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ABSTRACT

Vicarious liability in the franchising context is a fundamental issue, both in the United States and foreign jurisdictions. With no all-encompassing, clear precedent in the United States, other nations' approaches may provide lessons for American lawmakers and the U.S. franchising community. Together, the division between jurisdictions and the absence of uniform standards for imposing vicarious liability on franchisors demonstrate the need for more comprehensible and predictable case law. This need can be met through an examination of European regulations, model laws, and guidelines, as well as the laws in a number of nations worldwide, which indicate a pathway to better franchise agreements and possible governmental mandates (e.g., prominent, required notices about a franchise's business ownership). Franchisors would have in hand the means to determine their risks and plan their behavior, even accounting for the more effective approaches to franchisor vicarious liability that are sometimes found elsewhere in the global franchising community.

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I. INTRODUCTION

Franchising is one of the most popular methods for running and expanding a business. In the United States, there are approximately 760,000 operating franchised units,[1] accounting for one-third of all retail sales,[2] over 8.2 million directly employed persons,[3] another 10 million indirectly related jobs,[4] and over $2 trillion in annual retail

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1. IHS GLOBAL INSIGHT, FRANCHISE BUSINESS ECONOMIC OUTLOOK: MAY 2013 3 (May 31, 2013), http://emarket.franchise.org/Franchise_Business_OutlookMay.pdf [perma.cc/NE3Q-PHSX] (archived Jan. 28, 2017).

2. This has long been franchising's rough percentage of the total retail economy, since at least the year 2001. ROGER D. BLAIR & FRANCINE LAFONTAINE, THE ECONOMICS OF FRANCHISING 26–27 n.28 (2005). For earlier statistics, see LAVERNE L. LUDDEN, FRANCHISE OPPORTUNITIES HANDBOOK v (1995); Robert W. Emerson, *Franchising Covenants Against Competition*, 80 IOWA L. REV. 1049, 1050–51 n.4 (1995) (citing numerous sources concerning the rapid growth of franchising in both the 1980s and the early 1990s).

3. LUDDEN, *supra* note 2, at v.

4. *Id.*; *Franchise Businesses Produce Significant Impact on U.S. Economy*, INT'L FRANCHISE ASS'N, http://www.buildingopportunity.com/ (last visited Aug. 25, 2016) [https://perma.cc/LW2W-BDJF] (archived Jan. 28, 2017); INTERNATIONAL FRANCHISE ASSOCIATION, THE ECONOMIC IMPACT OF FRANCHISED BUSINESSES, VOLUME II: EXECUTIVE SUMMARY AND HIGHLIGHTS 6–7 , 11–12 (2008), http://www.franchise.org/uploadedFiles/Franchisors/Other_Content/economic_impact_documents/EconImpact_Vol2_HiLights.pdf [hereinafter NEC, The Economic Impact] [https://perma.cc/A82Q-

sales.[5] Furthermore, the American concept of franchising is expanding rapidly throughout the world, accounting for an ever-growing share of international commerce.[6] Collectively, these businesses have accrued hundreds of billions of dollars in annual sales.[7] This trend towards franchising means that the need for regulations in the franchise sphere is more important than ever. In response, more and more governments have decided to police those who choose to franchise with franchise-specific legislation; such legislation has already been integrated into over thirty nations' legal regimes.[8] This worldwide rise in domestic regulation will no doubt continue.

Overall, worldwide franchising, even more so than franchising in the United States, has experienced a high rate of growth in recent years.[9] As an example, Germany, a country where the first McDonald's

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SNB9] (archived Jan. 28, 2017) (stating that franchising—directly or indirectly—accounted for over 20 million jobs, representing an expanding proportion, over 15 percent, of the total private-sector workforce). Of course, while the number of direct employees was as high as 11 million in 2005, it certainly fell some during the economic downturn of 2008-10. *See* Robert W. Emerson, *Franchise Encroachment*, 47 AM. BUS. L.J. 191, 198 n.30 (2010) (citing employment statistics at just over 9.5 million employees as of 2009).

5.. As of 2006, franchising generated an overall output of $1.53 trillion. *Small Company Trends in 2007*, THE TRIB. (Dec. 31, 2006), http://www.greeleytrib.com/article/20061231/BUSINESS/112310347 [https://perma.cc/N96R-TLJ7] (archived Jan. 28, 2017). More current U.S. estimates are: 3,000 different franchisors in over 300 different business categories; more than 900,000 businesses (about one in 12 of total businesses) are franchised, and they generate almost 18 million jobs as well as over $2.1 trillion of economic output, including approximately 50 percent of all retail sales. *See Quick Franchise Facts - Franchising Industry Statistics*, AZFRANCHISES.COM, http://www.azfranchises.com/quick-franchise-facts/ (last visited Aug. 25, 2016) [https://perma.cc/CM4F-RMAW] (archived Jan. 28, 2017) (stating that franchises have generated over $2 trillion to the economy).

6. *See* Emerson, *supra* note 4, at 196–97 n.23 (detailing the numerous statistics indicating the phenomenal growth of franchising worldwide, both throughout Europe and such diverse and important national economies as those of Australia, Brazil, China, India, and Japan).

7. *See* MAN. LAW REFORM COMM'N, *Event Summary: Franchise Symposium Material Consultation Paper on Franchising Legislation*, 8 ASPER REV. INT'L BUS. & TRADE L. 181, 187 (2008) (reporting that according to a study conducted in 2001, "more than 767,000 franchised businesses directly employ[ed] 9.8 million people, with a payroll of $229 billion and an economic output of nearly $625 billion"; also noting that franchising in 2001 accounted for 11 percent of the private sector payroll and 9.5 percent of the private sector economic output - more than $1.53 trillion).

8. *See Executive Summary of Franchise Laws Around the World*, DLA PIPER (2008), http://files.dlapiper.com/files/upload/Summary%20on%20Intl%20Franchise.pdf [https://perma.cc/93R4-8QZD] (archived Jan. 28, 2017) (summarizing the laws of the 33 nations that specifically govern franchising); *see also Laws Applicable to Franchising*, DLA PIPER (2008), http://www.dlapiper.com/files/upload/Map%20Franchise%20Laws%20Global%20FINAL%20(2).pdf [https://perma.cc/47NC-NTK3] (archived Jan. 28, 2017) (map showing the spread of franchising-specific legislation across the globe – thirty-three nations, including six in the Americas, fifteen in Europe (seven European Union Nations and eight non-EU countries), and eight in East or Southeast Asia).

9. *See* Emerson, *supra* note 4, at 196–97 n.24 (detailing the numerous statistics indicating the phenomenal growth of franchising worldwide). In the United States, franchised businesses operated over 800,000 establishments in 2016, including

opened in 1971,[10] saw a 50.79 percent increase in franchisors, an 83.87 percent increase in franchisees, and a 40.62 percent growth in franchises from 1998 to 2008.[11] Similarly, China, a country that only recently opened its doors to the global market, has enjoyed steady growth in franchising, reaching over 1 million franchise shops by 2011.[12]

As franchises have increased in international popularity, crucial legal issues have emerged concerning basic jurisdictional matters, such as conflicts of law, fundamental contract interpretation disputes—or even exclusion of clauses in the franchise agreement—and the franchisor's potential vicarious liability for its franchisee's tortious actions. The contract and tort issues arise, in part, from a tenet of franchise ownership and management: franchisees are not completely free to run the business as they see fit. Besides government regulation of businesses generally, the franchisee is subject to the rules imposed by the franchisor in the parties' agreement or in ancillary documents (e.g., the operations manual).[13]

This Article concerns vicarious liability in the franchising context, as addressed in a number of foreign jurisdictions. As there is a lack of clear precedent in the United States, these foreign approaches may provide lessons for American lawmakers and the U.S. franchising community.[14] The lack of uniform standards for imposing vicarious

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franchisees and franchisor-owned establishments. In 2016, franchised businesses directly provided nearly nine million jobs, met a $351 billion payroll, produced $868 billion of output and added over $541 billion of gross domestic product. IFA FRANCHISE EDUCATION AND RESEARCH FOUNDATION (HIS MARKET ECONOMICS), THE ECONOMIC IMPACT OF FRANCHISED BUSINESSES: VOLUME IV (2016), http://franchise.org/sites/default/files/Franchise_Business_Outlook_Jan_2017.pdf [https://perma.cc/AP33-SFB4] (archived Mar. 16, 2017).

10. *A Brief History of McDonald's*, MCSPOTLIGHT, http://www.mcspotlight.org/company/company_history.html (last visited July 11, 2013) [https://perma.cc/BEE6-DKAY] (archived Jan. 28, 2017).

11. DEUTSCHER FRANCHISE VERBAND, FRANCHISE-FAKTEN 2010 4 (2010), https://www.rheinhessen.ihk24.de/blob/mzihk24/starthilfe/downloads/1450396/a9112a23d935eb37775837d3afd21eb4/Franchise_Fakten_2010-data.pdf [https://perma.cc/PQN4-QQ4V] (archived Feb. 11, 2017).

12. Ella S.K. Cheong, *China*, *in* INTERNATIONAL FRANCHISING CHN/1 (Dennis Campbell ed., 2nd ed., 2016); *see also* Robert W. Emerson, *Franchisees as Consumers: The South African Example*, 37 FORDHAM INT'L L.J. 455, 464 n.55 (2014) (detailing the large and growing presence of franchising in South Africa as well as in the even bigger, more established Australian, Chinese, French, and U.S. economies). By 2016, China's top 100 franchises generated total sales in 2016 equating to $66 billion. U.S. INT'L TRADE ADMIN., DEPT. OF COM., 2016 TOP MARKETS REPORT: FRANCHISING 19 (2016), http://www.trade.gov/topmarkets/pdf/Franchising_Top_Markets_Report.pdf [https://perma.cc/ZMH7-S9SY] (archived Mar. 16, 2017). China has over 4,500 franchises, more than even in the United States. *Id.*

13. *See* Schlotzsky's, Inc. v. Hyde, 538 S.E.2d 561, 562 (Ga. Ct. App. 2000) (stating that the franchisee has full and complete control of the day to day operation except as set forth explicitly in agreements with the franchisor).

14. *Compare* Kerl v. Dennis Rasmussen, Inc., 682 N.W.2d 328, 332 (Wis. 2004) (demonstrating the majority approach to franchisor vicarious liability, which assumes

liability on franchisors has undermined the ability of parties to a franchise agreement to evaluate the risks of entering into the relationship and better plan their subsequent behavior. This demonstrates the need for more understandable and predictable case law.

This Article also analyzes the variance in the national franchise legislation of foreign countries. Typically, courts in these various nations will analyze a franchisor's potential vicarious liability based on domestic legal systems.[15] For example, in civil law countries, such as France and Italy, the analysis relies heavily on the consumer's reasonable expectation as to the ownership and control of the franchise.[16] In contrast, in common law countries, such as the United States and Australia, the analysis turns on the extent of the control that a franchisor has over its franchisees.[17] Despite the lack of uniform standards in both U.S. and international franchising communities, vicarious liability in general has three core requirements: First, there must be a legally sufficient relationship existing between the person causing the plaintiff's injury and the vicariously liable defendant.[18] Second, the person must act wrongfully in causing the plaintiff's injury.[19] Third, the tortious act must have occurred within the scope of the relationship between the tortfeasor and the vicariously liable defendant.[20] The first core element of vicarious liability, the legally sufficient relationship, has been the source of much of the confusion in establishing a consistent blueprint in franchising law. Courts in countries that follow common law traditions have a problem defining the level of control needed to establish a relationship's legal sufficiency.

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that an independent agency relationship exists between the franchisor and franchisee and focuses on the question of whether the franchisor had sufficient control over the proximate cause of harm to make it vicariously liable), *with* Myers v. Garfield & Johnson Enters., Inc., 679 F. Supp. 2d 598, 617 (E.D. Pa. 2010) (demonstrating the minority approach and holding that the franchisor was potentially liable under three different theories: (1) directly as a "joint employer" with franchisee; (2) vicariously as franchisee's actual principal under an agency relationship; and (3) vicariously as plaintiff's "ostensible" employer).

15. GREGG RUBENSTEIN ET AL., VICARIOUS AND OTHER FRANCHISOR LIABILITY, 26 (2011), http://www.franchise.org/sites/default/files/ek-pdfs/html_page/vicariousliability(1)_0.pdf [http://perma.cc/HP8B-BLPK] (archived Jan. 28, 2017).

16. *Id.*

17. *Id.*

18. Joseph H. King, Jr., *Limiting the Vicarious Liability of Franchisors for the Torts of Their Franchisees*, 62 WASH. & LEE L. REV. 417, 424 (2005); RESTATEMENT (THIRD) OF AGENCY § 7.08 (2006). To this kind of claim some courts have answered that the plaintiff did not rely on the franchisor's care, at least with respect to the injuries suffered in the particular case, although others have denied the apparent-agency claim on the ground that a franchisor does not hold out the franchisee as an agent merely by licensing the trademark to him. *See* DAN B. DOBBS, PAUL T. HAYDEN, & ELLEN M. BUBLICK, THE LAW OF TORTS § 433 (2012) (explaining what makes a relationship legally sufficient in the vicarious liability context).

19. King, *supra* note 18.

20. *Id.*; *see also* RESTATEMENT (THIRD) OF AGENCY §7.07 (2006).

This Article examines franchisor vicarious liability in several foreign jurisdictions in an attempt to reduce the confusion surrounding franchisor vicarious liability in the United States.

II. THE CURRENT STATE OF VICARIOUS LIABILITY IN THE UNITED STATES

In the United States, the legally sufficient relationship requirement can be met either by establishing the presence of an actual, sufficient relationship (i.e., an actual agency relationship) or by satisfying one of the exceptions to the relationship requirement (e.g., the apparent agency exception, which is the most important exception in determining franchisor vicarious liability).[21] Thus, courts have identified two basic agency law theories for holding a franchisor vicariously liable: establishing either the actual or the apparent authority of the franchisee to render its franchisor liable for its conduct.[22] These concepts are based on traditional common law and have been applied to tort, statutory, and contract claims, as well as to the franchise relationship.[23]

A franchisor "may be held liable for acts of his franchisee when the actual relationship between them is that of principal and agent or master and servant."[24] Through this actual agency principle, a franchisor, like any other principal, is responsible for the acts or omissions of a franchisee that is, in fact, operating as the franchisor's agent.[25] The traditional approach for determining whether an economic relationship will be legally sufficient to support this application of vicarious liability is the *control test*,[26] which derives from the language of the Restatement (Second) of Agency: a servant is one "who with respect to the physical conduct in the performance of the services is subject to the other's control or right to control."[27] There are ten factors considered when applying the control test.[28] While most

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21. *See generally* Heather Carson Perkins et al., *Franchisor Liability for Acts of the Franchisee*, 29 FRANCHISE L.J. 174, 176 (2010) (noting that "the law on vicarious liability appears to be trending toward and analysis of whether the franchisor controlled the instrumentality that caused the harm").

22. DAVID A. BEYER, VICARIOUS LIABILITY (2013), http://www.franchise.org/sites/default/files/ek-pdfs/html_page/VICARIOUS-LIABILITY-_David-Beyer__0.pdf [http://perma.cc/A24T-4N6L] (archived Jan. 28, 2017); *see* THOMAS LEE HAZEN & JERRY W. MARKHAM, CORPORATIONS AND OTHER BUSINESS ENTERPRISES: CASES AND MATERIALS 40–41 (2009) (discussing how the issue of the right to control in a franchise context determines whether a franchisor has opened itself up to liability under either actual or apparent agency).

23. HAZEN & MARKHAM, *supra* note 22, at 41.

24. King, *supra* note 18, at 429.

25. BEYER, *supra* note 22, at 5.

26. King, *supra* note 18, at 430.

27. RESTATEMENT (SECOND) OF AGENCY § 220 (1958).

28. *Id.*; *see, e.g.*, Jones v. Filer, Inc., 43 F. Supp. 2d 1052, 1056 (W.D. Ark. 1999) (applying the ten factors). The *Jones* court expounded:

franchise agreements explicitly assert that the parties are independent contractors and disclaim any agency relationship,[29] the terms of "the contract will not be dispositive and the courts will review the true nature of the relationship in making its decision."[30] The courts will typically consider operations manuals and the underlying circumstances in assessing whether an actual agency relationship exists.[31]

In taking this holistic approach to actual agency, courts commonly require that the control of the franchisor relate to the day-to-day operations of the franchisee in order to establish vicarious liability.[32] Courts additionally distinguish control intended primarily to ensure the "uniformity and the standardization of products and services" of the franchisee from control over the "actual day-to-day work"—the majority of courts adopt this "daily operations" control test.[33] Moreover, many of these courts have required not only that the franchisor's control encompass day-to-day operations but also that the franchisor's control extend to the instrumentality for the injury at issue.[34]

> In deciding whether a given individual or entity is an agent or an independent contractor, the Arkansas courts have considered the ten factors found in § 220 of the Restatement (Second) of Agency: (a) the extent of control which, by agreement, the master may exercise over the details of the work; (b) whether or not the one employed is engaged in a distinct occupation or business; (c) the kind of occupation, with reference to whether, in the locality, the work is usually done under the direction of the employer or by a specialist without supervision; (d) the skill required in the particular occupation; (e) whether the employer or the workman supplies the instrumentalities, tools, and the place of work for the person doing the work; (f) the length of time for which the person is employed; (g) the method of payment, whether by the time or by the job; (h) whether or not the work is a part of the regular business of the employer; (i) whether or not the parties believe they are creating the relation of master and servant; and (j) whether the principal is or is not in business.

Id.

29. *See* Robert W. Emerson, *Franchise Contract Interpretation: A Two-Standard Approach*, 2013 MICH. ST. L. REV. 641, 697 (2013) (a survey of 100 U.S. franchise agreements in 2013 found 74 percent had a provision stating that the franchisee is an independent contractor and not an agent, although this is down from 91 percent of the franchise agreements for a comparable survey in 1993).

30. BEYER, *supra* note 22, at 5; *see, e.g.*, *In re* FedEx Ground Package Sys., 662 F. Supp. 2d 1069, 1085 (N.D. Ind. 2009) (citing Brown v. Who's Three, Inc., 457 S.E.2d 186, 191 (Ga. Ct. App. 1995)) (stating that the contractual characterization is not controlling and the fact finder may look beyond the terms of the contract).

31. *See FedEx*, 662 F. Supp. 2d at 1085 (providing examples of other materials a fact finder may look at when determining whether an actual agency relationship exists).

32. King, *supra* note 18, at 431.

33. *Id.* at 432.

34. *Kerl*, 682 N.W.2d at 338–41 (finding ten cases where courts adopted this narrower "instrumentality" causing the harm prerequisite for franchisor vicarious liability, rather than the broader standard of control generally regardless of whether related to the actual cause of harm); *see* RUBENSTEIN ET AL., *supra* note 15 (detailing the current majority approach to franchisor vicarious liability adopting the basic agency

A recent case exemplifying this approach is *Patterson v. Domino's Pizza, LLC*,[35] in which a franchisee's employee claimed that she was sexually harassed by a coworker, and that both she and the harasser were actually employees of Domino's, the franchisor. In a four-to-three holding that relied heavily on the terms of the franchise agreement, the California Supreme Court reinstated summary judgment for Domino's. The court declared that "[a] franchisor will be liable if it has retained or assumed the right of general control over the relevant day-to-day operations at its franchised locations . . . and cannot escape liability in such a case merely because it failed or declined to establish a policy with regard to that particular conduct."[36] Rejecting the appeals court's more expansive interpretation of vicarious liability, the California Supreme Court stated that the "imposition and enforcement of a uniform marketing and operational plan cannot automatically saddle the franchisor with responsibility for employees of the franchisee who injure each other on the job."[37] Thus, the court decided against possible franchisor vicarious liability for a franchisee-hired worker's alleged statutory or common law violations. Furthermore, the court concluded that "the mere fact that the franchisor has reserved the right to require or suggest uniform workplace standards intended to protect its brand and the quality of customer service at its franchised locations is not, standing alone, sufficient to impose 'employer' or 'principal' liability."[38]

There are some notable U.S. cases finding franchisor liability based on the franchisor's status either as the franchisees' employer[39] or as the joint employer (with its franchisees) of the franchise's

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standard that considers the franchisor's control or right of control over the instrumentality that is alleged to have caused the harm).

35. Patterson v. Domino's Pizza, LLC, 333 P.3d 723, 725 (Cal. 2014).

36. *Id.* at 743.

37. *Id.* at 726.

38. *Id.* at 739 n.21.

39. *See* Awuah v. Coverall N. Am., Inc., 707 F. Supp. 2d 80, 84–85 (D. Mass. 2010) (finding an employer-employee relationship between a janitorial services franchisor and its franchisees); *see generally* Robert W. Emerson, *Assessing Awuah v. Coverall North America, Inc.: The Franchisee as a Dependent Contractor*, 19 STAN. J.L. BUS. & FIN. 203 (2014) (examining *Awuah*, the franchise business model, franchising disclosure standards and legal requirements, and the limitations of agency and contract law in addressing problems unique to franchising; noting that franchisees are often prone to cognitive errors and psychological biases leaving them ill-equipped to make sound investment decisions, and concluding that franchisees need additional protections, including the right to form associations and enter into collective bargaining agreements with the franchisor).

workers.[40] Still, those holdings are a distinct minority.[41] The best established ground for finding franchisor vicarious liability is the more generalized interpretation of control explained above. While still leading to fewer pro-liability than no-liability decisions, this approach presents the most obvious, direct basis for expanding franchisors' potential vicarious liability.[42] This is because the actual authority on behalf of franchisors arises simply from the franchisor's overall control over the daily operations, nothing more specific.[43]

To compound the confusion generated by the courts' inconsistent approaches to establishing actual agency, there are several generally recognized exceptions to the actual agency requirement, the most prevalent being apparent agency.[44] Through the apparent agency exception, a franchisor may be liable for its franchisee's actions if "apparent" agency can be established, even if the franchisee is not the franchisor's actual agent, and even if the franchisor has not retained significant control over the franchised business.[45]

There are two aspects of franchising that make the apparent agency doctrine especially germane: (1) because franchisors own and operate some of their own retail units and franchise others, the consuming public is often unsure as to which one the principal company owns and operates and which ones it franchises; and (2) the trademark, uniformity, and standardization inherent in the brand name product or service precipitates the belief that the retail unit selling that product or service is operated by the principal company

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40. Browning-Ferris Industries of Cal., 362 N.L.R.B. 186 (2015) (holding that two entities— in effect, the franchisor and franchisee—are joint employers of, say, a franchised unit's employees if a franchisor has reserved authority to control the essential terms and conditions of that employment—setting wages and hours, the number of employees, the scheduling, manner, and type of work, and operating instructions— even if this power of the franchisor is not exercised and the actual control of employment matters is communicated to workers through the franchisee).

41. *See Kerl*, 682 N.W.2d at 331–32 ("[T]he marketing, quality and operational standards commonly found in franchise agreements are insufficient to establish the close supervisory control or right of control necessary to demonstrate the existence of a master/servant relationship for all purposes or as a general matter."); Gray v. McDonald's, USA 874 F.Supp. 2d 743, 750 (W.D. Tenn. 2012) ("[T]he undisputed evidence establishes that McDonald's and [its franchisee] are not so interrelated that they may be considered a single employer or an integrated enterprise.").

42. *See* Rainey v. Langen, 998 A.2d 342, 349 (Me. 2010) (holding, in a case involving Domino's, that "[w]e conclude that the traditional approach strikes an appropriate balance and, for that reason, decline to adopt the instrumentality rule"). *Rainey* is one of the last cases to withstand the shift in emphasis from general to specific operational control.

43. King, *supra* note 18, at 436. This is distinct from *Kerl*, in which the court assumed the franchisor-franchisee relationship is a principal-agent relationship, with the liability question simply being whether the franchisor had sufficient control over the proximate cause of harm to make the franchisor vicariously liable for the franchisee's actions. 682 N.W.2d at 332.

44. King, *supra* note 18, at 438.

45. BEYER, *supra* note 22, at 7–8; RESTATEMENT (SECOND) OF AGENCY §267 (1958).

rather than run as an independently owned and operated franchise.[46] This lack of public knowledge about the relationship between the franchising parties has led courts to deem franchisee use of the franchisor's trade name as grounds for finding apparent authority.[47] As a result of these two realities, the apparent agency doctrine is the theory that poses the greatest risk of vicarious liability for franchisors.[48]

Apparent agency exists if a franchisor, through its action or inaction, induces an innocent third party to reasonably conclude that the franchisee is the franchisor's agent or that the third party is dealing with the franchisor.[49] Thus, the third party must prove three elements to establish apparent agency: (1) a representation by the principal, (2) reliance on the representation by a third person, and (3) a change of position or damage suffered by the third person.[50] Claims of apparent agency can be overcome by adequate notice of independent ownership—that is, notice of the franchisee's separate identity and the independent ownership placed on signage, brochures, business cards, menus, checks, purchase orders, contracts, and advertising.[51] For additional protection, the franchisor can expressly disavow responsibility for employment and other franchisee matters in the

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46. King, *supra* note 18, at 439; *see generally*, Jonathan E. Schulz, *You Can't Have Your Cake and Eat It Too: The Standards for Establishing Apparent Agency*, 60 S.C. L. REV. 999 (2009).

47. Takenari Shimizu, *Japan*, *in* INTERNATIONAL FRANCHISING, *supra* note 12, at JAP/1, JAP/-10 (rejecting the franchisor's argument that it is common knowledge that major car dealers are franchisees and that franchisors are generally separate entities from franchisees). Corporate and franchise law specialist Shimizu refers to a Kobe, Japan district court case (the *Yupos Case*, in the Amagasaki Division) holding a car dealership franchisor vicariously liable to a third party for a franchisee's act. The court in *Yupos* denied the franchisor's argument that the third party knew or should have known it was not dealing with the franchisor since it is common knowledge that car dealers tend to be franchisees and that franchisors are generally separate entities from franchisees. *Id.* at JAP/9. The court considered the franchisee's use of the franchisor's *trade name* to be sufficient for apparent authority even though: (1) the trade name, address or indication of representative status were not depicted on the sales agreement or purchase price receipt; (2) the third party had previously dealt with the franchisee; (3) on business cards, the franchisee's name was larger than the franchisor's trade name; and (4) a released commercial television film mentioned the franchisor's solicitation of prospective franchisees. *Id.* at JAP/10.

48. *See generally*, Schulz, *supra* note 46.

49. BEYER, *supra* note 22, at 8; *see* Allen v. Greenville Hotel Partner, Inc., 409 F. Supp. 2d 672, 680 (D.S.C. 2006) (explaining that "even if there is no actual agency, a party may be liable as the principal for another if that principal holds the other out in a way that reasonably induces reliance on the appearance of an agency relationship").

50. BEYER, *supra* note 22, at 8.

51. *Id.* at 9; Wyatt Maxwell & Jess A. Dance, *NLRB Freshii Memo Offers Lessons to Franchisors on Minimising Employment Liability*, LEXOLOGY (June 16, 2015) http://www.lexology.com/library/detail.aspx?g=c7beeb1a-1ffc-44a6-a767-160f0754bdb3 [https://perma.cc/6X2V-RQKF] (archived Jan. 28, 2017) (referring, *inter alia*, to franchisors' prevention of possible apparent authority by "announc[ing the] independent relationship to [the] general public through conspicuous signage").

franchise agreement or operations handbook and avoid exerting control over personnel policies, such as hiring, scheduling, firing, and disciplining.[52]

As with actual agency decisions, cases involving attempts by plaintiffs to hold franchisors vicariously liable based on apparent agency have produced a whirlwind of confusing outcomes.[53] Since most franchises are regional, and quite often national operations with locations in multiple states, this jurisdictional disarray can result in a franchisor receiving different outcomes for the same behavior solely because of where the franchisee is located. For example, a court in one jurisdiction may find that the franchisor has adequate control over the franchisee in order to establish vicarious liability, while a court in a different jurisdiction may come to the opposite conclusion even though the behavior was based on the same level of control.[54] Such differential treatment demonstrates the need for more understandable and predictable case law.[55] Given the rapid growth in franchising and its central role in the world economy, the lack of clarity, predictability, and analytical integrity in the law governing the vicarious liability of franchisors is unsettling.[56]

III. INTERNATIONAL APPROACHES TO VICARIOUS LIABILITY

Although, on the whole, franchising has increased dramatically throughout the world in recent years,[57] each country that has chosen to regulate franchising through legislation has made its own regulatory mark. Often, a country's approach to regulation stems from the country's civil law or common law heritage.[58] Other nations are heavily influenced by collective agreements.[59] Below is a discussion of the organizations and agreements that have contributed to the creation of international franchise laws, followed by a discussion of how various countries have implemented their own regulations.

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52. Maxwell & Dance, *supra* note 51.

53. King, *supra* note 18, at 439–40 (noting that the outcomes of cases addressing apparent agency are fairly evenly divided and often turn on the issue of reliance); *see* Randall K. Hanson, *The Franchising Dilemma Continues: Update on Franchisor Liability for Wrongful Acts by Local Franchisees*, 20 CAMPBELL L. REV. 91, 100–05 (1997) (discussing several cases with differing rationales on apparent agency).

54. *See generally* King, *supra* note 18, 465 ("The legal principles governing the vicarious liability of franchisors are nothing if not unpredictable and inconsistent.").

55. The inference that a jurisdictional division demonstrates the need for predictable case law may be considered intuitive, but there is support for that proposition in the commentary and cases. *See supra* notes 14–18 and accompanying text.

56. King, *supra* note 18, at 484.

57. *See supra* notes 9–11 and accompanying text.

58. *See infra* notes 296–302 and accompanying text.

59. *See infra* notes 99–112 and accompanying text.

A. *Contributions to Franchise Law: Multinational Approaches*

1. Rome I Regulations and Conflict of Laws

As more businesses began to undertake international contractual obligations, the conflict of laws steadily increased.[60] Initially, the applicable law in the absence of choice was determined by the Rome Convention 1980 (RC).[61] Specifically, Article 4 of the RC determined whose law would apply to settle a disputed franchise contract.[62] Article 4.1 provides that "[t]he contract shall be governed by the law of the country with which it is most closely connected . . . ."[63] Further, Article 4.2 states that "[i]t shall be presumed that the contract is most closely connected with the country where the party who is to effect the performance which is characteristic of the contract has, at the time of conclusion of the contract, his habitual residence . . . ."[64]

Attempting to determine whose law should apply was especially difficult under the RC.[65] While Article 4.1 established that the country with the closest connection should prevail, Article 4.2 also recognized that the law of the party who held the "characteristic performance" should rule.[66] Thus, the question became whether the franchisor or franchisee was the party "who [wa]s to effect the performance which is characteristic of the contract . . . ."[67]

Experts and the case law were divided on this pivotal question.[68] Initially, the franchisor was found to be the party required to effectuate

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60. *See* 10 PAUL VOLKEN & ANDREA BONOMI, YEARBOOK OF PRIVATE INTERNATIONAL LAW 199 (2009).

61. Rome Convention on the Law Applicable to Contractual Obligations, Belg.-Den.-Ger.-Fr.-Ir.-It.-Lux.-Neth.-U.K., Jun. 19, 1980, O.J. C. 027, 34–46 (1998), http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:41998A0126(02):EN:HTML [hereinafter Rome Convention] [https://perma.cc/WN99-M9WJ] (archived Jan. 28, 2017).

62. VOLKEN & BONOMI, *supra* note 60, at 202.

63. Rome Convention, *supra* note 61, at art. 4.1. Artiicle 4.1 does continue with this caveat: "Nevertheless, a separable part of the contract which has a closer connection with another country may by way of exception be governed by the law of that other country." *Id.* This exception is elaborated upon in Article 4.3 of the 2008 European regulation known as Rome I. *Infra* note 87.

64. Rome Convention, *supra* note 61, at art. 4.2.

65. *See* Laura García Gutiérrez, *Franchise Contracts and the Rome I Regulation on the Law Applicable to International Contracts*, *in* 10 YEARBOOK OF PRIVATE INTERNATIONAL LAW, *supra* note 60, at 233, 234.

66. Gutiérrez further notes that "this problem was not confined to franchise contracts, but rather was common to all contracts lacking the exchange-of-goods/services-for-money structure." *Id.*; *see also The Rome Convention: The Contracting Parties' Choice*, 1 SAN DIEGO INT'L L.J. 127, 144 (2000) (discussing the application of the "characteristic performance" test).

67. Case C-133/08, Intercontainer Interfrigo SC (ICF) v. Balkenende Oosthuizen BV, (2009) http://curia.europa.eu/juris/document/document.jsf?docid=77859 &mode=req&pageIndex=1&dir=&occ=first&part=1&text=&doclang=EN&cid=56056 [https://perma.cc/7XRW-ARWQ] (archived on Jan. 29, 2017) (alteration in original).

68. Gutiérrez, *supra* note 65, at 235.

the characteristic performance of the contract.[69] Many argued that it was the franchisor who was required to undertake multiple obligations, who was the true foundation of the contract, and who was required to deal with a large number of complex contractual situations.[70] Under this theory, in the event of a conflict, and in the absence of choice, the law of the franchisor's country would be applied.[71]

Other experts argued, however, that the franchisee was the party required to carry out the characteristic performance of the contract.[72] Essentially, these commentators compared franchise contracts to distribution contracts and noted that, because "several [c]ourt decisions had deemed the obligations of the distributor to be the characteristic performance" under distribution contracts, the franchisee would be the party undertaking the characteristic performance under a franchise contract.[73] In one distribution case, a Swiss court held that, because the party bringing about the characteristic performance would be the distributor, the franchisee is the party that effects the characteristic performance.[74]

Still other experts argued for a more holistic approach.[75] These experts believed that, because it appeared impossible to determine which party effected the characteristic performance of a contract, the "law most closely connected with the contract should be applied on a case-by-case basis."[76] In light of the continuing conflict, a compromise was achieved in the form of a European regulation.[77]

The European Parliament and the Council of the European Union ratified Regulation (EC) No. 593/2008 (Rome I), governing the law

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69. *Id.*

70. *Id.*

71. The notion that the franchisor was the party affecting the characteristic performance also found precedent in Switzerland's Federal Code on Private International Law, which addressed conflicts of law for intellectual property contracts but had an influential effect on the drafting of the Rome Convention. *Id.* at 243 n.7.

72. *Id.* at 235.

73. *Id.* at 235–36 (alteration in original).

74. Rudolph Meroni, *Switzerland*, *in* THE INTERNATIONAL FRANCHISE OPTION 295–96 (Mark Abell ed., 1990) (citing an unreported case); *see also* Gutiérrez, *supra* note 65, at 236 n.9; Bundesgericht [BGer] [Federal Supreme Court] May 15, 1962, 88 ENTSCHEIDUNGEN DES SCHWEIZERISCHEN BUNDESGERICHTS [BGE] II 169, 170 (Switz.); [BGer] Aug. 8, 1962, 88 [BGE] II 325, 328 ; [BGer] Dec. 3, 1962, 88 [BGE] II 471, 474. *But see* [BGer] Feb. 12, 1952, 78 [BGE] II 74, 81. (discussing characteristic obligations in distribution contracts). These cases are all about exclusive distribution relationships and can be found at *Einfache Suche in Bundesgerichtsentscheiden*, BUNDESGERICHT, http://www.bger.ch/index/juridiction/jurisdiction-inherit-template/jurisdiction-recht/jurisdiction-recht-leitentscheide1954.htm (last visited Feb. 11, 2017) [https://perma.cc/H4TC-MGDA] (archived Feb. 11, 2017).

75. Gutiérrez, *supra* note 65, at 236.

76. *Id.*

77. *See* FRANCO FERRARI & STEFAN LEIBLE, ROME I REGULATION: THE LAW APPLICABLE TO CONTRACTUAL OBLIGATIONS IN EUROPE 41 (2009).

applicable to contractual obligations, in June 2008.[78] The purpose of Rome I is to regulate civil and commercial obligations, including franchising, in the event of a conflict of laws.[79] Unlike the RC,[80] Rome I specifically mentions "franchises" on two occasions, first in Recital 17 and again in Article 4.[81]

The significance of Recital 17 is that it classifies franchise contracts—and distribution contracts generally—as "contracts for service."[82] Recital 17 also establishes that these contracts "are the subject of specific rules."[83] This regulation is still unclear, however, and this classification of franchise contracts has remained a point of contention among the many experts seeking to determine (a) which specific rules, under Recital 17, franchises are subject to, and (b) whether the classification is in specific reference to Rome I's later discussion of franchises in Article 4(e).[84]

The second mention of "franchise" within Rome I is in Article 4(e), which specifies the applicable law for franchise contract actions where no applicable law has been chosen by the parties.[85] Article 4 states that, "[t]o the extent that the law applicable to the contract has not been chosen . . . a franchise contract shall be governed by the law of the country where the franchisee has his habitual residence."[86] Thus, in the event of a conflict of laws, the law that the designated court will apply is the law of the country of residence of the principal actor carrying out the contract: the franchisee.[87]

The rationale behind the European Community's (EC) regulation, opting to position the franchisee as the party effecting the

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78. Regulation (EC) No. 593/2008 of the European Parliament and of the Council of 17 June 2008 of the Law Applicable to Contractual Obligations, 2008 O.J. (L 177), 6 [hereinafter Rome I]. Rome I replaced the Rome Convention, which established uniform rules for determining the law applicable to contractual obligations in the European Union (EU). Rome I went into effect on December 17, 2009. *See id.* at art. 29.

79. *See id.* at art. 1.

80. *See generally* Rome Convention, *supra* note 61.

81. *See* Rome I, *supra* note 78, at rec. (17), art. 4.1(e).

82. *See id.*

83. Gutiérrez notes that the definition of a franchise contract as a service contract is not necessarily accurate. However, such a definition appears appropriate in light of the skirmish that ensued under the Rome Convention. *See* Gutiérrez, *supra* note 65, at 237 (noting that defining a franchise contract as a service contract comports with answering the question, "specifically, where would the service be provided in a franchise contract?").

84. This classification of franchise contracts is highly controversial, as it would affect not only provisions on applicable law, but also those on international jurisdiction. *See id.* at 236.

85. *See* Rome I, *supra* note 78, at art. 4.1(e).

86. *Id.* at art. 4.1–.1(a).

87. *See id.* at art. 4.. However, Article 4.3 also notes "where it is clear from all the circumstances of the case that the contract is manifestly more closely connected with a country other than that indicated... the law of that other country shall apply." *Id.* at art. 4. Thus, Article 4.1(e) would give way to Article 4.3 if necessary. *See id.* at art. 4.3.

characteristic performance of the contract, is twofold.[88] First, the franchisee has commonly been viewed as the weaker party to the contract,[89] and, therefore, in need of greater protection.[90] And second, by allowing the laws of the franchisee's habitual residence to govern the contract in the absence of choice of law, the law "[takes] into account the legal order of the State where the franchise is operated as the market affected by the contract."[91] In combining these two goals, the EC has increased the predictability of the law applicable to franchise contracts.[92]

Despite the contentiousness of Article 4(e)'s definition of franchisee as the party effecting the characteristic performance, the inquiry for determining which party effects that performance is well settled.[93] Many commentators prefer the RC's finding that the characteristic performance is effected by the franchisor.[94] Still, regardless of whether the franchisor or franchisee is the party who effects the characteristic performance, commentators agree that answering this question depends on the level of integration of the franchisee's business into the franchisor's business, and Rome I recognizes that the franchisee's freedom from or dependency on the franchisor can vary substantially.[95] As discussed later, while not

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88. *See* Gutiérrez, *supra* note 65. These are the opinions of Gutiérrez and not the official rationale given expressly by the EC.

89. The proposal itself implicitly states that franchisees are the weaker party and thus are deserving of protection under the regulation. *Commission Proposal for a Regulation of the European Parliament and the Council on the law applicable to contractual obligations (Rome I)*, 11 ¶ 9 COM (2005) 650 Final (Dec. 15, 2005), http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2005:0650:FIN:EN:PDF (last visited Aug. 25, 2016) [https://perma.cc/M4WU-SAFA] (archived Jan. 22, 2017) [hereinafter *Proposal for Rome I*] ("As regards contracts concluded with parties regarded as being weaker, those parties should be protected by conflict rules that are more favourable to their interests than the general rules.").

90. Gutiérrez, *supra* note 65, at 238.

91. *Id.* (alteration in original) (internal quotations removed) (discussing *Proposal for Rome I*, *supra* note 89).

92. VOLKEN & BONOMI, *supra* note 60 (noting that the determination of the party required to effect the characteristic performance and the identification of a characteristic performance in franchise contracts is exceedingly uncertain and controversial).

93. Gutiérrez *supra* note 65, at 243.

94. Such commentators include Professor Gutiérrez, who notes that this is because the franchisor is the party responsible "for the most complex obligations." *See id.* at 243.

95. FERRARI & LIEBLE, *supra* note 77, at 41. However, this is the settled answer to the conflict of law question in the EC, and it should be noted that countries such as China and Australia have different resolutions to conflict of law questions. In China, courts and judges alike are unsure of whether national or local regulations should apply to resolve conflict of law questions. *See* Michele Lee, *Franchising In China: Legal Challenges When First Entering The Chinese Market*, 19 AM. U. INT'L L. REV. 949, 984 (2004). Ultimately, it is crucial to note that "in the absence of franchise-specific legislation, the relationship between the franchisee and franchisor is governed [exclusively] by the [explicit] terms of the franchise agreement and the law of contract." Tamara Milenkovic Kerkovic, *The Main Directions in Comparative Franchising Regulation – Unidroit Initiative and its Influence*, 13 EUR. RES. STUD. J. 110 (2010).

nearly as transparent as the European regulation, it seems that both China and Australia have taken this approach.[96]

Ultimately, while Rome I was initially heralded as the opportunity to convert the 1980 Rome Convention into a European Community instrument by transforming and modernizing its provisions, commentators remain disappointed in the end result.[97] The rules of Rome I work well in the case of consumers and employees, but they disappoint in regard to presumptively weak parties, such as franchisees, due to their lack of bargaining power and generally lower amount of financial freedom.[98] Even so, commentators agree that it is preferable to have rules insulating weaker parties in most cases, even if those rules do not work well, rather than not having any such rules.[99]

2. UNIDROIT's Contribution to International Franchise Law and Vicarious Liability Concepts

The International Institute for the Unification of Private Law (UNIDROIT) is an independent intergovernmental organization of sixty-three Member States and was instituted to "study needs and methods for modernizing, harmonizing and coordinating private and, in particular, commercial law as between States and groups of States."[100] The principles set forth by UNIDROIT essentially serve as nonbinding general principles and rules and are largely conditional on the states' willingness to adopt them.[101] The Preamble to the UNIDROIT principles stipulates that the principles "shall be applied when the parties have agreed that their contract be governed by them."[102]

UNIDROIT was first founded as part of the League of Nations in 1926.[103] Following the collapse of the League, UNIDROIT was reestablished in 1940.[104] It was not until 1985, however, that uniform

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96. Interview with Andrew Terry, Professor of Business Regulation, Univ. of Sydney Bus. Sch. (May 15, 2015) (on file with author).

97. *See, e.g.*, Francisco J. Garcinmartín Alférez, *The Rome I Regulation: Much ado about nothing?* 2008 EUR. LEGAL F. 1 (2008).

98. CONVERGENCE AND DIVERGENCE IN PRIVATE INTERNATIONAL LAW 549 (K. Boele-Woelki et al. eds., 2010).

99. *See id.* at 549–50.

100. *See History and Overview*, INT'L INST. FOR THE UNIFICATION OF PRIV. L. (2009), http://www.unidroit.org/about-unidroit/overview [hereinafter UNIDROIT] [https://perma.cc/LE44-JKVR] (archived Jan. 23, 2017).

101. *Id.*

102. UNIDROIT, UNIDROIT PRINCIPLES OF INTERNATIONAL COMMERCIAL CONTRACTS (2010), http://www.unidroit.org/english/principles/contracts/principles2010/integralversionprinciples2010-e.pdf [https://perma.cc/2NKS-XXNW] (archived Jan. 29, 2017).

103. *See* UNIDROIT, *supra* note 100.

104. *Id.*

rules for franchising were proposed.[105] At this time, franchising was not a common concept in Europe, and North America was one of the only locales that had adopted the franchising concept.[106] Initially, franchisors' representatives opposed the ratification of any uniform international franchise regulations,[107] thus, no rules were adopted at the time, but UNIDROIT continued to monitor the international franchise situation.[108]

By 1993, however, interest in international franchising had grown tremendously,[109] and the Governing Council of UNIDROIT established the Study Group on Franchising, which ultimately produced two documents: the *Model Franchise Disclosure Law*, submitted to the Governing Council on September 25, 2002,[110] and the *Guide to International Master Franchise Arrangements*,[111] initially published in February 1998 and republished in 2007.[112] These documents demonstrated a pro-commerce, pro-franchising orientation.[113] Indeed, much of U.S.-franchisor expansion overseas is accomplished through a special, robust business format: master franchising.[114] In the master

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105. *See* MAN. LAW REFORM COMM'N, *supra* note 7, at 237. In fact, it was a Canadian member of the Governing Council who proposed to the organization there should be a uniform set of rules to govern franchise contracts. *Id.*

106. *See id.*

107. *See id.*

108. *See id.*

109. This new interest "was largely due to the increased attention devoted to franchising by legislators and the consequent proliferation of franchise laws, not all of which had, in the view of the members of the Study Group, given sufficient consideration to the specific nature and characteristic of franchising, thereby unintentionally putting the future development of franchising in the country concerned at risk." *Id.* (quoting UNIDROIT, MODEL FRANCHISE DISCLOSURE LAW (2002), http://www.unidroit.org/english/modellaws/2002franchise/2002modellaw-e.pdf (last visited Aug. 26, 2016) [hereinafter UNIDROIT Model Franchise Disclosure Law (2002)] [https://perma.cc/DZ9V-S9FA] (archived Jan. 23, 2017).

110. *See* UNIDROIT, *supra* note 100, at Achievements.

111. UNIDROIT, GUIDE TO INTERNATIONAL MASTER FRANCHISE ARRANGEMENTS (1998).

112. UNIDROIT, GUIDE TO INTERNATIONAL MASTER FRANCHISE ARRANGEMENTS (2d ed. 2007), http://www.unidroit.org/english/guides/2007franchising/franchising2007-guide-2nd-e.pdf (last visited Aug. 26, 2016) [hereinafter Master Franchise Guide (2007)] [https://perma.cc/29LZ-2DRN] (archived Jan. 20, 2017).

113. UNIDROIT notes, "[t]he Model Law is intended to encourage the development of franchising as a vehicle for conducting business. As a pro-commerce document, it recognizes that franchising offers the potential of increased economic development, especially among countries seeking access to know-how." UNIDROIT Model Franchise Disclosure Law (2002), *supra* note 109, at 10. The franchisor's development of and continuing provision of *savoir faire* (know-how) throughout the life of the franchise is a fundamental element of franchising in practice worldwide, and it is a legal requirement in most countries, especially civil law jurisdictions. Robert W. Emerson, *Franchise Savoir Faire*, 90 TUL. L. REV. 589, 589 (2016).

114. PETER D. HOLT & AMIR KREMAR, THE BASICS OF INTERNATIONAL MASTER FRANCHISING, http://www.franchise.org/sites/default/files/ek-pdfs/html_page/Sun-Intl-Summit-Track-1-Basics-Intl-Master-Fran_0.pdf (last visited Jan. 20, 2017) [https://

franchise model, the franchisor grants the master franchisee (also called a sub-franchisor) the right to franchise to individual unit franchisees.[115] In effect, the franchisor has no local employees because there is no direct relationship between the franchisor and the individual unit franchisees that contracted with the sub-franchisor. For example, the franchisor may grant twenty restaurant franchises to the sub-franchisor, who will then in turn contract those twenty restaurants out to unit franchisees. Under this model, the franchisor provides the business model and training to the sub-franchisor, who then provides the capital and human resources to grow the franchises.[116]

Because the franchisor does not have a direct relationship with the individual unit franchisees, the franchisor ordinarily will not be vicariously liable for any claims against the unit franchisee, the sub-franchisor, or the sub-franchisee.[117] While not being liable for claims is an advantage of this hands-off approach, there are disadvantages, including the fact that the franchisor does not have as much control over its franchised units as it would in a normal franchise relationship.[118] In master-franchise arrangements there are essentially two agreements made: an international agreement between the franchisor and the sub-franchisor (the master franchise agreement), and a domestic franchise agreement between the sub-franchisor and the sub-franchisee (the sub-franchise agreement).[119]

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perma.cc/PY2M-8ARE] (archived Jan. 20, 2017) (80 percent of international expansion being through master franchises, with the number of franchisors thus using master franchises internationally having doubled from 2001 to 2006).

115. *Id.*; Marisa D. Faunce & Christina M. Noyes, *Agreement and Issues Related to the Franchise Sales Process*, *in* COLLATERAL ISSUES IN FRANCHISING: BEYOND REGISTRATION AND DISCLOSURE 43, 69–70 (Kenneth R. Costello ed., 2014).

116. Lee Plave, *Deciding to Go International: Organizational and Business Considerations*, *in* FUNDAMENTALS OF INTERNATIONAL FRANCHISING, 1, 16 (Will K. Woods ed., 2d ed., 2013).

117. Carl E. Zwisler, *Selecting a Format for International Franchising*, *in* INTERNATIONAL FRANCHISING: A PRACTITIONER'S GUIDE 27, 42 (Marco Hero ed., 2010) ("As master franchisees act as the franchisor in their territories, franchisors [who grant the master franchises] avoid many of the costs and legal and financial risks that they would face in a territory if they were to grant franchises directly to unit franchisees.").

118. Susan Grueneberg, *Inbound Transactions: Introducing a Non-U.S. Franchise Program to the United States*, *in* FUNDAMENTALS OF INTERNATIONAL FRANCHISING, *supra* note 116, at 329, 338. (noting that master franchise programs permit more rapid market development, but "also results in less control over that development by the franchisor"); Plave, *supra* note 116, at 19 ("One of the greatest disadvantages of implementing a master franchise system is that the franchisor must cede a significant amount of system control for the target market to the master franchisee.").

119. Master Franchise Guide (2007), *supra* note 112, at 2. Usually, there is no direct relationship between the franchisor and sub-franchisee—the sub-franchisor assumes the right to license the sub-franchisees as the franchisor in the territory and retains the duties of a franchisor to the sub-franchisees. *Id.*at 3. Moreover, "[t]he franchise relationship will almost always involve the franchisor imposing a system and method of operation accompanied by controls." *Id.* at 171; *see, e.g.*, Greil v. Travelodge

The 2002 *Model Franchise Disclosure Law*[120] specifically addresses the disclosures a franchisor must make to a prospective franchisee.[121] It requires the franchisor to give these potential franchisees detailed information on various qualities of the potential franchisor.[122] The disclosure document must be presented to prospective franchisees at least fourteen days before the signing of any agreement or the payment of a non-refundable deposit.[123] Disclosure issues initially considered by the Study Group included "whether the franchisee has a statutory right to renew the agreement and whether the franchisee has a right to cure when he/she breaches the contract."[124] The Study Group, however, chose not to address the relationship of the parties because prior experience had revealed that relationship legislation had not yet proven effective.[125] The Study

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Int'l., Inc., 541 N.E.2d 1288 (Ill. App. Ct. 1989) (quoting Nichols v. Arthur Murray, Inc., 56 Cal. Rptr. 728 (Cal. Ct. App. 1967)).

120. *See* UNIDROIT Model Franchise Disclosure Law (2002), *supra* note 109, at 3–4 (The *Model Franchise Disclosure Law* contains ten articles in addition to a preamble. Article 1—deals with the scope of application of the law; Article 2—definitions; Article 3—delivery of the disclosure document; Article 4—the format of the disclosure document; Article 5—exemptions from the obligation to disclose; Article 6—information which must be disclosed; Article 7—acknowledgement of receipt of the disclosure document; Article 8—remedies; Article 9—the temporal scope of application of law; and Article 10—waivers). The franchisee cannot waive her rights under this law—such attempts are void. Man. Law Reform Comm'n, *supra* note 7, at 238; UNIDROIT Model Franchise Disclosure Law (2002), *supra* note 109, at 9.

121. "[T]he Model Law ensures that the prospective franchisees who intend to invest in franchising receive material information about franchise offerings, thus permitting them to make an informed investment decision. In addition, the Model Law brings security to franchisors in their relationships with franchisees, administrative authorities and courts." UNIDROIT Model Franchise Disclosure Law (2002), *supra* note 109, at 10.

122. The Model Franchise Disclosure Law sets out a list of information that the franchisor must include in the disclosure statement, including the franchisor's legal name, form and address, the franchisor's principal place of business (the address), and "the trademark, trade name, business name or similar name, under which the franchisor carries on or intends to carry on business in the State in which the prospective franchisee will operate the franchise business." *See id.* at 5–8 (for an exhaustive list of disclosure requirements); *see also id.* at 4 (for potential disclosure exemptions).

123. MAN. LAW REFORM COMM'N, *supra* note 7, at 238; *see also* UNIDROIT Model Franchise Disclosure Law (2002), *supra* note 109, at 3–4. The franchisor may deliver the disclosure statement to the franchisee in any format, so long as it is provided in writing. *Id.* at 4. The 14-day requirement does not apply to confidentiality agreements or security deposits for confidentiality agreements. *Id.* at 3–4.

124. MAN. LAW REFORM COMM'N, *supra* note 7, at 237 (quoting UNIDROIT Model Franchise Disclosure Law (2002), *supra* note 109, at 14).

125. *See* MAN. LAW REFORM COMM'N, *supra* note 7, at 237–38. Even if there is relationship legislation, the franchise contract tends to predominate. There is an optimistic view of the alternative to legislation (of doing nothing, hence shutting down franchise relationship law proposals). It emphasizes that franchisors and franchisees ought to have the freedom to make their own contract. Even though the parties (principally, the franchisee) may well make mistakes harming their own interests, in the long run the process of reaching and revamping agreements optimizes outcomes. A large measure of contract freedom persists even with substantive franchise laws. Instead,

Group reasoned that, while it could reach an agreement on disclosure provisions, "it was far more problematic to devise common norms for relationship issues in view of the great variety of relationships that existed within the context of franchising."[126] Thus, the *Model Franchise Disclosure Law* only addresses disclosure issues and excludes the relationship of the parties at the international level.[127]

UNIDROIT's *Guide to International Master Franchise Arrangements* (Guide)[128] focuses on the structuring of franchise agreements, including the negotiations, the drafting, and the legal effects of an agreement on the parties. Similarly to the *Model Franchise Disclosure Law,* the Guide was a product of the Study Group on Franchising organized by the Governing Council of UNIDROIT in 1993.[129] For the purposes of this Article, Chapter 14, "Vicarious Liability, Indemnification and Insurance," is the most significant.

Chapter 14 of the Guide mirrors the Restatement (Third) of Agency ("Third Restatement") when defining the potential liability of

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franchise relationship laws simply establish some boundaries, but the contract fills all within those boundaries. The main problem is that would-be franchisees, frequently proceeding without counsel (Robert W. Emerson, *Fortune Favors the Franchisor: Survey and Analysis of the Franchisee's Decision Whether to Hire Counsel*, 51 SAN DIEGO L. REV. 709 (2014)), fail even to consider their situation.

> Franchisees ignore disclosure documents, do not compare various franchise opportunities, and refrain from consulting with a specialized franchise attorney. Given this reality, theoreticians and legislators interested in creating franchise laws that protect novice franchisees from possible opportunism by franchisors must cast doubt on the assumption that franchisees are sophisticated, well-informed business people and incorporate into their analyses a more representative conception of franchisee behavior. The assumption that franchisees consider all relevant information before signing a franchise contract has little theoretical or empirical support in actual practice, and thus the door is open to reconsidering the adoption of franchise relationship laws.

Robert W. Emerson & Uri Benoliel, *Are Franchisees Well-Informed? Revisiting Debate Over Franchise Relationship Laws*," 76 ALB. L. REV. 193, 215–16 (2013).

126. *See* MAN. LAW REFORM COMM'N, *supra* note 7, at 238 (quoting UNIDROIT Model Franchise Disclosure Law (2002), *supra* note 109, at 14).

127. If the franchisor fails to deliver the disclosure statement within the allotted 14-day period, or if the statement contains a misrepresentation or omission of material fact, the franchisee reserves the right to terminate the franchise agreement and/or claim damages. MAN. LAW REFORM COMM'N, *supra* note 7, at 238; *see also* UNIDROIT Model Franchise Disclosure Law (2002), *supra* note 109, at 8. However, the franchisee may not lawfully terminate the franchise agreement if the franchisee, "[obtained] the information through other means, did not rely on the misrepresentation, or termination is a disproportionate remedy in the circumstances." MAN. LAW REFORM COMM'N, *supra* note 7, at 238; *see also* UNIDROIT Model Franchise Disclosure Law (2002), *supra* note 109, at 8.

128. *See supra* notes 110, 111.

129. *See supra* notes 99–111 and accompanying text.

franchisors.[130] Similarly to the Third Restatement,[131] the Guide establishes that, "in the absence of a legal relationship on which such a claim may be based, for example an allegation that an agency relationship exists, the franchisor is not vicariously liable for the sub-franchisor's, or indeed the sub-franchisees', defaults."[132] Thus, both the Third Restatement and the Guide require the establishment of an agency relationship in order for the franchisor to be vicariously liable for the franchisees' torts.[133]

Whether an agency relationship exists, according to the Guide, is determined by the amount of control the principal (the franchisor) retains over the agent (the franchisee).[134] Accordingly, "[f]or an agency relationship to give rise to a claim, it must be based on the right of the principal (in this case, the franchisor) to control the day-to-day operations of the business of the agent (the sub-franchisor or sub-franchisee)."[135] Moreover, "[i]n an agency relationship, the right to control will extend not only to the day-to-day business, but also to the result of the work and the manner in which the work is accomplished."[136]

A franchisor could also be liable for the torts of its franchisee under a theory of apparent agency.[137] In accordance with the Guide, "by using the franchisor's name, the sub-franchisor or sub-franchisee are held out to the public as agents of, or indeed as being, the franchisor and that they therefore have ostensible authority to commit the franchisor and to make the franchisor liable for their defaults."[138] This description of apparent agency mirrors Section 7.08 of the Third Restatement.[139]

The Guide suggests several techniques that franchisors may implement to avoid being held vicariously liable for the actions of a franchisee. In order for the franchisor to escape vicarious liability, the Guide recommends that the franchisor or sub-franchisor argue that the franchisee did not follow instructions and did not perform in

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130. *Compare* Master Franchise Guide (2007), *supra* note 112, at 170, *with* RESTATEMENT (THIRD) OF AGENCY § 7.07 (2006).

131. *See* RESTATEMENT (THIRD) OF AGENCY § 7.07 (2006) ("An employer is subject to vicarious liability for a tort committed by its employee acting within the scope of employment.").

132. Master Franchise Guide (2007), *supra* note 112, at 170.

133. RESTATEMENT (THIRD) OF AGENCY § 7.07 (2006); Master Franchise Guide (2007), *supra* note 112, at 170.

134. Master Franchise Guide (2007), *supra* note 112, at 170.

135. *Id.*

136. *Id.*

137. BEYER, *supra* note 22, at 5.

138. Master Franchise Guide (2007), *supra* note 112, at 171.

139. *See* RESTATEMENT (THIRD) OF AGENCY § 7.08 (2006) ("A principal is subject to vicarious liability for a tort committed by an agent in dealing or communicating with a third party on or purportedly on behalf of the principal when actions taken by the agent with apparent authority constitute the tort or enable the agent to conceal its commission.").

accordance with the franchisor's or the sub-franchisor's requirements.[140] In such instances, "the extent and conduct of the franchisor's or sub-franchisor's method of regulating and monitoring the sub-franchisee's business would be examined by the court, with a view to determining whether the franchisor or sub-franchisor could escape liability on the grounds that the sub-franchisee had failed to observe the requirements."[141] Above all, the Guide suggests that franchisors avoid controlling the daily operations of the franchisee.[142]

The Guide not only discusses how a franchisor can avoid liability but also discusses when a franchisor should indemnify a franchisee and assume sole responsibility for a tort. [143] The Guide comments that

> it is natural for the franchisor to assume sole and entire responsibility for any loss, damage, cost or expense (including court costs and reasonable legal fees) that arise out of any claim, action, administrative inquiry or other investigation that relates to its own operation of the business, independently of the reason for which it was made.[144]

Examples of when the franchisor should assume indemnification responsibility include product liability claims and actions for infringement of intellectual property rights.[145] The Guide notes that such indemnification assumptions by the franchisor should be documented within the franchise agreement.[146] According to the Guide, other such contractual assumptions or waivers consist of

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140. *See* Master Franchise Guide (2007), *supra* note 112, at 171 (noting that a franchise relationship is normally governed by a method of operation which includes a system and controls).

141. *Id.* In making this determination, the *Guide* notes, "the court would also need to determine whether the franchisor or sub-franchisor had acted reasonably in the enforcement or non-enforcement of the requirements." *Id.* at 172. Consequently, this could place stress on the franchise relationship in light of the fact that the franchisee might believe that he had been subjected to over-regulation. While at the same time, the franchisor may find that in order to appease the court, he is required to enforce such strict legal enforcement measures in order to compel the franchisee to comply. *Id.*

142. *Id.* It should be noted, however, that some commentators believe encouraging principals not to assert control over agents, in order to avoid liability, poses a risk to society because principals will not ensure that their agents are using due care or taking effective precautions to prevent harm to third parties. *See generally* Jennifer Arlen & W. Bentley MacLeod, *Beyond Master-Servant: A Critique of Vicarious Liability*, *in* EXPLORING TORT LAW 23 (Stuart Madden ed., 2005).

143. In U.S. franchise agreements, it is rare for a franchise contract to not have a "hold harmless" provision with the franchisee indemnifying the franchisor for some harms. Emerson, *supra* note 29, at 690 (a survey of 100 U.S. franchise agreements in 2013 found 96 percent had such a provision, up from 89 percent in a comparable 1993 survey).

144. Master Franchise Guide (2007), *supra* note 112, at 173.

145. *See id.* These types of liabilities can be protected against by the franchisor's purchase of an insurance coverage policy. Susan Vincent & G. Thomas MacIntosh II, *Insuring Against Franchisor Vicarious Liability*, *in* INTERNATIONAL FRANCHISE ASSOCIATION 34TH ANNUAL LEGAL SYMPOSIUM (2001).

146. Master Franchise Guide (2007), *supra* note 112, at 173.

> rules, specifying when the franchisor or sub-franchisor is entitled, or under what circumstances either of them is obligated, to undertake or assume the defence of any liability claim, action, inquiry or investigation, at whose risk and expense such a defence should be undertaken and the conditions under which a settlement might be made.[147]

The country of the party in which the action takes place is likely to assume the primary defense,[148] but the franchisor is generally "entitled to choose whether or not it should itself assume the defense against the third party's claim, always provided that this is permitted by the procedural laws of the host country."[149] If the franchisor's intellectual property rights are at issue, the situation differs from one country to the next.[150] In some jurisdictions, it is the franchisor, or the owner, who has the right to assume the primary defense;[151] however, in other jurisdictions, it is the franchisee, or the exclusive licensee, who has the right to assume the primary defense.[152] Moreover, the Guide suggests that the master franchise agreement should include "wording prohibiting the sub-franchisor from making any representations, or giving any warranties, with regard to any product that it has obtained from the franchisor which go beyond the representations or warranties given by the franchisor and/or beyond the standards usual in the host country."[153]

The Guide also recommends that franchisors obtain, and require their franchisees to possess, liability insurance.[154] It points out that, in North America, Europe, and Australia, most franchise agreements require sub-franchisors to take out liability insurance against third-party claims, as well as against property risks.[155] Further, the franchisee is usually also required to have liability insurance to guard against other potential risks.[156] A clause requiring the sub-franchisor

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147. *Id.* at 174.

148. If the party hosting the action chooses the primary defense he is expected to provide the other party or parties with full information on the progress of the proceedings. Nonetheless, the primary defense may always be chosen by the party who is ultimately facing liability. *Id.*

149. *Id.*

150. *Id.*; *see* Robert W. Emerson & Catherine R. Willis, *International Franchise Trademark Registration: Legal Regimes, Costs and Consequences*, 52 WAKE FOREST L. REV. (forthcoming 2017), for analysis of varying trademark registration rights and duties, including the law and data related to trademark applications accepted or rejected in nations such as Australia, Japan, Mexico, Russia, and South Korea.

151. Master Franchise Guide (2007), *supra* note 112, at 174.

152. *Id.*

153. *Id.* at 175.

154. *See* Vincent & MacIntosh, *supra* note 145, at 10.

155. *See* Master Franchise Guide (2007), *supra* note 112, at 175 (noting that these contractual clauses may only provide for a sub-franchisor's general obligation to take out an "appropriate" insurance policy).

156. *Id.*; Emerson, *supra* note 29, at 690 (a survey of 100 U.S. franchise agreements in 2013 found 97 percent had a provision expressly requiring the franchisee to pay for comprehensive liability insurance); *see also* Perkins et al., *supra* note 21, at 176 (providing a sample insurance clause including property insurance, business

or franchisee to obtain insurance should be included within the master franchise agreement.[157] Accordingly, it is suggested that the franchisor and sub-franchisor "discuss the liability risks that exist in the host country, not only under statutory law but also under case law, as well as what insurance coverage is available or usually taken out in that country."[158] The Guide advises this because there are some countries where taking out an insurance policy against third-party liability is unusual, expensive, or simply unavailable.[159] Thus, discussing such potential battles beforehand will help avoid an increased risk of, and the costs associated with, a potential lawsuit.[160]

Typically, the insurance clause would be included in the master franchise agreement and should "prescribe that the sub-franchisor shall at its own expense take out and maintain full insurance cover [sic] in all cases for which it is required by law, or for which it is otherwise necessary or at least useful in order to ensure the continued existence of the sub-franchisor."[161] The Guide further suggests that the franchisor "fix minimum coverage for damage to property and for damages caused by the interruption of business, as well as for third party liability risks for personal injury, death, damages to property and product liability."[162] The minimum amount of coverage the franchisor requires the sub-franchisor or franchisee to maintain should be periodically reviewed to ensure that it is in accordance with the host state's policies.[163] If needed, it should be adjusted to reflect the minimum amount of insurance coverage required by the host state.[164]

The franchisor should also require insurance coverage that encompasses both the franchisor generally and "its directors, officers, shareholders, partners or other licensees whenever the interests of

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interruption insurance, general liability insurance, automobile insurance, and worker's compensation).

157. *See* Master Franchise Guide (2007), *supra* note 112, at 175 (further commenting, "[s]uch contractual clauses may at times only provide for general obligation to 'take out an appropriate insurance policy,' leaving it to the sub-franchisor or sub-franchisee to decide what it considers to be 'appropriate,' but often the cover needed will be specified").

158. *Id.*

159. *Id.* at 176.

160. *See* Daniel Allen & Mindy Haverson, Note, *An Alternative Approach to Vicarious Liability for International Accounting Firm Networks*, 15 STAN. J.L. BUS. & FIN. 426, 446 (2010) (citing King, *supra* note 18, arguing that franchisors who require franchisees to carry liability insurance can limit risk when aggrieved parties would otherwise attempt to hold the franchisor vicariously liable).

161. Master Franchise Guide (2007), *supra* note 112, at 176.

162. *Id.*

163. *See id.* (discussing insurance coverage meeting "the risks and practice prevailing in the host country").

164. *Id.* A 2013 survey of 100 fast food, restaurant, and ice cream parlor franchise agreements found that the median level of coverage for comprehensive liability insurance found that 97 percent compelled the franchisee to pay for the insurance, with the median level of required insurance coverage for all the agreements being $2 million. Emerson, *supra* note 29, at 690.

these persons may be affected by the risks covered by the insurance policies."[165] A host country must allow such an extension of insurance coverage,[166] but, even if such an extension is permitted, it may not be worth the extensive costs required to do so.[167] If a host country does not permit an extension of the insurance policy, such an extension will be very costly for the franchisor. The Guide suggests, "it might be more appropriate for the franchisor to extend its own insurance coverage to possible risks stemming from third parties and to recover additional insurance premium through the franchise fee."[168] While stressing the importance of insurance coverage, the Guide maintains that this is only one of many factors in establishing a "healthy commercial law environment," which is of paramount importance for franchising.[169]

In addition to these organizational considerations, the Guide goes on to discuss other important issues pertaining to international franchising. In particular, international legislation and rules relevant to franchising are discussed in Annex Three of the Guide.[170] Annex Three notes that franchise regulations are essentially divided into two categories.[171] The first includes laws that apply to contracts in general, and the second includes laws that apply specifically to franchise regulation.[172] Laws that are franchise-specific encompass "agency law and the law regulating other distribution contracts."[173] The Guide explains that "[t]here may be aspects of the relationship between a franchisor and its franchisees that are covered by agency law, independently of whether the courts actually assimilate the franchise relationship concerned to one of agency, or by the law regulating other distribution contracts."[174] Therefore, the Guide advises that legislation

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165. Master Franchise Guide (2007), *supra* note 112, at 176–77.

166. *Id.* at 177; *see* Luisa Soares de Silva et al., *Civil Liability Inurance. Contracts for Directors Under Portuguese Company Code*, EMERGING ISSUES ANALYSIS 3099 (2008) (explaining that despite the prevalence of Director's and Officer's Insurance in the United States and United Kingdom, it is a relatively new and developing concept throughout Continental Europe and Asia).

167. UNIDROIT Master Franchise Guide (2007), *supra* note 112, at 177.

168. *Id.*

169. *Id.* at 276; *see also* Allen & Haverson, *supra* note 160, at 447 (asserting that insurance "does not provide sufficiently strong incentives to individual member firms and that it does not do enough to deter member firm misconduct").

170. *See* Master Franchise Guide (2007), *supra* note 112, at 276 (noting these laws and regulations are in addition to those regulating commercial contracts or intellectual property rights).

171. *Id.*

172. *Id.*

173. *Id.* Other areas of law that are discussed include: general contract law, leasing and security interests, financial investments, intellectual property, competition law, fair trade practices law, corporate law, taxation, property law, legislation on consumer protection and product liability, insurance law, labor law, the law regulating the transfer of technology, legislation regulating foreign investments currency control regulations and import restrictions and/or quotas, legislation regulating joint ventures, and industry specific laws or regulations. *See generally id.* at 276–81.

174. *Id.* at 276–77.

that regulates agency relationships and distribution contracts be considered when analyzing a franchise relationship.[175]

Annex Three also discusses a nation's implementation, or lack thereof, of franchise-specific legislation.[176] The Guide notes that, while an increasing number of nations have implemented franchise-specific legislation, "still only a limited number regulate franchising."[177] Moreover, implementation of franchise-specific legislation in those nations is generally limited to domestic rather than international franchise regulations.[178] This lack of international franchise regulation is due in large part to "the complexity of the relationship and to the great number of areas of law involved in a franchise relationship."[179]

When nations adopt franchise-specific legislation, the regulations usually concern disclosure rules rather than governance of the relationship between the parties.[180] Annex Three explains that, while the degree and detail of the information required to be disclosed varies from nation to nation, generally "the laws will require the franchisor to provide the prospective franchisee with information on a number of points that will enable the franchisee to make an informed decision on

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175. *Id.* at 277. Comparable statements about distribution or agency law affecting franchise laws have been made about the law in numerous countries, with four examples being Spain, Austria, Italy, and Germany. Ignacio Alonso, *Spain*, *in* GETTING THE DEAL THROUGH – DISTRIBUTION & AGENCY IN 17 JURISDICTIONS WORLDWIDE 90, 94 (Andre R. Jaglom ed., 2015); Gustav Breiter, *Austria*, *in* GETTING THE DEAL THROUGH – DISTRIBUTION & AGENCY IN 17 JURISDICTIONS WORLDWIDE, *supra* note 175, at 5, 6; Marco De Leo, *Italy*, *in* GETTING THE DEAL THROUGH – DISTRIBUTION & AGENCY IN 17 JURISDICTIONS WORLDWIDE, *supra* note 175, at 71, 71–72; Martin Rothermel & Benedikt Rohrssen, *Germany*, *in* GETTING THE DEAL THROUGH – DISTRIBUTION & AGENCY IN 17 JURISDICTIONS WORLDWIDE, *supra* note 175, at 59, 60, 63; *see also* ANDRE R. JAGLOM, DISTRIBUTION CONTRACTS (2014), http://www.thsh.com/Publications/Other-Publications/Distribution-Contracts.aspx#.V0X2JvkrKUl [https://perma.cc/XD6S-3889] (archived Jan. 30, 2017) (discussing the same concepts—distribution and agency law impacting franchise law—with respect to U.S. law). The reverse can also apply: franchise legislation reaching distributorships. *See* ANDRE R. JAGLOM, THE BROAD SCOPE OF FRANCHISE LAWS: TRAPS FOR THE DISTRIBUTION CONTRACT DRAFTER (2014), http://www.thsh.com/documents/The-Broad-Scope-of-Franchise-Laws-2014.pdf [https://perma.cc/RDD2-U3PW] (archived Jan. 28, 2017) (discussing how broadly worded state franchise legislation in the United States often affects distribution contracts).

176. *See* Master Franchise Guide (2007), *supra* note 112, at 281; *compare* Rose M. Faria, *France Serves as a Gateway to Europe*, INT'L FRANCHISE ASS'N, http://www.franchise.org/franchise-news-detail.aspx?id=33190 (last visited Jan. 28, 2017) [https://perma.cc/ZN98-JSNH] (archived Jan. 23, 2017) (discussing France's long history of franchise-specific legislation) *with* Bryan Schwartz & Leandro Zylberman, *Event Summary: Franchise Symposium Materials: International Franchise Regulation*, 8 ASPER REV. INT'L BUS. & TRADE L. 317, 335 (2008) (discussing Italy's lack of franchise-specific legislation until 2004).

177. Master Franchise Guide (2007), *supra* note 112, at 281.

178. *Id.*

179. *Id.*

180. *Id.*

whether or not to enter into the agreement."[181] A comparative analysis of the recent period of adoption of franchise-specific legislation shows that, with the exception of the Russian Civil Code, every nation's franchise laws, in some way, deal with the disclosure requirements reflected in UNIDROIT's Guide.[182]

These franchise-specific laws also usually provide a definition of which relationships constitute franchises. For example, in Malaysia, the law dictates that the relationship is established where the franchisee operates a business separately from the franchisor, such that he is not an agent, partner, or service contract provider.[183] One would thus think that the franchisor, as a known separate business, would not ordinarily be vicariously liable for the franchisee's acts. However, a country defining the franchise relationship in this way (and Malaysia is just one of dozens of nations that does so) does not exclude franchisors from potential vicarious liability under actual or apparent authority.[184] Thus, to continue with the Malaysian example, the Malaysian courts have found that a franchisor can be held vicariously liable under theories of actual or apparent authority whenever the franchisor has some control over third parties *or* franchisees.[185]

Ultimately, the Guide is, as its name suggests, a guide to what regulations nations should implement.[186] However, although there are many differences between the types, texts, and levels of detail of instruments regulating franchising agreements, national franchising laws mostly require the same type of information as UNIDROIT recommends.[187] In analyzing the disclosure laws of various nations, the Guide illustrates their considerable variance.[188]

B. *Model Nations*

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181. Specifically, Annex Three notes the following points which the franchisor should disclose to the franchisee: the franchisor and the directors of the enterprise; the history of the enterprise; the legal constitution of the enterprise; the intellectual property concerned; the financial situation, with audited financial statements for the two or three preceding years; the other franchisees in the network; information on the franchise agreement, such as the duration of the agreement, conditions of renewal, termination and assignment of the agreement; as well as information on any exclusivities. *Id.*

182. LENA PETERS, INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW (UNIDROIT) 48–49 (Roger Blanpain ed. 2011); Kerkovic, *supra* note 95, at 257.

183. Leela Baskaran, *Malaysia*, *in* INTERNATIONAL FRANCHISING, *supra* note 12, at MAY/1, MAY/32.

184. *Id.*

185. *Id.*

186. *See* Kerkovic, *supra* note 95, at 257.

187. *Id.*

188. Nations with such varying approaches to disclosure include Albania, Australia, Belarus, Belgium, Brazil, Canada (Alberta, Ontario and Prince Edward Island), China, Croatia, Estonia, France, Georgia, Indonesia, Italy, Japan, Kazakhstan, Lithuania, Malaysia, Mexico, Moldova, Romania, Russia, South Korea, Spain, Sweden, Ukraine, United States, and Vietnam. *See generally id.* at 282–301.

The following discussion highlights some of the regulatory schemes that have emerged in some important and representative jurisdictions. As previously mentioned, the regulatory schemes of the countries discussed are largely dependent on their roots in either a common law or a civil law system.

1. The European Union

The scope of the European Union's franchising legislation was defined with the European Court of Justice's (ECJ) decisions in the case of *Pronuptia de Paris GmbH* (Frankfurt am Main) and *Pronuptia de Paris Irmgard Schillgalis* (Hamburg).[189] The German Federal Court of Justice referred these cases to the ECJ for the purposes of establishing a ruling on the interpretation of Article 85 of the European Economic Community (EEC) Treaty.[190] This Treaty deals with particular categories of exclusive dealing agreements.[191] The ECJ determined that "the franchisor must be in a position to protect certain interests vital to the business and to the identity of the network (for example, the know-how), although the provisions must be essential for this purpose."[192] Accordingly, after *Pronuptia*, the Commission of the European Union rendered decisions on five franchising cases[193] and ultimately accepted a Block Exemption Regulation on franchise agreements.[194]

The Block Exemption Regulation entered into force on February 1, 2000 and identified the different categories of franchise agreements to which it applied:[195] Article 2 of the regulation indicated "to which restrictions of competition the exemption should apply"; Article 3 indicated "to which it should apply notwithstanding the presence of certain obligations"; Article 4 addressed "to which it should apply on certain conditions"; and Article 5 dealt with exemptions "[to] which it should not apply."[196] The regulation also supplied an opposition

189. Master Franchise Guide (2007), *supra* note 112, at 301 (citing Case 161/84 of 28 January 1986).

190. *Id.*

191. *See id.* (noting that the German Federal Court of Justice sought a ruling on the application of Article 85(3) of the ECC Treaty to certain exclusive dealing agreements). Specifically, it concerns potential quarrels over a franchisee's obligation to pay the franchisor for any arrears on fees. *Id.*

192. *Id.* at 301–02.

193. Commission Decision 87/14, 1987 O.J. (L 8) 49 (EC); Commission Decision 87/17, 1987 O.J. (L 13) 39 (EC); Commission Decision 87/407, 1987 O.J. (L 222) 12 (EC); Commission Decision 88/604, 1988 O.J. (L 332) 38 (EC); Commission Decision 89/94, 1989 O.J. (L 35) 31 (EC); Master Franchise Guide (2007), *supra* note 112, at 302 n.131.

194. Master Franchise Guide (2007), *supra* note 112 at 302 (citing Commission Regulation 4087/88, 1988 O.J. (L 359) 46 (EC) (explaining the application of Article 85(3) of the Treaty to categories of franchise agreements)).

195. *Id.* at 302.

196. *See id.* (discussing the application of the various Articles in the Franchising Block Exemption Regulation).

procedure at Article 6.[197] After just four months, however, the regulation was superseded by the Block Exemption Regulation on Vertical Restraints,[198] which entered into force on June 1, 2000.[199] Unlike its predecessor, this new exemption did not specifically mention "franchising."[200] Nonetheless, "the Guidelines that accompany the text make it quite clear that it applies also to franchising."[201] These rules, affecting a wide range of sales of goods and services, address highly significant points for franchises, including intellectual property issues and in-term and post-term noncompetitive provisions.[202]

2. France

There is a notable distinction between agency doctrine in common law countries, such as the United States, and civil law countries, such as France (and many other Member States of the European Union): in the analysis of vicarious liability claims, courts in civil law countries focus far more on the reasonable expectations of consumers, as opposed to the extent of a franchisor's control over its franchisee.[203] Thus, disclaimers in advertisements and at franchisee locations that serve a notice function—to indicate the independence of the franchise corporation—naturally play a more vital role in combating vicarious liability claims.[204] Accordingly, the absence of disclaimers as to the independence of a franchise corporation can prove fatal in civil law liability claims.[205]

France provides an illuminating example of mature franchise law. The country boasts the largest franchising market in Europe, with total sales of $51.6 billion and more than 929 franchisors.[206] Similarly

197. *Id.* at 302 n.138.

198. *Id.* at 303–04 (citing Commission Regulation 2790/1999, 1999 O.J. (L 336) 21 (EC) on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices); The focus of this Regulation is the vertical agreements that fall under Article 81(3), including "agreements for the purchase or sale of goods or services where these agreements are concluded between non-competing undertakings, between certain competitors or by certain associations of retailers of goods, [and] vertical agreements containing ancillary provisions on the assignment or use of intellectual property rights." However, the Regulation does not prohibit all restrictions on vertical agreements. In fact, some vertical restraints are permitted, including those that have a positive effect, such as "the improvement of economic efficiency." Moreover, highly anti-competitive restraints, including fixed resale prices and territorial protections, cannot reap the benefit of the exemption.

199. *Id.* at 303.

200. *See id.* (noting that Commission Regulation 2790/1999 does not mention franchising in its text).

201. *Id.* at 303–04 (citing Commission Notice, 2000 O.J. (C 291) 1 (EC)).

202. *Id.* at 304 (citing Commission Regulation (EC) 2790/1999 at arts. 2(3) & 5(a)(b)).

203. RUBENSTEIN ET AL., *supra* note 15.

204. *Id.*

205. *Id.*

206. Faria, *supra* note 176.

to the United States, France has a rich history in franchising, which dates back to the 1930s when a knitting company started to "franchise" its business model in France.[207] Soon after the start of franchising, in a 1937 case,[208] the French Supreme Court recognized the test for vicarious liability "to be one of authority and subordination, characterized by 'the right to give the employee (*préposé*) orders or instructions as to the manner in which he shall undertake the functions for which he is employed.'"[209] Then, in the 1970s, franchising started to grow and began appearing in all sectors of the economy, analogously to the development patterns in the United States. This growing market precipitated the need for franchising-specific legislation.[210]

In 1989, the French Assembly became the first EU Member State to implement legislation addressing this issue when it passed Act. No. 89-1008, known as *Loi Doubin* (codified in the French Commercial Code as Art. L.330–3).[211] Although Loi Doubin is not franchise specific, it relates to all forms of commercial arrangements whose contracts contain exclusivity clauses.[212] It, therefore, details requirements that apply to franchisors as well as other licensors, including disclosure of relevant dates and descriptions, but refrains from addressing any franchise-specific relationship issues that would arise after the initial formation of the agreement.[213] Thus, discussion of the vicarious liability of franchisors is absent from Loi Doubin.

France still lacks any formal legislation directed at the ongoing relationship aspects of franchise agreements. Instead, general contract law largely governs these issues.[214] However, in the event that a franchisor exercises sufficient control over the franchisee, the latter may be viewed as an employee, which would lead to the application of French labor law.[215] This labor law test focuses on whether there is a

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207. *Id.*

208. Cour de cassation [Cass.] [Supreme Court for Judicial Matters] 1e civ., May 4, 1937, Bull. civ. I, No. 95 (Fr.).

209. PAULA GILIKER, VICARIOUS LIABILITY IN TORT: A COMPARATIVE PERSPECTIVE 58–59 (2010).

210. Faria, *supra* note 176.

211. Rémi Delforge & Gilles Menguy, *France*, *in* INTERNATIONAL FRANCHISE SALES LAWS 161, 165 (Andrew P. Loewinger & Michael K. Lindsey eds., 2015).

212. *National Regulation by Country,* EUROPEAN FRANCHISE FED'N, tbl.1, http://www.unidroit.org/guide-franchise-2nd-national-info/131-instruments/franchising/guide/guide-2edition/national-information-2nd-franchise/country/299-france-legislation-and-regulations-relevant-to-franchising (last visited Mar. 5, 2017) [https://perma.cc/BU4T-VWDY] (archived Mar. 4, 2017).

213. *See* Delforge & Menguy, *supra* note 211, at 165–66 (setting forth the one article Loi Doubin as adopted by Decree 91-337).

214. *See* Kerkovic, *supra* note 95, at 113 (noting that French law merely requires the parties to make certain disclosures before entering into a franchising agreement).

215. Emanuel Schulte, *France*, *in* FRANCHISE IN 30 JURISDICTIONS WORLDWIDE 62, 63 (Philip F. Zeidman ed., 2014), http://www.franchise.org/sites/default/files/ek-pdfs/html_page/F2014-France_0.pdf [https://perma.cc/7UJ6-QEZ3] (archived Jan. 17, 2017).

"subordination link" between the franchisor and franchisee.[216] In particular, subordination may exist where the franchisee's duty merely consists of selling goods that are predominantly supplied by the franchisor, at conditions and prices set by the franchisor, and in premises owned or rented by the franchisor, or where the franchisee's remuneration largely depends on the conditions instituted by the franchisor.[217] Despite the relative clarity of the direct subordination link, questions abound with respect to potential liability between parties to the franchise contract and third parties.

If labor law does not apply, general contract law, as set out in the French Civil Code, indicates that a contract may establish liabilities only between the contracting parties and not between third parties.[218] This is because the French test of *subordination juridique* (legal subordination) focuses on "identifying who has the right to give orders or instructions to the employee as to how to do their job."[219] A 2006 French Supreme Court decision rejected this rigid approach, however, and moved toward a more flexible interpretation, finding that a third party may have an action based in tort. In that case, a commercial tenant's managing agent (the third party) had a claim in tort against a landlord who had breached the lease with the tenant.[220] Thus, "the power to give instructions need not have a contractual or legal basis, but instead may simply exist as a matter of fact . . . it is no longer necessary to prove that such power has been exercised," as long as the person in question is found to possess authority over the alleged subordinate.[221]

Furthermore, while French law views the franchisee as the employer of its own employees, if there is a direct subordination link between the franchisor and the franchisee's employees, there is a risk that the franchisor may be deemed to be their employer, which could lead to vicarious liability, and even criminal sanctions under certain circumstances.[222] Thus, a "franchisor not fulfilling its contractual obligations towards a franchisee which consequently is no longer able to pay the suppliers, may face an action brought by the same suppliers for the damages they suffered."[223] In hopes of avoiding this risk, it is crucial for franchisors to ensure that the franchisee is the sole decision-

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216. *Id.* at 63.
217. *Id.*
218. RUBENSTEIN ET AL., *supra* note 15, at 14.
219. GILIKER, *supra* note 209, at 66.
220. RUBENSTEIN ET AL., *supra* note 15, at 14 (citing Cour de cassation [Cass.] [supreme court for judicial matters] ass. plén., Oct. 6, 2006, No. 541 (Fr.)). The French court held that a third party has an action in tort against a contracting party by proving that the contracting party committed a civil wrong by breaching the contract; in other words, the third party may seek compensation, based on tort principles, by invoking the contractual fault of a party whose breach caused him damage.
221. GILIKER, *supra* note 209, at 66.
222. Schulte, *supra* note 215, at 63.
223. RUBENSTEIN ET AL., *supra* note 15, at 14.

maker in hiring, providing work instructions, supervising, and sanctioning and terminating the employment contracts of the franchisee's employees.[224]

Additional regulation comes from the Code of Ethics, promulgated by the French Franchise Federation (FFF).[225] Although FFF membership is not mandatory for French franchise corporations, the Code nevertheless provides insight into commonly recommended and expected behavior.[226]

In France, the simplest, yet perhaps most effective restraint on any claim of vicarious liability against franchisors is the national administrative order, known as the *Neiertz Decree*.[227] This decree requires every franchisee to identify its ownership status and to inform consumers that the franchisee is an independent business distinct from its franchisor: "[a]nyone selling products or providing services that is bound by a franchise agreement with a franchisor must inform the consumer of its being an independent business, in a legible and visible manner on all information documents, especially advertising, as well as inside and outside the point of sale."[228] This administrative decree "essentially aims to promote customer knowledge" about the franchised nature of a business.[229] It is thus meant "to ensure that the consumer does not think he is dealing directly with the franchisor or the parent company."[230] In effect, such Neiertz Decree notices, whether on sales receipts, invoices, in any other correspondence, on a website, in an advertisement, or in any sign or posting at the franchise's physical location (e.g., its office or store), tend to make apparent authority impossible for most practical purposes, both according to the

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224. *Id.* at 15.

225. *See generally* EUR. FRANCHISE FED'N, EUR. CODE OF ETHICS FOR FRANCHISING (2003).

226. *Id.*

227. In the French Ministry of the Economy, Finance and Budget, the State Secretary of Consumer Affairs issuing the Decree of February 21, 1991 was Veronique Neiertz, hence the shorthand title, *l'arrêté Neiertz* ("the Neiertz Decree").

228. Dêcret du 21 février 1991 relatif à l'information du consommateur dans le secteur de la franchise [Decree of Febuary 21, 1991 on Consumer Information in the Franchise Sector], Journal Officiel de la République Française [J.O.] [Official Gazette of France], Mar. 1, 1991, p. 2963 («Toute personne vendant des produits ou fournissant des services, liée par un accord de franchise à un franchiseur, doit informer le consommateur de sa qualité d'entreprise indépendante, de manière lisible et visible, sur l'ensemble des documents d'information, notamment de nature publicitaire, ainsi qu'à l'intérieur et à l'extérieur du lieu de vente.») (Eng. trans. by author).

229. *Annuaire et Conseil pour réussir en Franchise*, AC FRANCHISE SARL, http://ac-franchise.com/page/larrete-neiertz (last visited Aug. 26, 2016) [https://perma.cc/9R48-YS8Y] (archived Jan. 22, 2017) (The decree « vise essentiellement à faire connaître à la clientèle la qualité de franchisé de commerçant . . . ») (Eng. trans. by author).

230. *Id.* (« qui la sert pour que le consommateur ne pense pas qu'il a affaire directement avec le franchiseur ou la maison-mère. ») (Eng. trans. by author).

French and English language and under both French and Anglo-American law.[231]

3. Italy

Unlike France, Italy seemed to ignore the commercial practice of franchising, declining to implement any real legislative discipline until very recently.[232] Most scholars believe this lack of discipline was probably one of the key reasons for the rapid expansion of franchises in Italy and throughout Europe in the last few decades.[233] However, this utter lack of discipline made it impossible to establish a consistent definition of *franchise* and, consequently, spawned numerous controversies.[234] Finally, in 2005, thirty years after the first appearance of a franchise agreement in the country, Italy enacted a franchise law[235] and provided a legislative framework for franchising[236] in Law Number 129/2004, although this law did not contain any specific provision on a franchisor's vicarious liability.[237]

In light of Law Number 129/2004's failure to address vicarious liability, scholars have turned to the Italian civil code and case law in order to determine a franchisor's vicarious liability for the acts of its franchisee.[238] Identically to French law, under a general rule detailed in the Italian civil code, a contract may be binding and effective only

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231. The meaning of "impossible" is the same in French and English. More important, such notices—whether in France's Civil Law or in the Anglo-American common law—destroy any reasonable basis for a customer's reliance on a presumed agency relationship. Although not required by statute in the United States, "plain notices about independent ownership and operations should be part of the effort to warn a franchised chain's customers and potential customers that the risks of tort losses and contract breaches are not incurred by the franchisor." Robert W. Emerson, *Franchisors' Liability When Franchisees Are Apparent Agents: An Empirical and Policy Analysis of "Common Knowledge" About Franchising*, 20 HOFSTRA L. REV. 609, 669 (1992). In fact, most U.S. franchise agreements now likely require the franchisee to post notices telling the public about the franchisee's independent status. Emerson, *supra* note 29, at 697 (explaining a survey of 100 U.S. franchise agreements found 79 percent had such a clause, up from just 21 percent of the agreements in a comparable survey in 1993).

232. Schwartz & Zylberman, *supra* note 176, at 335 (noting that "Italy first adopted franchise legislation on 21 April 2004, with the introduction of the *Law on Commercial Affiliation*").

233. Valentina Giarrusso, *Franchise Agreements Under Italian Law*, *in* THE COMPARATIVE LAW YEARBOOK OF INTERNATIONAL BUSINESS 493, 494 (Dennis Campbell ed., 2007).

234. *Id.* at 494–95; *see also* Francesca Ferrero & Julia Holden, *Italy*, *in* INTERNATIONAL FRANCHISING, *supra* note 12, at ITA/16 (arguing that the lack of specific franchise law in Italy contributed to a growth of "'atypical' contracts").

235. Decreto Ministeriale 2 settembre 2005, G.U. n. 129 /2004 (It.).

236. *Id.* at 4.

237. RUBENSTEIN ET AL., *supra* note 15, at 11; *see also* Aldo Frignani & Francesca Turitto, *Italy*, *in* INTERNATIONAL FRANCHISE SALES LAWS *supra* note 211, at 237, 240 (the law's scope includes disclosure, rights of use, and obligations of the parties, but does not mention vicarious liability).

238. RUBENSTEIN ET AL., *supra* note 15, at 11.

between the parties entering into it. Thus, a franchisor may only be liable to a third party under particular circumstances for liability in tort.[239] Yet, just as French courts broadened this rigid approach, Italian courts have established two legal bases for holding a franchisor liable for the conduct of its franchisees or a franchisee's employees.[240]

First, a third party may bring suit against a franchisor for the franchisee's acts if the franchisor and the franchisee appear to be one single entity and the third party reasonably believes that it is entering into an agreement with an agent of the franchisor.[241] Thus, Italian courts have held that a franchisor may be vicariously liable for the tortious acts of a franchisee that is its apparent agent.[242] The apparent agent doctrine was first applied in Italy in *Grimaldi S.p.A. v. Magatelli Effci S.a.s.*, where the Court of Milan ruled that, in order to build a case of vicarious liability, the apparent agency relationship must be (1) based on objective grounds, (2) generated because of franchisor instructions and contractual forms, and (3) arising from the third party's reasonable reliance upon a good faith belief that the franchisor and the franchisee are the same entity.[243] Therefore, to avoid this risk, the franchisor and the franchisee must make it obvious to third parties that they are independent and autonomous entities and that the franchisee is not an agent of the franchisor.[244]

Second, if the franchisor has the right and the power to control and manage a franchisee, then the franchisor may be liable for that franchisee's conduct.[245] The franchisor's vicarious liability as the controlling company may occur when the franchisor has the right to hire and fire, sets hours of work and rates of pay, and gives directions on the work performed by the franchisee's personnel.[246] In addition, similarly to some U.S. jurisdictions, a franchisor could be liable if it

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239. *Id.*; *see also* Decreto Ministeriale 2 settembre 2005, G.U. n. 129 /2004 (It.).

240. RUBENSTEIN ET AL., *supra* note 15, at 11; *compare* Pretura Milano, 21 luglio 1992, Contratti, pag. 173 n. DE NOVA, Franchising ed Apparenza, 1993 (establishing the grounds to build a case of vicarious liability based upon the apparent agency relationship), *with* Tribunale di Milano, 25 giugno 2005, Rivista giuridica del lavoro e previdenza, 97, ss, 2006 (determining the liability of a franchisor as a "controlling company" or as a company exercising direction and coordination activity).

241. RUBENSTEIN ET AL., *supra* note 15, at 11.

242. Maria Elena Giorcelli et al., Vicarious Liability of the Franchisor for Acts and Omissions of the Franchisees and their Employees: Canada, Italy and The United States (2013) (unpublished presentation), www.idiproject.com:8000/media/materials/24-Panel_Zwisler.ppt [https://perma.cc/ZSG6-QFZ6] (archived Feb. 11, 2017).

243. RUBENSTEIN ET AL., *supra* note 15, at 12; (*citing* Pretura Milano, 21 luglio 1992, *in* Contratti, pag. 173 n. DE NOVA, Franchising ed Apparenza, 1993).

244. *See* Ferrero & Holden, *supra* note 234, at ITA/17; RUBENSTEIN ET AL., *supra* note 15, at 11.

245. RUBENSTEIN ET AL., *supra* note 15, at 11; *see also* Vichi v. Koninklijke Philips Elecs, N.V., 85 A.3d 725, 798–807 (Del. Ch. 2014) (comparing Delaware and Italian law of vicarious liability outside of franchising context, where Delaware law turned on apparent agency but Italian law turned on employer control).

246. RUBENSTEIN ET AL., *supra* note 15, at 11.

controls the uniformity and the standardization of products and services.[247] In a recent decision, an Italian court held that, if a franchisor can contractually control the quantity, colors, and products to be sold by the franchisees, the franchisor may be held liable.[248] In this regard, the franchisor and franchisee may be reclassified, for the purposes of the labor laws, as a single unified employer—that is, the franchise agreement is seen as a surreptitious instrument to jointly manage two businesses disguised as a franchise relationship.[249] Therefore, it is in the franchisor's best interest to limit its powers to direct the franchisee's business within the franchise agreement and to avoid management of the franchisee's personnel within their day-to-day operations.[250]

4. Germany

In Germany, the franchisee is ultimately liable "for all obligations resulting from its activity, especially for claims for damages of all kinds."[251] However, the franchisor generally cannot escape product liability claims.[252] But, if the franchisor was not at fault for the particular defect, he may be able to exempt himself under the *Produkthaftungsgesetz-ProdHaftG* (Product Liability Act).[253] Section 1(3) of the Product Liability Act states that the liability of the manufacturer of a component part is exempt if the mistake is caused by the construction of the product in which a part of the product is incorporated, or if the harm resulted because of the product manufacturer's instructions.[254] In a case where the franchisor and franchisee are both at fault, they are both jointly and severally liable to the harmed party.[255] To each other, however, they are liable only for the share of damage they caused individually.[256] In order for the franchisor, as the quasi-manufacturer, to avoid liability, it must not allow the consumer to assume that it is the manufacturer.[257] Thus, the franchisor should ensure that notice is provided for any product that

247. *Id.* at 13.
248. *Id.*; Tribunale di Pescara, 2 febbraio 2009, Foro it. 2009, I, 2829 (It.).
249. RUBENSTEIN ET AL., *supra* note 15, at 12–13.
250. *Id.* at 12.
251. Stefan Bretthauer, *Germany*, *in* INTERNATIONAL FRANCHISING, *supra* note 12, at GER/28–29.
252. *Id.*
253. *Id.*
254. Produkthaftungsgesetz [ProdHaftG] [Product Liability Act], Dec. 15, 1989, BGBlI at 2198, § 1 (Ger.), (translated at http://www.utexas.edu/law/academics/centers/transnational/work_new/german/case.php?id=1397 (last visited Jan 22, 2017) [https://perma.cc/VDC7-TZDR] (archived Jan. 22, 2017)); *see* Bretthauer, *supra* note 251, at GER/29–30 (outlining how Germany's Product Liability Act may or may not affect franchisors).
255. *Id.*
256. *Id.* (citing the Product Liability Act, Section 5).
257. *See* Bretthauer, *supra* note 251, at GER/30.

the franchisee actually manufactures by having the franchisee attach a note asserting that the franchisor is not the manufacturer of the finished product.[258] However, this policy of notification may not be the best strategy for a franchisor striving for uniformity throughout the franchises.[259] Franchisors will want to weigh the importance of uniformity against the risk of liability.[260]

Ultimately, German case law no longer requires a detailed right of control for vicarious liability: "it is sufficient that the employer can at any time determine the scope and duration of the tasks of the employee, restrict them or terminate them." Thus, the focus is no longer on the fact of the franchisor actually instructing the franchisee how to do his job, but rather on the ability of the franchisor to do so.[261]

In 2007, the Federal Supreme Court of Germany issued decision XZR 137/04,[262] reinforcing the concept that a franchisor may become bound by contracts between its franchisee and a customer where the franchisee does not disclose to the general public that it is a legally independent entity.[263] Thus, there exists a possible source of vicarious liability for the acts of the franchisee if a third party assumes that the franchisee is acting on behalf of the franchisor and the franchisor knows or should have known this but does not mind.[264] The franchisee is then considered to be an agent of the franchisor.[265] This risk could be minimized by the franchisor denying agency in the franchise agreement, ensuring that the franchisee identifies itself as an independent business (including by registering a business name), or

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258. *Id.*

259. The more the individual franchisee controls production, and thus protects the franchisor from potential liability for a product defect, the more likelihood of variance in production within the network.

260. *See* Bretthauer, *supra* note 251, at GER/29

261. GILIKER, *supra* note 209, at 66–67.

262. An English translation of the decision is found at: http://translate.google.com/translate?hl=en&sl=de&u=http://www.telemedicus.info/urteile/Marken-und-Namensrecht/Domainnamen/689-BGH-Az-I-ZR-13704-Euro-Telekom.html&prev=/search%3Fq%3Dtelekom%2Bzr%2B137/04%26client%3Dfirefox-a%26hs%3DYZM%26rls%3Dorg.mozilla:en-US:official (last visited Jan. 22, 2017) [https://perma.cc/8CFG-VUHN] (archived Jan. 22, 2017).

263. In German law, a franchisor could be liable to third parties for the franchisee's acts under one or more of these situations: (1) contractual liability to consumers due to the franchisee's appearance, in terms of its legal position; (2) "tortious organisational liability"; (3) liability of a franchisor-producer of a defective product sold by a franchisee; (4) on occasion, when a franchisee commits an act of unfair competition of the franchisee. Marco Hero, *Country Report Germany*, *in* Int'l Distribution Inst., Franchising Country Reports, at 10 (2015); Bretthauer, *supra* note 251, at GER/1, GER/27–31. The first situation encompasses apparent authority as a possible ground for franchisor liability due to franchisee actions.

264. RUBENSTEIN ET AL., *supra* note 15, at 15; *see also* BGH Dec. 18, 2007, XZR 137/04, §§ 164, 242, http://juris.bundesgerichtshof.de/cgi-bin/rechtsprechung/document.py?Gericht=bgh&Art=en&Datum=2007&Seite=3&nr=42638&pos=118&anz=3318 [https://perma.cc/WN79-PN7E] (archived Mar. 5, 2017).

265. *Id.*

ensuring that the franchisee has to bear the liability in the internal relationship.[266]

5. China

China is currently experiencing a rapid expansion of franchising.[267] And, over the last twenty years, China has developed a comprehensive legal framework governing franchises, including laws dealing with both disclosure requirements and relationship issues.[268] Yet, because of China's unique isolationist policy, franchising was not easily adopted.[269] With China's concurrent commitments to market development and to political socialism, the development of franchising in China has been something of an enigma as compared to the traditional adoption of franchising in European countries.[270] In the early 1990s, the word "franchise" had no direct Chinese translation; instead, the closest translation amounted to "chain of stores."[271] In spite of its isolationist policies, however, the Chinese government began to recognize the viability of a "chain of stores" (or franchise) as a business structure.[272] Although, even as the country cracked its doors open to foreign investment, it has maintained a cautious approach in structuring its rules governing foreign enterprises.[273]

Franchising in China has developed from being unrecognized and unregulated to becoming a viable, increasingly adopted business model.[274] At first, the Chinese government did not formally regulate franchising, but—in order to foster it—the government issued *Interim Measures on Regulating Franchise Operations* (Franchise Measures) in 1997.[275] Article 5 of these measures identified two types of franchise structures: (1) a direct franchise and (2) a franchise that allows master

266. *Id.*

267. *See* Ilan Alon & Ke Bian, *Franchising Profile and Practices in the People's Republic of China*, 1 IBAT J. MGMT. 98, 100–05 (2004) (highlighting the rapid growth of franchising in different sectors in China, including food, retail, real estate, health, education, and services).

268. *See* MINISTRY OF COMMERCE OF THE PEOPLE'S REPUBLIC OF CHINA: MEASURES FOR THE REGULATION OF COMMERCIAL FRANCHISE art. 9–12, 19 (2005), http://www.lapres.net/franchise.pdf [https://perma.cc/JJ5K-58Z5] (archived Feb. 5, 2017) (articles 9–12 deal with the rights and obligations of franchisors and franchisees; article 19 deals specifically with the disclosure requirements of franchisors).

269. *See* Lee, *supra* note 95, at 954 (describing China's history of isolationism since the start of communism).

270. *See id.* ("China has continued its commitment to political socialism.").

271. William Edwards, *The Pros and Cons of Franchising in China*, CHINA BUS. REV. (Jul. 1, 2011), http://www.chinabusinessreview.com/the-pros-and-cons-of-franchising-in-china/ [https://perma.cc/DT5C-KYQ2] (archived Jan. 22, 2017).

272. Lee, *supra* note 95, at 956.

273. *Id.* at 956–57.

274. *See* Cheong, *supra* note 12, at CHN/1 (citing the positive outlook corporations have on franchising in China, including McDonald's Corporation's plans to expand further in Shanghai and Shenzhen).

275. Edwards, *supra* note 271.

franchisees to distribute the franchise out to sub-franchisees.[276] In the same year, "[t]he China Chain Store and Franchise Association (CCFA)—a quasi-government nonprofit membership association for Chinese and foreign retailers, franchisers, and well-known foreign brands—also formed."[277] The CCFA now has nine hundred members with 180,000 outlets across China, and generated annual sales of $300 billion in 2010—the top 120 franchisors alone amassed $52.4 billion.[278] Thus, the franchise business model has burgeoned into a desirable business model in China due to the population's increasing affluence and strong middle-class base.[279]

Yet, even with the potentially promising opportunities for franchisors in the Chinese market, they should be cautious of "the lax licensing regulations, vague laws, and weak intellectual property protection that could undermine the very identity of a franchise."[280] Consequently, foreign franchisors should ensure that they maintain as much control as possible in their business ownership, intellectual property, and contractual agreements.[281] But, by ensuring this control as additional protection against the nebulous nature of Chinese laws, franchisors are simultaneously opening themselves up to greater risks of vicarious liability because they maintain maximum control over the franchisee.[282]

Because of China's unique franchising structure, it is crucial to first understand and appreciate the types of franchises recognized under the Chinese Franchise Measures.[283] Under Article 5 of the 1997 Franchise Measures, a franchise could be either a direct franchise or a sub-franchise.[284] Direct franchising is established through a contractual relationship in which a franchisor directly grants franchise rights to a candidate but does not grant the right to sub-franchise those rights.[285] In direct franchising, the franchisor directly gives the franchisee the right to operate individual or multiple franchise units in a specific location or area; this has proven successful for several foreign franchisors.[286] For the other, "indirect" type of franchising, a sub-franchise operates under a master franchising agreement—an

276. Lee, *supra* note 95, at 957.
277. Edwards, *supra* note 271.
278. *Id.*
279. Lee, *supra* note 95, at 951–52.
280. *Id.* at 952–53.
281. *Id.* at 953.
282. *See* Master Franchise Guide (2007), *supra* note 112, at 172 ("Excessive control over the sub-franchisee could result in the franchisor and sub-franchisor being exposed to liability for the acts or omissions of the sub-franchisee.").
283. *See* Lee, *supra* note 95.
284. Bryan W. Blades, *Franchising in China: A Current Perspective*, 14 CURRENTS: INT'L TRADE L.J. 20, 22 (2005).
285. *Id.* (emphasis added).
286. *See* Lee, *supra* note 95, at 957 (listing Kodak as an example of a franchisor who has successfully utilized direct franchising).

agreement that grants a franchisee "the exclusive rights to operate franchise outlets in a designated territory along with the right to then sub-franchise those rights to other parties within that territory."[287] These Franchise Measures have attracted great interest from commentators in common law jurisdictions, as they provide a unique illustration of franchising law in a civil law country.[288]

The Franchise Measures have proven most interesting in regards to the potential vicarious liability for franchisors in China because they require a franchisor to guarantee the quality of the products sold by its designated suppliers.[289] The Chinese government hopes to protect consumers by holding the franchisor liable for the products sourced from outside suppliers.[290] This is consistent with the practice of other civil law countries, focusing on the reasonable expectations of consumers when determining the vicarious liability of franchisors.[291] Even with these seemingly straightforward protections, however, there is scant discussion of franchisor vicarious liability under the Franchise Measures—these measures instead serve mainly as an industry guideline promoting franchise business.[292]

Because of the rapidly developing economic and social conditions, compounded by the rampant fraud in domestic franchising activities in China, the Chinese State Council enacted a law in 2007 that more directly addresses the rights and obligations of the parties in franchising: the *Regulations on Administration of Commercial Franchise Regulations* (Franchise Regulations).[293] The Franchise Regulations apply to commercial franchises, which essentially consist of three elements: (1) the franchisor licenses to the franchisee "operational resources," (2) the franchisee operates under a unified business format, and (3) the franchisee pays the franchisor a franchise fee.[294] "Unlike the [Franchise] Measures, the [Franchise] Regulations do not explicitly address master franchise relationships and the subfranchising activities conducted thereunder."[295]

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287. Blades, *supra* note 284, at 22–23.

288. *See* Paul Jones, *The Regulation of Franchising in China and the Development of a Civil Law Legal System*, 2 CHINESE L. & POL'Y REV. 78 (2006) (discussing the differences between franchising law in common law and civil law jurisdictions, using China as an example).

289. Erik B. Wulff & Tao Xu, *Franchise Regulation in China*, 25 FRANCHISE L.J. 19, 21 (2006).

290. *Id.*

291. *See* RUBENSTEIN ET AL., *supra* note 15, at 11–17 (discussing the policies of other civil law countries).

292. Zhiqiong June Wang & Andrew L. Terry, *The Impact of China's Regulatory Regime on Foreign Franchisors' Entry and Expansion Strategies*, 7 ASIAN J. COMP. L. 1, 7–8 (2011).

293. *Id.* at 10; *see* Paul Jones & Erik Wulff, *Franchise Regulation in China: Law, Regulations, and Guidelines*, 27 FRANCHISE L.J. 57 (2007) (discussing the applicability of the regulations).

294. Jones & Wulff, *supra* note 293, at 58.

295. *Id.*

The Franchise Regulations also require that a franchisor "shall have a mature business model . . . [and] shall own at least two directly operated company owned outlets for more than one year."[296] Courts have applied the latter requirement—dubbed the 2+1 rule—inconsistently, and questions abound as to whether it is only an administrative provision or whether it is a substantive requirement.[297] While the Franchise Regulations made significant changes to the registration and disclosure of franchisors, the focus of this discussion is on their relationship and conduct modifications.

The regulations integrate the mantra that "persons engaged in franchising must follow the principles of voluntariness, fairness, honesty, and good faith," listing the basic rights and obligations of both franchisors and franchisees.[298] The franchisor is required to furnish a "franchise operations manual to the franchisee, and provide continuing operational guidance, technical support, business training, and other services to the franchisee in accordance with the franchise agreement."[299] The Franchise Regulations depart from the Franchise Measures by removing the much criticized provision that made the franchisor and franchisee jointly and severally liable for the quality of designated supplier products and services.[300]

In China, however, these are all contract law principles.[301] So, rather than impose liability on franchisors through agency law, liability is imposed through the principles of Chinese contract law.[302] Apparent authority derives from agency concerns and third-party rights that are distinct from the franchising contract.[303] And the franchisor's potential liability to franchisee customers seems to be reasonable and in line with Chinese traditions, such as that of protecting injured parties and punishing those businesses that are profitable as a result of a direct or indirect connection to improper conduct linked to consumer injuries (e.g., selling defective goods or furnishing faulty services).[304]

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296. Wang & Terry, *supra* note 292, at 14 (alteration in original).

297. *Id.* at 16.

298. *Id.* at 20.

299. *Id.*

300. *Id.*

301. *Id.*; *see also* MINISTRY OF COMMERCE OF THE PEOPLE'S REPUBLIC OF CHINA, CONTRACT LAW art. 111 (2003) (imposing liability on a company that injures a party due to breach of contract).

302. *See id.* ("If the quality fails to meet the agreed requirements, liability for breach of contract shall be borne in accordance with the agreement between the parties.").

303. Wang & Terry, *supra* note 292, at 20.

304. GENERAL PRINCIPLES OF THE CIVIL LAW OF THE PEOPLE'S REPUBLIC OF CHINA arts. 122–26 (1987), http://www.npc.gov.cn/englishnpc/Law/2007-12/12/content_1383941.htm [https://perma.cc/BJ8V-VPCG] (archived Jan. 22, 2017) (dealing with liability to companies for the injuries of third parties).

6. Australia and New Zealand

In stark contrast to the aforementioned civil law countries, which place a greater focus on consumers' reasonable expectations when determining vicarious liability, common law countries, including Australia, place a greater emphasis on the extent to which the franchisor controls the franchisee.[305] In Australia, the general proposition is that a principal is usually responsible for all acts within its agent's actual or apparent authority; in deciding whether an act was within the scope of an agent's authority, the amount of control is the essential factor.[306] In Australia, "the doctrine of vicarious liability aims to produce fair and just outcomes and comfortably sits beside a 'regime that imposes liability for fault.'"[307]

Despite Australia's relative progress in the application of vicarious liability in the agency context, the doctrine of vicarious liability continues to be restricted in application to solely employer-employee relationships—it does not apply to independent contractor relationships.[308] But, Australian courts have begun to move away from a rigid "control" test and have adopted a multi-factor test to determine whether a person is an employee or an independent contractor—the "totality of the relationship test."[309] Even with this move away from the bright-line control test, however, courts still place the greatest weight on control in determining whether a person is an employee or not when applying the totality of the relationship test.[310] In determining the right of and level of control exercised, courts consider such factors as "stipulating hours that may be worked, whether a uniform or a particular style of clothing is required, workplace rules, detailed instructions relating to the work itself and how it is to be carried out, and quality control procedures."[311]

This approach can be contrasted with that used in England, which also requires that the franchisee be an employee of the franchisor in order to hold the franchisor vicariously liable, but only finds an

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305. *See* RUBENSTEIN ET AL., *supra* note 15, at 26 (discussing the distinction in the context of civil law and common law countries).

306. *Id.* at 6.

307. Andrew Terry & Joseph Huan, *The Vicarious Liability of Franchisors in Australia*, Presented at the 26th Annual International Society of Franchising Conference 7 (Ft. Lauderdale, Fla., May 17, 2012) (quoting Jason Neyers, *A Theory of Vicarious Liability* 43 ALBERTA L. REV. 287, 289 (2005)).

308. *Id.* at 8.

309. *See* RUBENSTEIN ET AL., *supra* note 15, at 6. This is in congruence with other common law countries such as Canada. The traditional Canadian test, known as the "control test," states that an individual will be considered to be an employee for vicarious liability where the employer not only tells the person what to do, but how to do it. *Id.* at 9. Yet, just as Australia has adopted a multi-factor test, Canada has embraced the "entrepreneurship test" which suggests that, besides control, other factors may determine the difference between employees and independent contractors. *Id.* at 9–10.

310. *Id.* at 6.

311. Terry & Huan, *supra* note 307, at 9-10.

employment relationship when the franchisee is receiving wage compensation from the franchisor.[312] Finding vicarious liability under such a narrow view is extremely unlikely under most franchise arrangements, where the franchisee earns, or at least tries to earn, profits from owning and running a business, not from a paycheck from the franchisor.[313]

In Australia, vicarious liability will apply in the franchising context when the franchisor and franchisee are in an employer-employee relationship.[314] This determination requires courts to examine all circumstances of the relationship in totality.[315] Yet many scholars have been critical of the multi-factor totality of the relationship test, as it is subjective and difficult to predict the number or combination of factors required to establish that a worker is an employee, particularly considering how greatly outcomes vary on a case-by-case basis.[316] From the franchisor's perspective, this type of test gives the franchisor less certainty that its level of control will not

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312. John Pratt, *England and Wales*, *in* INTERNATIONAL FRANCHISING, *supra* note 12, at ENG/1, ENG/26–27 (relying upon standards announced in Ready Mixed Concrete v. Minister of Pensions & Nat'l Ins., (1968) 1 All Eng. Rep. 433 (Eng.)) (holding that a contract of service exists - thus, whether the person is an employee/agent - if (1) the contract is consistent with the characteristics of a contract of service, (2) for wage compensations, a servant agrees to provide work or a skill performing a service for the master, and (3) performance of that service is subject to the master's control).

313. *See* ROBERT ROSENBERG & MADELON BEDELL, PROFITS FROM FRANCHISING (1969) (*Franchising* has long been defined as constituting, *inter alia*, a method for distributing branded goods or services through independent businesses (franchisees), with the franchisor continually supplying to each franchisee both know-how and brand identification and with these fees-paying and royalties-paying franchisees each "enjoy[ing] the right to *profit* and run[ning] the *risk of loss*.") (emphasis added). Federal disclosure requirements, met by following a format prescribed by the Federal Trade Commission (FTC) in the federal rule entitled "Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures" (promulgated in 1979 and amended in 2007), requires a disclosure about actual or potential profits or losses if a franchisor makes "financial performance representations." 16 C.F.R. § 436.5(s) (2009). Indeed, the fight over the franchisor's statements about a prospective franchisee's profits was at the heart of the battle over what a franchisor should have to disclose to potential franchisees. Stuart Hershman & Joyce G. Mazero, *Historical Development of Earnings Claims (Now Financial Performance Representations) Regulations*, *in* FINANCIAL PERFORMANCE REPRESENTATIONS: THE NEW AND UPDATED EARNINGS CLAIMS 1, 11–29 (Stuart Hershman & Joyce Mazero eds., 2008) (on the history of the longstanding push for and ultimate denial of mandatory earnings claim disclosures). Regardless of the legal framework, the franchisee's most basic objective is "individual profit-maximization (that is, net revenues)." Robert W. Emerson, *Franchises as Moral Rights*, 14 WAKE FOREST J. BUS. & INTELL. PROP. L. 540, 576 (2014); *see also* Robert W. Emerson, *The Neutral Factfinder as a Pathway to Legal Reform: Examples from Franchising*, 10 VA. L. & BUS. REV. 63 (2015) (detailing, throughout the article, numerous examples of lost profits claims brought by franchisees).

314. Terry & Huan, *supra* note 307, at 11. Alternatively, the parties could be in an agency relationship, or both might be present (agency *and* employment).

315. *Id.*

316. *See* RUBENSTEIN ET AL., *supra* note 15, at 7 (discussing the advantages of the "economic reality test" over the multi-factor totality of the relationship test).

amount to an employment relationship in a court's eyes. As a result, the High Court in *Hollis v. Vabu Pty. Ltd.*[317] adopted the "economic reality test," where, instead of considering the degree to which an employer may be said to have the right to control an employee, the court considers the extent to which a worker may genuinely be said to be in business on his or her own.[318] Thus, when someone is deemed an independent contractor, the court will examine whether, in the course of bargaining between the two parties, there was a genuine "trade-off" of advantages.[319] Ultimately, scholars have found that this economic reality test is a more appropriate test against which to measure the franchising relationship.[320]

Also of marked importance in the context of franchising is the fact that Australian common law only recognizes individuals as employees.[321] Thus, there is an assumption in the Australian courts that a company cannot be an employee, even if a person is a sole owner and shareholder of the company—neither a corporate body nor a partnership will be recognized as an employee.[322] Again, this classification can be compared to that used in England, which does find a franchisor vicariously liable if the franchisee is an employee, or is an agent or partner.[323] In Australia, it is only that smaller franchise owned and operated by a sole proprietor that may be classified as an employee.[324]

Because of the real challenges Australian plaintiffs face in bringing vicarious liability actions against franchisors based upon an employer-employee relationship, the majority of cases move forward with agency as the basis for franchisor liability.[325] Under Australian law, in order to establish an agency relationship between a franchisor and franchisee, plaintiffs must prove the presence of two elements: "the *consent* of both the principal and the agent, whether express or implied to the agency relationship; and *authority* given to the agent by the principal to act on the principal's behalf."[326] It is important to note that

317. *Hollis v. Vabu Pty Ltd* (2001) 181 CLR 263 (Austl.).

318. *Id.* at 39–45.

319. *Id.* at 58.

320. RUBENSTEIN ET AL., *supra* note 15, at 7.

321. *See id.* at 6 (explaining that corporations and partnerships are not recognized as employees).

322. *See id.*; Terry & Huan, *supra* note 307, at 12.

323. Pratt, *supra* note 312, at ENG/26; *see also* Natalia Lewis, *Franchisee or Employee and Vicarious Liability of Franchisors – the UK Perspective*, 2013 Annual Meeting of the International Distribution Institute (Munich, Germany) (June 15, 2013) at 5, http://www.idiproject.com:8000/media/materials/23-Paper_Lewis.pdf [https://perma.cc/2BZS-7ASJ] (archived Jan. 23, 2017) ("Since . . . a franchisee/franchisor relationship is unlikely to be considered sufficiently close in character to an employer/employee relationship, vicarious liability [in England] is most unlikely to arise.").

324. Terry & Huan, *supra* note 307, at 12.

325. *Id.* at 13.

326. RUBENSTEIN ET AL., *supra* note 15, at 7.

control over an agent's actions is far less decisive in Australia, and thus less likely to be the sole determinant in establishing an agency relationship than it is in the United States.[327] Instead, the Australian position dictates that an agent is one who has *authority* to act for another.[328] Despite favoring the authority test over the control test (similarly to the United States), franchisors in Australia can be held liable under both actual agency—established by a conferral of authority—or apparent agency when the principal held out to a third party that a particular agent had authority.[329]

Liability under actual agency is best understood as a "creature of contract," formed by a conferral of authority by the principal to the agent to act on the principal's behalf.[330] The main thrust of the Australian agency relationship is to allow the principal to be represented by the agent, and, concurrently, to create legal relations with third parties.[331] In the franchising context, the franchisor's liability is derived from the franchisor having authorized the franchisee to act on its behalf, and not from the inherent control that the franchisor exercises over the franchisee.[332] Ultimately, if the franchisee acts as an agent of the franchisor and within the scope of its authority, and the franchisor controls the channels of business, then the franchisor is vicariously liable for the franchisee's conduct by way of actual agency.[333] In order to mitigate the risk of this potential liability, the franchisor should deny agency in the franchise agreement and ensure that the franchisee identifies itself as an independent business.[334]

More central to this discussion is the theory of apparent agency. In order to establish apparent agency in Australia, the plaintiff must (1) establish that the franchisor has represented or "held out" the franchisee as possessing authority, (2) reasonably rely on the representation, and (3) suffer a detriment as a result of the representation.[335] While a franchise agreement may explicitly reject an agency relationship, this does not technically preclude a finding of apparent authority, but, there is limited case law on apparent agency in the franchising context.[336] In an early case on franchisor liability

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327. *Id.*

328. Terry & Huan, *supra* note 307, at 13 (emphasis added).

329. *Id.*

330. *Id.* at 14.

331. *Id.*

332. *See id.* (contrasting the difference between the U.S. control test and the Australian authority test for actual agency liability).

333. *See* RUBENSTEIN ET AL., *supra* note 15, at 25 (noting that in Australia control without actual authority is unlikely to satisfy the theory of actual agency in order to hold the franchisor liable for the acts of its franchisee).

334. *Id.*

335. Terry & Huan, *supra* note 307, at 15.

336. *Id.* This dearth of Australian case law stands in stark contrast to the U.S. law, which regularly handles apparent authority cases involving franchisors,

under apparent agency arising in Australia's sister state of New Zealand,[337] *Fitzgerald v. H & R Block*,[338] the New Zealand High Court held that, although the franchise agreement explicitly stated that there was no agency relationship between the parties, the plaintiff sought to establish that the authority bestowed upon the franchisee to trade under the name "H & R Block" amounted to the "holding out" of authority for the franchisee to function as the franchisor's agent.[339] The merits of this argument were not addressed, however, as the court ultimately held that, because the franchisee had used his own corporate letterhead, the plaintiff knew that his dealings were with the franchisee and not with the franchisor; thus, the franchisor was not vicariously liable through apparent agency for the acts of its franchisee.[340]

In response to the great difficulty plaintiffs face in establishing apparent agency, a possible new category of franchisor vicarious liability has surfaced in Australia: the "representative agent test."[341] This intermediate category of representative agent does not fit within either employee or independent contractor standing, but instead falls somewhere between the two and leaves the franchisor subject to

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franchisees, and third party plaintiffs. To provide a sense of how deep such case law is, the author in March 2016 conducted a Lexis search of federal appeals court cases and state supreme court cases (franchis! /50 "apparent authority" or "apparent agency" or "apparent agent" or "agent by estoppel" or "agency by estoppel"), which found, from 1978 to the present, opinions on their merits about a franchisee's apparent authority to act for the franchisor in six of the federal circuits and in eight different state supreme courts. Of course, these high-level cases no doubt are just the tip of the iceberg. The vast majority of federal cases do not reach the level of reported appeals court cases, and very few state cases become state supreme court opinions.

337. Australia and New Zealand share a common law heritage and have strong commercial and legal ties. In franchising, for example, New Zealand simply had a chapter in the Australian-based Franchise Association of Australia & New Zealand until 1996, when the Franchise Association of New Zealand was formed. *Our History*, FRANCHISE ASS'N OF NEW ZEALAND, (http://www.franchiseassociation.org.nz/our-history.html) (last visited Jan. 23, 2017) [https://perma.cc/9AU3-G4LA] (archived Jan. 23, 2017); *see* Owen Wright & Andrew McAuley, *Australian Franchising Research: Review, Synthesis and Future Research Directions*, 20 AUSTRALASIAN MARKETING J. 158, 158–59 (2011) (noting the formation of the Franchisors Association of Australia in 1981 and that in 1993 this association extended membership to include franchisees and was renamed the Franchise Association of Australia and New Zealand (FAANZ); after New Zealand formed its own association, FAANZ became known as the Franchise Council of Australia in 19 in 1998).

338. This is an unpublished judgment from June 1990 noted in, among other sources, Steward Germann, *New Zealand – Termination of Master Franchise Agreements and the Consequences*, 5 J. INT'L FRANCHISING & DISTRIB. L. 37. (2007); Michael Raine & Belinda Atkinson, *Franchisor Liability for Franchisee Misconduct*, FRANCHISING UPDATE, n.7 and accompanying text (June 2007), http://www.dibbsbarker.com/publication/Franchising_Update_June_2007.aspx [https://perma.cc/2E5E-BS37] (archived Jan. 23, 2017).

339. *Id.*

340. *Id.*.

341. RUBENSTEIN ET AL., *supra* note 15, at 8.

vicarious liability.[342] Under this minority approach, vicarious liability can be found where an independent contractor is a representative, meaning that it executes the franchisor's functions and furthers its economic interests, effectively as part of its enterprise.[343] Thus, if a franchisee is furnished with the authority to act as the franchisor's representative, the franchisor should be liable for its franchisee's negligence to contractors acting within the scope of that authority.[344] If this minority view were adopted more broadly, the application of vicarious liability in Australia would balloon and likely encapsulate many more franchisor-franchisee relationships.[345] However, this is not the current law in Australia, as the majority of courts have held steadfast in the application of the traditional multi-factor, totality of the relationship test.[346]

IV. CONCLUSION

International franchise law remains unsettled. The rapid growth of franchising worldwide,[347] particularly in legally distinct but economically integrated regions, such as North America (with federal nations such as Canada and the United States) or Europe (with the quasi-federal structure under the European Union), has created an international need for streamlined, predictable and understandable franchising law over various jurisdictions. This challenge has been met with international principles and agreements that provide a better understanding of international franchising standards, as well as a model with which to clarify and reconcile different domestic approaches to franchising and liability.[348]

For example, Rome I offers a method for regulating civil and commercial obligations when there is a conflict of laws in the franchise context.[349] Similarly, the UNIDROIT Guide and its amendments provide clarity as to when an agency relationship is formed between a franchisor and franchisee,[350] how a franchisor may limit vicarious liability and seek indemnity from franchisees for torts,[351] and why franchisors should have liability insurance and require their sub-franchisors and franchisees to do the same.[352] In addition, the Guide discusses the implementation of franchise-specific legislation to

342. Terry & Huan, *supra* note 307, at 18.
343. RUBENSTEIN ET AL., *supra* note 15, at 8.
344. *Id.*
345. Terry & Huan, *supra* note 307, at 20.
346. *Id.*
347. *See supra* notes 1–8 (detailing the increased prevalence of franchising practices).
348. *See supra* notes 60, 77, 110, 111 and accompanying text.
349. Rome I, *supra* note 78, at art. 1.
350. Master Franchise Guide (2007), *supra* note 112, at 170.
351. *Id.* at 171, 173.
352. *Id.* at 175.

streamline franchise law.[353] An example of this type of legislation is the Block Exemption Regulation on Vertical Restraints.[354] Legislation such as this and others will continue to impact how franchises operate in Europe and provide a model for our domestic franchise laws.

Yet, even with Rome I and the UNIDROIT Guide, it is readily apparent that different states have divergent approaches to franchising standards. At one end of the spectrum, civil law countries such as France, Italy, and Germany focus more on the reasonable expectations of consumers when determining the vicarious liability of franchisors.[355] At the other end, common law countries, including the United States and Australia, concentrate more on the extent of the control a franchisor has over its agent franchisee when deciding the extent of a franchisor's vicarious liability.[356] An in-depth analysis of each of these civil and common law countries reveals that, whether the focus is on consumer expectations or the level of control, the area of law concerning franchisor's vicarious liability is both complex and unsettlingly diverse.

Through this analysis of different countries' laws the Article also brings the newer, emerging approaches of franchise liability to the attention of international franchise law scholars. One of these innovative developments is the representative agent concept sometimes followed in Australia, where a franchisor may be liable for the negligence of its franchisee so long as the franchisee acted within the scope of franchisor-granted authority.[357] This concept has the effect of making the franchisor a guarantor for any tort liability debt that the franchisee incurs to a third party.[358] If the franchisee does not have the assets to pay a tort judgment against it, the franchisor-as-guarantor acts as a surety and "picks up the bill" for the franchisee. Yet, beyond tort liability debt, the franchisor would not be liable unless the typical forms of actual or apparent agency are present.[359]

Implementing this representative agent model in the United States may result in increased legal vulnerability for franchisors, but such exposure can easily be curbed if the franchisor establishes a distinction between itself and the franchisee. To ensure this separation, a franchisor would want to distinguish itself by notifying customers, suppliers, and other third parties of its independent

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353. *See id.* at 281 (listing legislative techniques to increase franchisor-franchisee disclosure to develop franchise law).

354. *Id.* at 303–04.

355. RUBENSTEIN ET AL., *supra* note 15, at 26.

356. *See id.* at 9 (identifying the importance of control in Common Law regimes).

357. *Id.* at 8.

358. *See id.* ("If [this practice] were to prevail, the risk to franchisors of vicarious liability for the acts of their franchisees in Australia would increase significantly").

359. *Id.*

status.[360] This would serve as a protection for the franchisor, because, without justifiable reliance on the appearance of agency, a third party would not be able to sue the franchisor directly or obtain a judgment against the franchisor.

Protection could also be implemented in the form of a mandated warning,[361] which franchisees would have to make to any third parties with whom they interact; this is similar to the law in France that requires notice to franchise customers about the true owner of the enterprise from which they are purchasing a good or service.[362] Under this regime, misplaced reliance on an apparent agency would no longer be justified.[363] Indeed, in website business, marketing best practices call for elaborate upfront declarations of information.[364] Thus, every franchised outlet should have to post the name of that outlet's owner prominently, on all major business communications, including advertisements, websites, storefront signs, and contractual documents. At the very least, these communications should indicate that a particular franchised business is not the same as the franchisor itself. Examples might include the following: P & D's Subway®; Suburban Valley LLC Hampton Inn; and Anytime Fitness of North Florida, Independent Proprietors.[365]

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360. *See* BEYER, *supra* note 22, at 8 ("In the absence of any notice (or sufficient notice) to the public that the franchisee outlet is independently operated, the risk of apparent agency is heightened"). Such a franchisor still might be a surety under the representative agent concept, despite efforts to limit liability. This point is discussed *supra* notes 339–44, 355–57 and accompanying text.

361. The warning should be a requirement that franchisees must meet and that franchisors could be expected to monitor as a matter of self-interest. Such requirements are already standard fare for local governments needing to be able to have contact information for property owners of leased business premises. *See* CITY OF ST. PETERSBURG CODES COMPLIANCE ASSISTANCE DEPT., LEGAL PREMISES AGENT DESIGNATION FORM, http://www.stpete.org/codes/docs/LEGAL_PREMISES_AGENT_DESIGNATION_FORM.pdf (last visited Jan. 22, 2017) [https://perma.cc/6EHA-8TZW] (archived Jan. 22, 2017) (a form St. Petersburg, Florida meant "to ensure that a responsible person can be readily contacted about the condition of a building, the City Code Chapter 8, Section 8-99 requires that all owners of *non-owner occupied buildings* within the City appoint and designate an individual").

362. RUBENSTEIN ET AL., *supra* note 15, at 14; *see supra* notes 225–29 and accompanying text.

363. Indeed, as the leading commentator on French franchise and distribution law has opined, apparent authority in the franchising context simply is not a serious issue in French law, courtesy of the Neiertz Decree notice (*supra* notes 225-229 and accompanying text). Interview with Didier Ferrier, Prof. of Law (emeritus), Univ. of Montpellier (Fr.), in Montpellier, France (June 5, 2014).

364. *Guidelines for representing my business on Google*, GOOGLE https://support.google.com/business/answer/3038177?hl=en (last visited Jan. 22, 2017) [https://perma.cc/6EJU-K2R7] (archived Jan. 22, 2017).

365. *See* Emerson, *supra* note 231, at 669 (giving similar examples of franchisee business names that inform others of the business' independent ownership and operations, which in turn should "render the franchisor—who ought to be directly named—not liable for the acts or omissions of the franchisee.")

To ensure that these warnings are effective, franchisors would have a statutory duty to monitor their design and display. As a matter of fairness, and to ensure that the franchisor oversees these matters thoroughly, the franchisor's supervisory obligation would not create or even implicate franchisor vicarious liability; any liability would stem solely from direct, franchisor responsibility for a franchisee's actions or inaction. In other words, franchisor actions (whether too much or too little) that fail to notify effectively the franchisee customers about the true business ownership could only lead to statutory liability for these franchisor failures and any provable, direct consequences thereof.[366]

In addition, if the business ownership notification requirement included a high statutory damages provision, this should have the salutary effect of coercing obedience from franchise systems. The law would speak to the sophisticated parties (franchisors) for whom compliance would be essentially a one-time decision to adopt policies and controls.[367] With a statute or regulation announcing that violations are serious and subject to cumulative, aggregated charges (e.g., daily penalties per customer in a possible class action suit), compliance should become an easy decision for franchisors. That is, it should incentivize the adoption of policies and controls which are easy to implement system-wide to avoid not just vicarious liability actions but, more immediately, statutory penalties.[368] Vicarious liability has been implemented for other business relationships and franchising contexts. In the Australian state of Victoria, liability is imposed on the principal in a real estate relationship (the franchisor) when its agent (the franchisee) acts negligently or commits fraud.[369] Likewise, in Israel, the court followed a similar agency approach for a case where property holders sued a real estate franchisor and its franchisee realtor. The Israeli court undoubtedly would have found franchisor liability for franchisee negligence or fraud. However, agency theory did not warrant liability because the franchisor was never informed about

366. Monitoring receipts or other communications from a franchised enterprise to its customers has been considered in light of a federal statute. A restaurant customer brought a vicarious liability claim against franchisor Denny's due to the franchisee's failure to comply with the credit or debit card receipt duties of the Fair and Accurate Credit Transactions Act of 2003, 15 U.S.C. § 168(c) (2006) (FACTA), In its provisions mandating the truncating of electronically generated credit card numbers on receipts, FACTA provides that "no person that accepts credit cards or debit cards for the transaction of business shall print more than the last 5 digits of the card number or the expiration date upon any receipt provided to the cardholder at the point of the sale or transaction." 15 U.S.C. § 1681(c)(g)(1) (2006). *See also* Patterson v. Denny's Corp., No. 07-1161, 2008 U.S. Dist. LEXIS 6747, at *1 (W.D. Pa. Jan. 30, 2008) (the court denied Denny's motion to dismiss on the grounds that if the franchisor controls the software for printing receipts in franchisee stores, then franchisor could be liable for a FACTA violation).

367. Samuel L. Bray, *Announcing Remedies*, 97 CORNELL L. REV. 753, 782–85 (2012).

368. *See id.* at 783–84 (discussing the severity of statutory sanctions, such as those in the Right to Financial Privacy Act).

369. Interview with Andrew Terry, *supra* note 96.

the details of its franchisee's work, and thus the franchisor could not have known about any negligence or intentional wrongdoing.[370] Finally, the liability can extend to other activities: for example, under Spanish law, franchisors can be held liable when the advertising of their products leads the consumer to believe they are the enterprise the consumer is dealing with.[371]

The expansion of these approaches to the franchising context, through the representative agent approach or something similar, would expand liability for franchisors and protect consumers in a broader way than existing agency principles. This is especially important to consider in the tort liability context (e.g., for defective products), where a tort victim may be unsuccessful in recovering from an insolvent franchisee.[372] Still, where the franchisee is insolvent, a plaintiff will have to prove traditional actual or apparent agency in order for the franchisor to be held vicariously liable.[373]

Some countries have already circumvented this tort concern as well. In Lithuania, when end-users buy goods from a franchisee, their products liability suits may hold the franchisor liable for defective (unsafe) products, for otherwise poorly made products, or for inferior servicing of products; the franchise agreement cannot insulate the franchisor from this franchisor-franchisee joint liability.[374] Similarly, in Portugal, a franchisor can be held liable when a consumer suffers injury "from a product defect or a misconception of know-how" regarding the brand.[375] Perhaps most broadly, Malaysian courts have held the franchisor vicariously liable when the franchisee is using the franchisor's trademark.[376]

As demonstrated earlier in this Article, in the context of German law, the focus is no longer on whether the franchisor instructs a franchisee how to do this job, but is on the possibility that the

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370. *See* Peggy Sharon & Inbal Natan-Zehavi, *Israel*, *in* INTERNATIONAL FRANCHISING, *supra* note 12, at ISR/1, ISR/7 (citing *Guy Ovadia v. Anglo Saxon & Others*, No. 2313/03, 2007 CA (CA 31 July 2007). In *Guy Ovadia*, the franchisee realtor acted negligently toward her clients (the plaintiffs) by never posting "for sale signs" and selling the clients' property for $165,000 when their requested price was about $240,000). The Israeli Magistrate Court held that the brokerage agency (the franchisor) was not liable to the franchisee's clients, under any agency theory (presumably, an actual authority claim) because (1) the franchise agreement placed liability for damages on the franchisee, and (2) the franchisor never knew about the details of the franchisee's work for the plaintiffs (her negligence toward the plaintiffs). *Id.*

371. RUBENSTEIN ET AL., *supra* note 15, at 14.

372. RESTATEMENT (THIRD) OF TORTS: PROD. LIAB. § 1 cmt. e (1998).

373. RUBENSTEIN ET AL., *supra* note 15, at 14.

374. Paulius Markovas & Rita Kambleviciene, *Lithuania*, *in* INTERNATIONAL FRANCHISING, *supra* note 12, at LIT/1, LIT/15 (citing Article 6.773(1)–(2) of Lithuania's Civil Code).

375. Magda Mendonça Fernandes, Mónica Pinto Candeias & Filipa Correia da Silva, *Portugal*, *in* INTERNATIONAL FRANCHISING, *supra* note 12, at POR/1, POR/9.

376. Baskaran, *supra* note 183, at MAY/12.

franchisor is able to control the franchisee's actions.[377] This focus has shifted because of the broad umbrella of apparent agency, which usually views the franchise relationship from the viewpoint of the consumer, similar to the "agent representative" approach. Both approaches support the extension and expansion of possible franchisor liability from the public policy rationale that consumers have a right to expect that control has been or is exercised if the franchisor could exercise that control. By establishing a franchise system, a franchisor can easily be hauled into court or be expected to pay a judgment through the doctrine of apparent agency, which leaves a lot of guessing as to whether liability will be found after evaluating the facts and circumstances. The representative agent approach would differ in that the franchisor could always plan ahead and build a reserve in the event of tort liability incurred by the franchisee.

Divergent franchising standards exist and are likely to endure between states in the United States, thus domestic legislators would be well served to examine these international franchising approaches and clarify and reconcile the nation's various approaches—regulatory and judicial—to franchising liability. While the likelihood of international fluidity in franchise laws is remote, continuity in franchise laws across the United States is not impossible. Uniform laws have been established in other areas of law (e.g., contract law) and can serve as an example for uniform franchise laws. In observing international franchising approaches, legislators will ensure that franchise law will not vary so widely across domestic jurisdictions. The result of disputes will be more predictable, and franchisors, as well as franchisees, will benefit from a better understanding of the legal consequences of their decisions.

377. GILIKER, *supra* note 209, at 66–67.

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