalid).

In the absence of an express statutory restriction, judicial forum selection clauses are otherwise “presumptively valid” and should be “specifically” enforced, unless the resisting party “could clearly show that enforcement would be unreasonable and unjust, or that the clause was invalid for such reasons as fraud and overreaching.” The Bremen v. Zapata Off-Shore Co., 407 U.S. 1 (1972). In order to demonstrate unreasonableness, the challenging party must show that “trial will be so gravely difficult and inconvenient that [the party seeking a different forum] will for all practical purposes be deprived of his day in court.”

Assuming that the franchise agreement is not unconscionable, arbitral forum selection clauses are generally enforceable, notwithstanding state statutes, which could be read to limit them, because the FAA preempts these statutes. In Bradley v. Harris Research, Inc., 275 F.3d 884 (9<sup>th</sup> Cir. 2001), *supra*, a California franchisee sought to invalidate a franchise agreement provision requiring arbitration in Utah. In reversing the district court, the Ninth Circuit required the California franchisee to arbitrate in Utah. Even though (1) the franchisee had signed the franchise agreement under protest, asserting that it was a contract of adhesion and lacked mutuality, and (2) California franchise law provides that “a provision in a franchise agreement restricting venue to a forum outside this state is void,” the Ninth Circuit found that the arbitration agreement was binding and that the arbitration should take place in

Utah because the FAA preempted the California franchise law. The franchisees did not raise unconscionability on appeal. See *also* Doctor's Assoc., Inc. v. Hamilton, 150 F.3d 157 (2<sup>nd</sup> Cir. 1998) (N.J. franchise law preempted by FAA); OPE Int'l LP v. Chet Morrison Contractors, Inc., 258 F.3d 443 (5<sup>th</sup> Cir. 2001) (Louisiana franchise law preempted by FAA).

Other recent decisions suggest, however, that franchisees may be able to avoid arbitration in distant venues by arguing that venue provisions are unconscionable. See, e.g., Ticknor v. Choice Hotels Int'l, Inc., 265 F.3d 931 (9th Cir. 2001) (franchise agreement's arbitration provision requiring arbitration in Maryland under Maryland law held unconscionable under Montana law and not preempted by the FAA); Bolter v. Superior Court, 87 Cal. App. 4<sup>th</sup> 900 (2001) (court struck down part of arbitration provision which required arbitration in Utah because it was unconscionable and not preempted by the FAA). A California court recently held that a requirement that a California consumer arbitrate in Georgia was unconscionable, stating "a forum selection clause that discourages legitimate claims by imposing unreasonable geographical barriers is unenforceable under well-settled California law." Aral v. Earthlink, Inc., 134 Cal. App. 4<sup>th</sup> 544 (2005). The court decided that whether the forum selection clause was unconscionable was a "gateway" issue for the court, not the arbitrator, thereby avoiding FAA preemption.

### c. Choice of Law

Most states follow the Restatement position that choice of law provisions should be honored unless:

- (A)(1) There is no substantial relationship between the state and (a) the parties or (b) the transaction and (2) there is no other rational reason for choosing the law of the state; or
- (B) Using the law of the chosen state would be contrary to a fundamental policy of (1) a state that has a materially greater interest in the matter, or (2) a state whose law would apply in the absence of the choice of law provision.

Restatement (Second) of Conflicts § 187.

The Court in Ticknor v. Choice Hotels Int'l, Inc., 265 F.3d 931 (9th Cir. 2001), applied the Restatement test in accordance with Montana law and refused to enforce a choice of law provision in favor of Maryland because the Court found the contract as a whole to be a contract of adhesion.

However, even if the choice of law provision passes the Restatement test, several states with franchise disclosure and franchise relationship laws have anti-waiver provisions to insure that franchisees residing or operating in the state have the protection afforded by that state's law. Notwithstanding these anti-waiver laws, in a case involving a California franchisor and a Pennsylvania franchisee, Cottman Transmission Sys., Inc. v. Melody, 869 F. Supp. 1180 (E.D. Pa. 1994), the Court held that the California franchise laws did not void a choice of law provision in favor of Pennsylvania law with respect to claims of fraud and negligent misrepresentation in connection with the sale of a franchise.

d. Waiver of Class-Wide Relief

Recently, in Independent Association of Mailbox Center Owners, Inc. v. Superior Court, 133 Cal. App. 4<sup>th</sup> 396 (2005), franchisees of Mail Boxes, Etc. sought to pursue claims on a classwide basis based upon the forced conversion of their stores to a new format ("UPS Stores") after the acquisition of the franchisor by UPS. The franchise agreement for many of the franchisees contained a clause banning classwide arbitration. Finding that franchise agreements can have some characteristics of contracts of adhesion, and their provisions can be examined to see if they contain provisions that are unconscionable, the court refused to enforce a class action waiver it found to be adhesive and unconscionable. (The court also found that a class was appropriate even though there were three separate forms of contracts involved and that there were "difficult issues" remaining regarding "separating out the common issues of law and fact ... from the individualized ... issues.") See also Discover Bank v. Superior Court, 39 Cal. 4<sup>th</sup> 148 (2005) ("class action waivers in consumer contracts of adhesion are unenforceable, whether the consumer is being asked to waive the right to class action litigation or the right to classwide arbitration"); Aral v. Earthlink, Inc., 134 Cal. App. 4<sup>th</sup> 544 (2005) (ban on class-wide arbitration in consumer case held unconscionable).

e. Jury Trial Waiver

The right to a jury trial is waivable in federal courts and in all states but Georgia, Minnesota and California. See Bank South, N.A. v. Howard, 444 S.E.2d 799 (Ga. 1994); Minnesota Rules, 1995, Department of Commerce Section 2860.4400.J; Grafton Partners L.P. v. Superior Court, 36 Cal. 4<sup>th</sup> 944 (2005) (California Supreme

Court unanimously decided that a pre-dispute jury trial waiver in a contract between an accounting firm and its client was unenforceable because it violated the state constitution). *Cf. AAMCO Transmissions v. Harris*, 1990 U.S. Dist. LEXIS 7387 (E.D. Pa. 1990) (jury waiver enforced in litigation between franchisee and franchisor).

Any waiver of a jury trial, however, must be conspicuous. *Westide-Marrero Jeep Eagle, Inc. v. Chrysler Corp.*, Bus. Franchise Guide (CCH) ¶ 11,710 (E.D. La. 1999) (waiver in franchise agreement just above signature block held enforceable).

f. Punitive Damages Waiver

Courts are divided on whether or not punitive damages may be waived.

California courts have deemed waivers of punitive damages and other remedies to be unenforceable. As stated by the court in *Independent Association of Mailbox Center Owners*, supra, "To the extent that the arbitration clauses ... seek to deprive the claimants of statutorily authorized remedies [including punitive damages], or relief a court would otherwise be allowable to them, they are unconscionable, and the trial court should have stricken them from the arbitration clause." But see *Bolter v. Superior Court*, 87 Cal. App. 4<sup>th</sup> 900 (2001) (although the court relied on, among other things, the punitive damages waiver to find the arbitral forum selection clause unconscionable, it did not strike the punitive damages waiver).

Some courts are in accord, and others are not. See, e.g., *Ex Parte Thicklin*, 824 So.2d 723 (Ala. 2002) (Alabama Supreme Court finds punitive damages waiver to be unconscionable); *Sanderson Farms, Inc. v. Gatlin*, 848 So.2d 828 (Miss. 2003) (Mississippi Supreme Court holds punitive damages waiver to be enforceable).

Some statutes expressly prohibit waivers of punitive damages. Most notably perhaps, the PMPA expressly prohibits the waiver of any rights under the law. 15 U.S.C. § 2805(f); *Graham Oil Co. v. ARCO Products Co.*, 43 F.3d 1244 (9th Cir. 1995).

g. Provisions re Time Limitations on Claims

As a general rule, courts allow parties to agree on shorter limitations periods than those prescribed by statute, as long as the shorter periods are reasonable. *Tupper v. Bally Total Fitness*

Holding Corp., 186 F. Supp. 2d 981 (E.D. Wis. 2002). A shortened limitations period is unreasonable if it is so short that it shows that it effectively prevents lawsuits. Northlake Reg'l Medical Center v. Waffle House Sys. Emp. Benefit Plan, 160 F.3d 1301 (11<sup>th</sup> Cir. 1998).

A shortened limitations period has been held to be unreasonable where it benefits only one party. Burroughs Corp. v. Suntogs of Miami, Inc., 472 So.2d 1166 (Fla. 1985). However, at least one court has enforced a limitations period that limited only claims of the franchisee. Thabet v. Mobil Corporation, Bus. Franchise Guide (CCH) ¶ 12,612 (Cal. App. 2003). The safer and maybe better practice is to make such provisions mutual where possible. See discussion *infra* at V.G.3. g.

Some states and federal statutes have statutory bars on changing the limitations period, where the shorter period restricts the ability to enforce any rights through a legal proceeding. Idaho Code § 29-110(1), Sheehan v. Norris Irrigation, 410 N.W.2d 569 (S.D. 1987) (applying South Dakota law). Maryland law specifically prohibits shorter limitation periods for claims brought under franchise and unfair competition laws. D&K Foods, Inc. v. Bruegger's Corp., Bus. Franchise Guide (CCH) ¶ 11,506 (D. Md. 1998). Similarly, the parties cannot agree to a shortened limitations period that would effectively waive provisions of the PMPA. Graham Oil Co. v. ARCO Products Co., 43 F.3d 1244 (9th Cir. 1995) (cannot reduce one-year statute of limitations to 90 days).

### 3. Suggested Ways to Address Dispute Resolution Issues

#### a. Three-Step Process

One way to try to resolve disputes is a three-step process employed in a number of franchise agreements. Under this provision, the parties must engage in a face-to-face meeting and then participate in mediation, prior to engaging in arbitration. Obviously, however, this could create problems in terms of a speedy resolution of a matter. Therefore, it is important that the franchise agreement state that a demand for arbitration may be filed prior to, or during the pendency of, the face-to-face meeting and mediation process. It should also state that the face-to-face meeting and mediation are to take place as soon as possible after the filing. To avoid delay, strict time limits should be set forth, as well for the selection or appointment of the arbitrator and for the actual completion of the arbitration. The franchise agreement should make clear that the mediation and the arbitration may

proceed on parallel tracks to avoid unnecessary delay. Following is an example of such a provision:

- Claim Process. Any litigation, claim, dispute, suit, action, controversy, or proceeding ("Claim") between or involving you and us on whatever theory and/or facts based, and whether or not arising out of this Agreement, will be processed in the following manner, except as expressly provided below at Section [re injunctive relief carve-out].
- First, discussed in a face-to-face meeting held within 30 days after either you or we give written notice to the other proposing such a meeting.
- Second, if not resolved, submitted to non-binding mediation for a minimum of eight hours before (i) Franchise Arbitration and Mediation, Inc. ("FAM") or its Successor (or an organization designated by FAM or its Successor), or (ii) another mediation organization approved by all parties, or (iii) by Judicial Arbitration and Mediation Service (JAMS) or its Successor (or an organization designated by JAMS or its Successor), if FAM cannot conduct such mediation and the parties cannot agree on a mediation organization. Any mediation/arbitration (and any appeal of arbitration) will be conducted by a mediator/arbitrator experienced in franchising. Any party may be represented by counsel and may, with permission of the mediator, bring persons appropriate to the proceeding. If both you and we do not want to participate in mediation, you and we may proceed to arbitration as provided below.
- Third, submitted to and finally resolved by binding arbitration before and in accordance with the arbitration rules of FAM or its Successor (or an organization designated by FAM or its Successor); provided such that if arbitration is unable to be heard by any such organizations, then the arbitration will be conducted before and in accordance with the arbitration rules of JAMS or its Successor (or an organization designated by JAMS or its Successor). The arbitrator shall be experienced in franchising, and if the parties cannot agree on the appointment of the arbitrator within thirty days of commencement of the arbitration, then the arbitrator shall be selected solely and exclusively by the arbitration organization. On election by any party, arbitration and/or any other remedy allowed by this Agreement may be commenced prior to, or during the pendency of, the face-to-face meeting and mediation process. The face-to-face meeting and mediation are to take place as soon as possible after the commencement of the arbitration. In other words, the face-to-face meeting and/or mediation and the arbitration may proceed on parallel tracks for the purpose of

avoiding any delay. Judgment on any preliminary or final arbitration award shall be final and binding, and may be entered in any court having jurisdiction (subject to the opportunity for appeal as contemplated below).

- Fourth, a final award by an arbitrator (there will be no appeal of interim awards or other interim relief), may be appealed within thirty (30) days of such final award. Appeals will be conducted before a three (3) arbitrator panel appointed by the same organization as conducted the arbitration, each member of which shall be experienced in franchising. The arbitration panel will not conduct any trial de novo or other fact-finding function. Such panel's decision may be entered in any court having jurisdiction and will be binding, final and non-appealable.

b. Selection of Arbitrator, Rules in Arbitration

Franchise agreements should be very clear as to the organization which will conduct the arbitration (e.g., AAA, FAM, JAMS, etc.). There are many well-respected ADR organizations. However, each has its own rules and procedures (for example, as to the scope of discovery). Accordingly, consideration should be given as to the rules to be followed when selecting the organization.

As for particular arbitrators, it is helpful for a number of reasons if the arbitrator(s) are knowledgeable regarding franchise law. Therefore, a provision requiring that the arbitrators have a certain experience level in franchise law may be desirable (e.g., an attorney with at least 25 years experience, with his/her practice for the last 5 years comprised of at least 50% of his or her time being spent on franchise law matters). One potential problem with including such a requirement is that (depending on the amount of experience that is required) the potential pool of arbitrators may be relatively limited as a result, which could lead to delay.

c. Rules re Discovery in Arbitration

While each ADR organization has its own rules, the franchise agreement may be used to modify the rules, which are not desired, and it should, in any event, identify the rules on discovery. For example, the agreement may place limits on the scope of written discovery (e.g., document production demands only), the number of depositions, and the length of any depositions (such as the current seven hour limit in federal court).

A limitation on discovery that franchisors should consider strongly is that discovery may be had as to the relationship between the franchisor and the particular franchisee only, and as to no other franchisee. Such a limitation will not only limit the scope (and cost) of the arbitration, it will also prevent fishing expeditions by attorneys.

d. Equitable Relief Carve-Out

Even if a franchisor deems arbitration to be generally desirable, there are situations where arbitration will not enable the franchisor to obtain relief. The most obvious situation is where the franchisor is seeking injunctive relief on an emergency basis. Accordingly, the arbitration provision in the franchise agreement should provide that the parties may seek injunctive relief through the court system:

- Notwithstanding the arbitration provisions above, Franchisor may bring an action in any court of competent jurisdiction for injunctive or other extraordinary relief, without the necessity of posting any bond, as Franchisor deems necessary or appropriate (i) respecting violations of Franchisee's obligations under [the in-term covenant not to compete], or (ii) respecting the use or display of the Brand, or (iii) to otherwise compel Franchisee to take steps reasonably necessary to preserve Franchisor's reputation, goodwill and proprietary rights. Franchisee acknowledges that Franchisee is one of a number of licensed franchisees using the Brand and that failure on Franchisee's part to comply fully with any of the terms of this Agreement respecting the foregoing obligations regarding examinations, audits and the Brand could cause irreparable damage to Franchisor or its other franchisees. Therefore, Franchisor shall have the immediate right to seek a preliminary order or injunction enforcing the foregoing obligations during the pendency of all arbitration or other proceedings, without the necessity of Franchisor posting a bond. This covenant is independent, severable and enforceable, notwithstanding any other rights or remedies Franchisor may have.

e. Forum Selection

To the extent that they are otherwise enforceable (see above), franchisors should anticipate that franchisees will argue that forum selection provisions that require them to arbitrate in an inconvenient location are unconscionable. Thus, these provisions should be conspicuous in any agreement to enhance the chances that they

will be enforced. Having the Franchisee initial this, and other clauses likely to be challenged, may be a wise practice.

Any venue provision should include a provision barring the use of the forum state's conflict of laws rules to conclude that the matter should be heard in the home state of the franchisee.

f. Choice of Law

As noted above, most states will honor choice of law provisions in most circumstances. To increase the chances that the provision will be honored, it may be helpful to include language in the franchise agreement that the parties recognize that certainty as to the law to be applied to their relationships is important to their ability to conduct ongoing business, and that the parties have agreed that a particular state's law shall apply to any dispute between them related to the franchise relationship. To ensure that the franchisee can invoke the Lanham Act for pursuing claims under the Act for trademark infringement and unfair competition, the agreement should likely state that the state's law does not apply to the extent that the Lanham Act applies.

As discussed above, there will likely be situations where a franchisor does not want a particular state's law to apply. The franchise agreement should state that the law to be applied is that of a particular state, except for provisions deemed to be unenforceable under the law of that state, in which case the law of another state (perhaps the state where the franchisee is located or does the bulk of its business) shall apply. For California franchisors, a better approach could be to include a choice of law provision applying the law of the state of the franchisee, as follows:

- You and we agree on the practical business importance of certainty as to the law applicable to your and our relationship and its possible effect on the development and competitive positions of the System. Therefore, you and we also agree that, except with respect to the applicability of the Federal Arbitration Act, 9 U.S.C. § 1 et seq. and the effect of federal preemption of state law by such Act, and except to the extent governed by the United States Trademark Act and other federal laws and as otherwise expressly provided in this Agreement, this Agreement and all other matters, including, but not limited to, respective rights and obligations, concerning you and us, will be governed by, and construed and enforced in accordance with, the laws of the state where the largest geographic portion of your Area is located. You and we agree that this provision shall be enforced

without regard to the laws of such state relating to conflicts of laws or choice of law; except that the provisions of any law of that state regarding franchises (including, without limitation, registration, disclosure, and/or relationship laws) shall not apply unless such state's jurisdictional, definitional and other requirements are met independently of, and without reference to this Section.

g. Mutuality

For all arbitration and other pre-dispute provisions that do not provide for mutual obligations or are designed to be more restrictive to the franchisee than the franchisor, there is a real risk that such provisions may be invalidated. In fact, a non-mutual provision (e.g., non-mutual waivers) could jeopardize the entire arbitration agreement. Accordingly, the franchisor should strongly consider making all such provisions mutual.

h. Waivers of Rights

To the extent they are otherwise enforceable (see above), franchisors should anticipate that waivers, such as jury trial, punitive damages and class action waivers, will be attacked as unconscionable. Therefore, waiver language must be conspicuous. Requiring the franchisee to initial or otherwise acknowledge these waivers should increase the chances that they will be deemed enforceable (assuming they are not barred by statute, as noted above).

As with almost any provision of the agreement, it is important that waivers be easily severed from the rest of the agreement to avoid a court ruling the entire agreement to be so infected that it is discarded in its totality. In that regard, the franchise agreement should also have a provision explicitly stating that, if any provision of the agreement is deemed to be unenforceable, it shall be modified to the extent possible under law, and that the unenforceability of the provision shall have no effect upon the rest of the agreement.

Franchisors may consider carve-outs to any waivers. For example, a franchisor may wish to pursue punitive damages in actions with respect to trademark infringement, misappropriation of trade secrets, and indemnity provisions (i.e., to ensure that a franchisee must indemnify the franchisor for any punitive damages award related to the franchisee). Thus, the punitive damages waiver could provide an exception for these types of actions.

i. Provisions re Damages Limitations

In addition to provisions waiving punitive damages, the franchise agreement may place a cap on damages under which the total liability of the parties to each other relating to the franchise agreement in any way shall be no greater than a certain dollar amount.

j. Provisions re Time Limitations on Claims

As noted above, the courts generally uphold contractual limitations periods, if they are not too short (such as 90 days) or unilateral. The limitations provision in the franchise agreement should anticipate that the franchisee will seek to expand the time period to bring a claim by invoking the discovery rule (i.e., that the limitations period does not run until the claimant discovered the facts giving rise to the claim or should have discovered the facts in the exercise of reasonable diligence). Therefore, the contractual limitations period provision should not only set out a traditional limitations period, but also should explicitly place an outside limit on the time period for bringing claims, which runs from the date of the occurrence of the acts/omissions which give rise to the claim (much like a statute of repose). However, such a provision could be used by a franchisee to avoid the payment of fees, where a sufficient period of time elapsed before the franchisor discovered the delinquency. Therefore, franchisors may wish to consider carving out from any shortened limitations claims for the payment of ongoing fees where franchisees have misreported information.

## **SCHEDULE 1**

### **CHECKLIST FOR DEVELOPING**

#### **A FRANCHISE AGREEMENT**

This checklist is meant to facilitate your thinking as a prospective franchisor about what you should include in your franchise program. The items in this checklist should be considered from both a legal and a business perspective before structuring your franchise program or drafting a franchise agreement. Bear in mind that this list is not exhaustive and there may be some issues that are unique to your particular business that you should bring to our attention.

#### Term and Renewal

*What is the duration (term) of the franchise agreement?*

*Under what conditions can the franchisee renew the agreement?*

*How long is the renewal term? How many renewals?*

*Is there a renewal fee and how much?*

*Will the franchisee have to sign a new agreement at the time of renewal?*

*Under what conditions can the franchisor refuse to renew the agreement?*

#### Territory

*Will the franchisee be assigned a particular territory or distribution area? How will the territorial boundaries be determined (e.g., designated zip codes, cities/counties/states, population, radius from business)? Will sales outside of the territory be restricted? How will restrictions be enforced?*

*Exactly what, if any, exclusivity or protection is granted in the territory (e.g. no other franchise locations? no company-owned locations? )*

*Exactly what development and distribution rights are reserved to the franchisor in the territory, e.g. national account sales, on-line, telemarketing, catalog, other direct sales or distribution channels, sales of related or competing products/services under other trademarks?*

Standards of Operation and Quality Control.

Which of the following categories will the franchisor control and to what extent?

*Site selection*

*Appearance of premises*

*Hours of operation*

*Merchandise or services sold*

*Sources of supply -- franchisor, third parties, restrictions?*

*Prices. Suggested pricing or maximum pricing limits?*

*Bookkeeping/accounting procedures and systems*

*Employee dress or uniform*

*Customer service standards. Warranty program? Return policies? Customer complaint procedures?*

*Customer restrictions. Will the franchisee be limited to certain types of customers or distribution channels? Will the franchisor reserve certain customers or accounts to itself?*

*Sales quotas. Will the franchisee need to meet quotas to retain rights in the territory or to the franchise? How will they be determined?*

*Training franchisee and franchisee's employees. Who provides? Who must complete? Any ongoing training requirements?*

*Approved products and services. Must franchisee only offer what you approve? Must franchisee offer full line or certain key products/services?*

*New products and services. Under what conditions can you add or subtract products and services from the program? Are there any limits on changes? Can new products/services be fundamentally different from existing ones? Any limits on amount franchisee can be required to spend to implement changes?*

*Other businesses. Can the franchisee or its principals own/operate other businesses? Any limitations?*

*Required equipment and systems. Must the franchisee use specific equipment in the business? Who supplies? Any specific computer system or program required? Will the franchisor have on-line access to the computer system or data? Any proprietary software involved? Any franchisor Intranet?*

Payments for Franchise Rights

Initial fee. *How much is the initial franchise fee?*

Is it uniform for all franchises?

Negotiable?

Does it vary based on territory, population, other factors?

Method of payment

Lump sum

Financed

When is it due?

Refundable in whole or in part? If so, when and under what conditions?

Royalty. *How much is the royalty fee?*

How is it paid? Weekly? Monthly? Other?

What is the royalty based on? Gross sales? Other?

Fixed royalty percent or sliding scale based on volume?

Is there a minimum royalty? If so, how much is it?

Deposit. *Will the franchisee make an initial deposit before paying the balance of the franchise fee? If so, what is the amount of the deposit and when is it paid? Under what conditions, if any, is the deposit refundable? Will you reserve a territory in exchange for deposit?*

Supplies or Services Furnished by Franchisor

Will any supplies or services (including fees associated with use of a computer system) be sold to franchisees? If so, describe them and the method of payment.

Must franchisees purchase these items from the franchisor or are there other approved suppliers?

Equipment Furnished by Franchisor

Is any equipment sold/leased to franchisees?

If so, is it a separate transaction or part of initial franchise package?

Inventory

Describe the procedures for supplying inventory, including sources and any purchasing arrangements with third party sources.

Describe the procedures for payment of inventory.

Describe any inventory financing available from franchisor or from other sources.

Is there a bailment, consignment, commissioned sales or similar arrangement with the franchisee? If so, please explain.

Administrative Services and Fees

Any services such as bookkeeping, billing and collection provided to franchisee for a fee (in addition to royalty)? Describe.

Bundled or unbundled services (package or pick and choose)?

Advertising and Promotion Expenses. How much, if anything, will the franchisee have to spend on each of the following types of advertising:

National

Local

Regional

To whom are the payments made (e.g., to suppliers, franchisor, regional cooperatives or national advertising fund)?

Will the franchisor establish separate funds or entities for any particular type of advertising, e.g., national advertising fund or regional cooperatives? Who administers and is there an administration fee? Who controls creative content, media, geographic

scope? Any franchisee input as to advertising themes, content or focus? Any limitations on use of the funds?

#### Assistance of Franchisor

*Training. Initial? Continuing? At whose expense? Fees?*

*Advertising and marketing. Brochures, promotions, media advertising, direct mail, business leads, 800 number, web page, ad slicks?*

*Ongoing advice and consultation? How much, how often?*

*Field support. Will you send representatives to the franchisee's location on a periodic or as requested basis? Will you provide written reports or evaluations?*

*Business "audits"?*

*Conferences and franchisee meetings?*

*Supplier/vendor discounts, purchasing arrangements?*

*National account sales/support?*

- I. Intranet? What are its functions?
- J. Proprietary computer or POS system? Functions?
- K. Other technology or Web-based assistance, e.g., reservation system?

#### Site Selection and Control

*From what type of location does the franchisee operate (retail, warehouse, commercial office, home office)?*

*Location/site approval? What are criteria for approval?*

*Assistance in site selection? Will you assist in identifying, evaluating and/or selecting site? If so, describe how.*

*Leases. Will you assist in negotiating or reviewing the lease? Will you require certain provisions to be included in the lease?*

*Site specifications - size, cost, permitted use*

*Signage*

*Relocation. Is it permitted and what conditions?*

*Satellite, temporary or kiosk locations. Are they permitted and under what conditions?*

*Franchisor control. Will you want site control so you can take over premises from franchisee? How will you secure that control (e.g., leasing of premises and subleasing to franchisee, collateral assignment of lease)?*

## Trademarks

*Federally registered trademark(s)?*

*State registrations?*

*What rights does franchisee have to use the trademarks? Who else has been granted rights to use?*

*What will you do if someone infringes the marks?*

*Will you indemnify franchisee if a third party sues for infringement?*

*How do you plan to monitor franchisee use of the marks (approval of advertising, field visits, control of supplier for business cards, stationery)?*

*Rights to change or modify the trademarks. Who pays for costs if the marks are changed?*

## Other Intellectual Property

*What trade secrets are used in the business (e.g., business methods and formats, techniques, procedures, recipes, formulas, customer data that are not generally known and have competitive value?)*

*How are trade secrets protected (e.g., confidentiality agreements, security measures?)*

*Any patented devices or processes? What are franchisee's rights to use?*

*Any copyrights such as those for proprietary software, web sites, manuals, curricula, advertising materials? What are franchisee's rights to use?*

*How are copyrights protected (e.g., copyright registrations, license agreements)?*

*Is a covenant not to compete necessary?*

*During the term of the agreement?*

Post term? Applicable on all terminations, nonrenewal?

How long will it last?

In what geographical area will it be effective?

*Grant-back of improvements developed by franchisee?*

Compliance with Laws/Indemnification

*Franchisee responsible for all permits, licenses? Any industry specific licensing or regulatory requirements?*

*Franchisee indemnity of franchisor. Anything excluded? Control of defense?*

*Requirement to carry insurance. Franchisor as additional insured. What types of coverage? Policy limits? Approved carriers?*

Settlement of Disputes

*Grievance procedures?*

*Use of nonbinding mediation or binding arbitration? If so, what disputes are covered (e.g., territory disputes) and what will be excluded (e.g., trademark matters)?*

*Who pays costs of mediation or arbitration?*

*Where will mediation, arbitration or litigation take place?*

*Attorneys' fees to prevailing party? (two-edged sword)*

*Limitation of punitive or other damages (enforceability?)*

*Jury trial waiver (enforceability?)*

Termination of the Agreement

*What events trigger termination without opportunity to cure, e.g., insolvency, repeated defaults, abandonment, material misrepresentation?*

*What defaults are curable and how long to cure?*

*How to wind up the business. Will you take over the business and if so, how is this implemented (e.g., buy-out option). Will you buy back inventory? Fixtures? Signs? Other?*

*Post-termination requirements, e.g., de-identify, assign telephone numbers, return proprietary items. Other?*

## Franchisee's Business Organization

*Will you require the franchisee to be a specific type of business entity (sole proprietorship, general partnership, corporation, limited liability company) or will you prohibit certain entities from owning the franchise (e.g., limited partnerships)?*

*Will you require the franchisee to form a new corporation or other entity solely for the purpose of owning the franchise?*

*Will a principal owner of the franchise be required to personally operate/devote best efforts to the business, or can the franchisee hire a manager? Will managers need to be equity owners of the franchise?*

*When do you want to know (and approve) of a transfer of an ownership interest in the franchise? 20%? 10%? Change in control? Other?*

## Transfer or Sale of the Franchise

*Under what conditions will you consent to new owner?*

*Are there different conditions for transfer of less than controlling ownership interest?*

*Conditions of transfer approval. Transfer fee (how much?), release of claims, new owner training, paying amounts due, signing a release or signing a current franchise agreement...Any that don't apply? Any others that do?*

*Standards of personal and financial ability of new owner*

*Do you want the right of first refusal on any sales or transfers?*

*Do you want an option to buy back the franchisee's business and territory rights? If so, explain when it could be exercised and valuation method.*

*Procedures upon death or disability of a franchisee. Will you terminate the franchise or permit continued operation until substitute franchisee is found? How long to find new franchisee? Will you assist in running the business temporarily?*

## Supplier Arrangements/Third Party Contracts

*Key vendors/suppliers. Are there arrangements with third parties that support or are critical to the operation of the franchise system or the franchised business?*

*Contracts. What agreements are in place with suppliers? How are you going to secure the continuation of supplier arrangements? Contingency plans for substitute or supplemental suppliers?*

*What happens to the franchise if any such arrangement is interrupted or terminates? Consider disclaimers of franchisor responsibility for supplier actions.*

## Development Rights

*Development agreements. Will you sell rights to develop a territory? If so:*

*What will you charge for those rights?*

*How will you establish the development schedule, assess market penetration goals and evaluate results?*

*How will you enforce development requirements?*

*Is territory exclusive and if so, to what extent (see discussion above on territory)? What are the conditions for maintaining exclusivity (e.g., meeting certain sales or development goals)?*

*Under what circumstances will development rights terminate or be terminable?*

*Franchisee rights of first refusal for additional franchises or territories?*

*Franchisee options for additional franchises or territories?*