THE FRANCHISE RELATIONSHIP AND ALLEGED DISCRIMINATION IN CONTRACT TERMS OR ENFORCEMENT: RUMINATIONS ON "SIMILARLY SITUATED" FRANCHISEES, ANALOGOUS FEDERAL LAW, AND OTHER CONCEPTS

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I. Introduction

This article discusses the various approaches taken by the states, the courts, and the federal government in dealing with franchise discrimination and suggests how franchisees might go about prosecuting a successful claim of franchise discrimination. The content will thus be beneficial to both franchisors and franchisees, but also to legislatures, who should take heed and implement statutory guidelines for whether a valid discrimination claim exists. The article will start by analyzing the two requirements that a franchisee must meet in order to successfully bring a valid discrimination claim: (1) the franchisee must be similarly situated to other franchisees; and (2) the franchisor's disparate treatment of the franchisee must relate to a material aspect of the business operation. The article will continue by discussing several states' statutory provisions dealing with franchise discrimination and lastly will address other claims that franchisees may bring, alternative to those that the statutory provisions provide.

As for the federal approach to the issue, only two U.S. industries, petroleum and automobile dealerships, have federal statutes that provide substantive laws regarding the relationship between franchisor and franchisee.[1] Thus, a franchisee may bring an action under federal law only in some contexts. The recourse for a franchisee within a specific state may vary. In some states, a franchisee may be able to bring a cause of action for franchise discrimination because the state legislature has enacted express legislation creating the cause of action.[2] Lastly, a franchisee may allege a general breach of the implied covenant of good faith and fair dealing, which is implied by most states into all contractual agreements.[3]

The relationship between franchisor and franchisee is generally governed by the terms of the franchise agreement and the often-complex operations' manual provided to the franchisee by the franchisor.[4] The manuals, and sometimes other specification documents,[5] establish standardized procedures for the operation of the franchise, thus ensuring continuity of the brand across franchise locations.[6] This goal permeates franchise agreements, as franchisors generally maintain similar contractual terms among all of their free franchisees.[7] While franchisors' analogous agreements can create consistency within a franchise network, they also expose franchisors to discrimination claims by franchisees when franchisors do not consistently apply the agreement or manual between franchisees. Contract terms could be considered boilerplate and disregarded by a court if the franchisee reasonably relied on past interactions with the franchisor that gave an impression their relationship would function in a way contrary to the language of the agreement.[8]

For example, under Minnesota state law, a court found that the franchisor had discriminated against a franchisee when it unreasonably withheld consent for transfer of the

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[1] *See infra* Part IV.
[2] *See infra* Part III.
[3] *See infra* Part IV.
[4] Mark J. Burzych & Emily L. Matthews, *Vive la difference? Selective Enforcement of Franchise Agreement Terms and System Standards*, 23 FRANCHISE L.J. 110, 110 (2003).
[5] E.g., Policies and forms concerning site development, hiring procedures, advertising, or insurance.
[6] *Id.; see also* Robert W. Emerson, *Franchise Terminations: Legal Rights and Practical Effects When Franchisees Claim the Franchisor Discriminates*, 35 AM. BUS. L.J. 559, 593 (1998) (discussing the verbiage and effect of an operations manual as incorporated in the franchise agreement).
[7] Burzych & Matthews, *supra* note 4, at 110.
[8] *See infra* Part II.

franchise and it refused to consent to the franchisee's selling of the franchise.[9] The discriminatory aspect came into play when the franchisee presented evidence that similar applications of fourteen other franchisees had been approved by the franchisor. A second example of franchise discrimination would be if a franchisor were to enforce performance quotas against some franchisees but not against others.[10] As these examples show, franchise discrimination can occur in various contexts and is exemplified by the franchisor treating one franchise differently than others.

II. Elements of Franchise Discrimination

A. "Similarly Situated" - Discretionary Approach

While not defined statutorily, discrimination can be interpreted to mean differences in the way franchisors treat similarly situated franchisees with regard to a material aspect of the franchised business.[11] Due to the inherent ambiguity of the terms "similarly situated" and "material aspect," courts have exercised broad discretion in determining whether different treatment among franchisees constitutes discrimination. For example, in *Implement Service, Inc. v. Tecumseh Products Co.*, the court acknowledged that "whether a plaintiff/franchisee is 'similarly situated' to other franchisees will, of course, depend on which factors about the franchisees are compared."[12] While a seemingly obvious statement, the court acknowledged the disparate application of the term "similarly situated" and the resulting inconsistent effect when varying factors are considered.[13] The court conveyed that if there is insufficient evidence for a franchisee to demonstrate a prima facie case that it is similarly situated with other franchisees who are being treated more favorably, then the claim will proceed no further.[14] In this case, the franchisee had sought an injunction against the discrimination against it, such that it would be subject to the same standards in maintaining its franchise location as similarly situated franchisees.[15]

A venerable post-Civil War enactment in the U.S. Code, 42 U.S.C. § 1981,[16] has been interpreted to require that similarly situated franchisees receive equally advantageous treatment, free of racial discrimination. In *Elkhatib v. Dunkin Donuts, Inc.*, the court addressed a § 1981 claim and evaluated whether multiple franchisees were similarly situated, while suggesting that the requirement "should not be applied mechanically or inflexibly, but rather is a common-sense flexible inquiry that seeks to determine whether there are enough common features between the individuals to allow a meaningful comparison."[17] In *Elkhatib*, the franchisee, Elkhatib, a Palestinian Arab of the Muslim faith, had operated multiple Dunkin Donuts franchise locations

[9] Burzych & Matthews, *supra* note 4, at 116.
[10] Edward R. Spalty & Todd C. Ditus, *Risky Business: Franchise Terminations for Failure to Meet Performance Quotas*, 6 FRANCHISE L.J. 1, 21 (1987).
[11] W. MICHAEL GARNER, FRANCHISE AND DISTRIBUTION LAW AND PRACTICE § 10:49 (2014).
[12] Implement Serv., Inc. v. Tecumseh Prods. Co., 726 F. Supp. 1171, 1181 (S.D. Ind. 1989) (holding that an equipment seller, who had been enlisted as an authorized service distributor by manufacturer's central warehouse distributor, did not have a discrimination claim for contract termination, based in part on its failure to prove that it was similarly situated to those franchisees being treated more favorably).
[13] *Id.* (considering the factors "relevant to the underlying business decision being made").
[14] *Id.*
[15] *Id.* at 1175.
[16] 42 U.S.C.A. § 1981 (West 2012).
[17] Elkhatib v. Dunkin Donuts, Inc., 493 F.3d 827, 831 (7th Cir. 2007).

beginning around 1979.[18] Five years later, Dunkin Donuts began to offer a line of breakfast sandwiches, which the franchisee refused to offer at his franchise locations for the religious purpose of declining to sell pork products.[19] In 2002, the franchisee requested a relocation of his franchise operations to a "prime" location; Dunkin Donuts denied the application for relocation because of the franchisee's failure to carry Dunkin Donuts' full line of breakfast sandwiches.[20] The franchisee then filed suit, alleging that the refusal to allow him to relocate or renew his franchises based on his religious choice not to sell pork products constituted racial discrimination.[21]

The court found that the franchisee failed to establish that he could perform his obligations under the franchise contract because he was unwilling to serve the full line of products, and that there were no similarly-situated non-protected individuals treated more favorably.[22] The court further stated that only "substantial similarity, not complete identity, is required."[23] The key common features between the Elkhatib and the franchisees he claimed to be substantially similar to were that they each failed to carry all or part of the breakfast line of products at their franchise locations, despite their franchise agreement requiring them to do so, and they were all franchisees of Dunkin Donuts located in Chicago.[24] The court found Dunkin Donuts' argument, that the other franchisees that plaintiff compared himself to were granted permission not to carry the breakfast line for non-similar purposes, persuasive; for example, one location was not able to carry the line because they did not have space in the franchise location to install the oven required to serve the products.[25] The interpretation of § 1981 above was of the statute's textual mandate that:

> All persons within the jurisdiction of the United States shall have the same right in every State and Territory to make and enforce contracts, to sue, be parties, give evidence, and to the full and equal benefit of all laws and proceedings for the security of persons and property as is enjoyed by white citizens, and shall be subject to like punishment, pains, penalties, taxes, licenses, and exactions of every kind, and to no other.[26]

If the standard set forth in *Elkhatib*, relating to racial discrimination against similarly situated franchisees under § 1891, is applied more broadly to encompass any discriminatory action – such as actions by franchisees against franchisors for applying different standards to their particular franchise location, but not for racial reasons – courts would have increased power to consider varying factors when evaluating whether franchisees are similar enough to permit a useful comparison of franchisor treatment. Even if the courts addressing selective enforcement discrimination claims have not explicitly stated that they are applying this broad, flexible standard rather than a set rule, it is clear from their application that courts can consider many factors applicable if highly context specific. When a standard is applied broadly in some contexts, narrowly in others, and in a way where different factors may be accounted for in only

[18] *Id.* at 828.
[19] *Id.*
[20] *Id.*
[21] *Id.* at 829.
[22] *Id.* at 830.
[23] *Id.*
[24] *Id.*
[25] *Id.*
[26] 42 U.S.C.A. § 1981 (West).

certain contexts, it is difficult for litigants to craft appropriate arguments and, in attempting to avoid a lawsuit, for franchisors to decide which franchisees will be classified as similarly situated. For example, in *Wisconsin Music Network, Inc. v. Muzak Ltd. Partnership*, similarly situated franchisees were defined as "those whose previous contracts had expired," as it was the expired status that was the common thread among franchisees treated differently.[27] In a separate context, in *Implement Service*, the geographical status of franchisees was the key factor in determining whether the franchisees were similarly situated because the discrimination claim involved allocations that were "driven by considerations of geography."[28] Whereas in cases like *Elkhatib*, the fact that franchisees were all located in Chicago did not mean that they were similarly situated. Therefore, in every discrimination claim, the court has wide discretion to apply factors pertinent to determining whether franchisees are similarly situated, similar to the discretion used in *Elkhatib*.

This focus on whether franchisees are similarly situated may lead to a single-mindedness that overlooks the discrimination when a non-franchised unit within the network is favored over franchised units; that is, the court may only consider the treatment that is given to other franchisees, rather than non-franchised units that are also a franchisee's competitors. For example, even if a store is company-owned rather than franchised, disparate treatment may be present in that the two stores (franchised and company-owned) are treated differently. Thus, the courts should also consider how franchisors treat their own stores in determining whether the terms of a franchise agreement are actually discriminatory. The conditions a franchisor imposes on its franchisees ordinarily must not be more severe than those requirements placed on the franchisor's company-owned units. For example, the Rolex Company was not permitted to compel its jewelry store franchisees to install a repair shop when Rolex did not impose that mandate on its own stores.[29] Likewise, a distribution contract in which the manufacturer compelled the distributor to offer advice and assistance to consumers, but did not do so for its own sales force that developed mail orders, was found to be wrongful discrimination.[30]

A case-by-case analysis considering franchised and company-owned locations alike would provide flexibility for courts and benefit the franchisee because it would allow courts to be creative in finding a way to meet the "similarly situated" requirement described above. It has already been demonstrated how courts tend to apply a variety of factors in conducting the similarly situated analysis, so that a state statute's requirement that courts consider one more would not be a burden on the court system. A court's consideration of this factor will also enhance a franchisee's ability to prove it has been discriminated against if all of the system's locations nearby are company-owned, rather than franchised. The impact of discrimination

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[27] Wis. Music Network, Inc. v. Muzak Ltd. P'ship, 5 F.3d 218, 221-24 (7th Cir. 1993).

[28] *Implement*, 726 F. Supp. at 1181 (holding that the alleged discrimination arose out of certain franchisor allocations on the basis of geography, and hence the inquiry about whether the franchisee was similarly situated to others was to be determined by looking at the geographic relationship between the plaintiff-franchisee and the other franchisees who had been treated more favorably).

[29] Cour de cassation [Cass.] [supreme court for judicial matters] com., Oct. 26, 1993, Bull. civ. IV, No. 91-21931 (Fr.).

[30] Professor Didier Ferrier, the foremost commentator on French distribution law, refers to a holding from a lower court in Limoges, France. Didier Ferrier, The Use of Uniform Criteria for Selecting Outlets Under EU Competition Rules and Their Impact on the Members of the Network, Address at the International Distribution Institute / International Chamber of Commerce Joint Conference, Current Developments in International Contracts Law (June 16-18, 2011), *available at* http://www.idiproject.com/docs/user/NIL/2011/materials/13-Ferrier.pdf, at 2.

among franchisees is comparable to the impact of a franchisee being treated less favorably than a company-owned store.

B. "Similarly Situated" – Guided Approach

An obvious drawback to such a broad standard is the potential for inconsistent application of the term "similarly situated," as described in the preceding Section. If the factors to be considered vary widely within each discrimination claim, the probability of a plaintiff-franchisee's success likely will fall, as the franchisor probably can put forth justifiable reasons for the differences in treatment.[31] The plaintiff's success is further thwarted by the difficulties it faces in pleading its case about how other franchisees are similarly situated.

One way to address this problem would be for legislatures to establish statutory guidelines that enumerate certain factors that courts could evaluate in each claim. For example, the state legislature could provide a list of factors for courts to consider in determining whether a franchisee is similarly situated to another. That list of factors can be exclusive and only provide for a certain list of factors that will satisfy "similarly situated." Or the list of factors can be non-exclusive and include a catchall provision, which would allow courts to consider extraneous factors in special circumstances. Then the state legislatures can adapt and modify the factors as necessary to adapt with changing times. If the state legislature does not act to implement this type of guided approach, judges themselves could analyze a certain set of factors in each discrimination lawsuit by a franchisee.[32] If courts followed these guidelines (statutory or judicially created), thus evaluating the same or similar factors in each lawsuit for discrimination, the franchisor would likely struggle to establish a justifiable reason for the discrimination, as it would not have the ability to persuade the court that there were factors more important to the operation of the franchise than those alleged by the franchisee. At the very least, this type of guidance would ensure that the courts consider certain factors for each plaintiff, which may be an impetus or strategy to the franchisee bringing the claim.

Even if courts did not follow established guidelines in considering whether franchisees are similarly situated, the standardized terms that franchisors tend to employ in franchise contracts and operation manuals may alone be sufficient for courts to characterize all members of a single franchise as similarly situated. However, while in many cases courts may consider the franchisor's use of standardized terms, courts likely will not apply the factor to all cases, because franchisors typically maintain the right to adjust the contractual terms among franchisees, except for in limited exceptions involving the Petroleum Marketing Practices Act (PMPA). For example, under the PMPA,[33] a federal law dictating many of the terms of the franchisor-franchisee relationship for gasoline service stations, franchisors are not required to make the terms of a franchisee's new franchise agreement identical to all other franchise agreements a franchisor has with other franchisees.[34] The PMPA "only requires that the franchise terms be similar, i.e., not discriminatory, to other franchises currently in effect or currently being offered by the purchasing franchisor."[35] In the international arena, Egypt does actually require that a

[31] Emerson, *supra* note 6, at 572.
[32] Robert W. Emerson, *Franchise Terminations: Good Cause Decoded*, 51 WAKE FOREST L. REV. __ (2016 forthcoming).
[33] 15 U.S.C. §§ 2801-2807, 2821-2824, 2841 (2007).
[34] Unocal Corp. v. Kaabipour, 177 F.3d 755, 767 (9th Cir. 1999).
[35] *Id.* (quoting S. Nevada Shell Dealers Ass'n v. Shell Oil Co., 725 F. Supp. 1104, 1109 (D. Nev. 1989)).

franchisor use an identical form contract for all of its franchisees – an approach that would never gain favor in the United States.[36] Additionally, and most important for our analysis, the state statutes that prohibit discriminatory behavior[37] do not specifically provide that a franchisor cannot alter contractual provisions among franchisees.

C. "Material Aspect"

Besides proving it is similarly situated to other franchisees that are being treated more favorably, the plaintiff-franchisee may also be required to address whether the discrimination pertains to a material aspect of the business. This has specific application to claims pertaining to discrimination in the termination of a franchise, as many state statutes provide that termination is only acceptable if the terminated franchisee failed to substantially perform some material aspects of the contract.[38] The same is true under the PMPA, which stipulates in Section 2802(b)(2)(A) that a franchisor cannot terminate the franchise for contract violations "unless the provisions of the contract that were violated are 'both reasonable and of material significance to the franchise relationship.'"[39] Therefore, when asserting that a franchisor has improperly terminated the franchise, a franchisee would be required to prove that there was no failure on its own part to perform the material portions of the agreement.

In determining whether provisions of a contract have been of reasonable and material significance to the franchise relationship under this Section, courts have deemed many provisions as material. For example, provisions requiring a franchisor to report gasoline storage tank meters to the franchisor at the time the price change became effective were reasonable and material to the agreement.[40] A provision stating that a franchisee was to discontinue use of franchise oil company's trademarks if the franchisee cease selling franchisor's motor fuels was also a provision of reasonable and material significance to the franchise contract.[41] Under the PMPA, in determining whether a provision is reasonable and of material significance to the franchise relationship courts use a two-part test. "First, the defendant must show that the determination to include the provision in the franchise agreement was made in subjective good faith. Second, it must appear that the determination was made in the normal course of business."[42] Typically, a court is looking for the franchisor's decision to include the provision to be based on his or her ordinary business experience and knowledge.

III. State Statutory Provisions Dealing with Franchise Discrimination

State statutes relating to franchise discrimination are minimal. Because of this, franchisees face difficulty in raising franchise discrimination claims. For example, assume that

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[36] *See* Egypt, *infra* note 164.

[37] ARK. CODE ANN. § 4-72-204 (West 2012); HAW. REV. STAT. § 482E-6(2)(C) (West 2012); 815 ILL. COMP. STAT. 705/18 (2012); IND. CODE ANN. § 23-2-2.7-2(5) (West 2012); WASH. REV. CODE § 19.100.180(2)(c) (2012); WIS. STAT. ANN. § 135.03 (West 2012).

[38] Emerson, *supra* note 6, at 577 n.69.

[39] Patel v. Sun Co., Inc., 948 F. Supp. 465, 475 (E.D. Pa. 1996) (quoting 15 U.S.C. §§ 2802(b)(2)(A)).

[40] Geib v. Amoco Oil Co., 29 F.3d 1050 (6th Cir. 1994).

[41] Di Napoli v. Exxon Corp., 549 F. Supp. 449 (D.N.J. 1982).

[42] Kurtis A. Kemper, *Cause of Action Against Oil Company Under Petroleum Marketing Practices Act [15 U.S.C.A.§§ 2801 to 2806] for Termination or Nonrenewal of Franchise*, 8 Causes of Action 627 (Originally published in 1985) (citing Gruber v Mobil Oil Corp, 570 FSupp 1088 (ED Mich 1983)).

an aggrieved franchisee, Fran, has sued the franchisor, Copious Company, for discrimination. When a court is presented with Fran's claim that she is being treated worse than other franchisees, the court must first start with a review of the written franchise agreement between Fran and Copious.[43] Presumably, the court would review the listed terms and conditions to determine the most basic of findings: whether the franchisor's alleged behavior contradicts the agreement itself.[44] The court would likely take the terms of the Copious-Fran agreement as well as Copious' actual treatment of Fran, and compare both (the agreement and the treatment) with that of similarly situated franchisees.

Even if the court determines that Fran is being treated differently, though, the court must still decide the legal effect of such treatment, such as whether the differential treatment was relevant or material.[45] This second step is likely to present a challenge for the franchisee because most states do not explicitly forbid franchise discrimination by statute, making it so Fran would need to prove a non-statutory right to relief, such as under a different statutory provision or under common law. In undertaking this analysis, the court would consider any other explanation from Copious as to why its differential treatment of Fran arose from legitimate business concerns. As to what constitutes a "legitimate business concern," courts interpreting the phrase have not provided a steadfast definition, although they have made it clear that the range of franchisor concerns that are encompassed are broader than what would be required for finding good cause in the termination context. One court captured the spirit of this concept: a franchisor is "justified in identifying untapped opportunities or unutilized potential and adjusting its distribution network to realize greater profits When the franchisor demonstrates that its business decision is legitimate and made in good faith… a court should not replace the grantor's decision with its own."[46] This step is thus another potential death knell to the franchisee's claim, as courts have given wide deference to the business rationales offered by franchisors.[47]

When an applicable statute does exist, though, and a franchisee establishes that it is being treated differently than other similarly situated franchisees, the court will look to the statute to determine if the disparity is legally sufficient to constitute discrimination.[48] Courts will evaluate the large majority of claims under state legislation, as there is no over-arching federal statute that applies to all franchise relationships. In fact, only two U.S. industries, petroleum and automobile dealerships, have federal statutes that provide substantive laws regarding the relationship

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[43] *See* Burzych & Matthews, *supra* note 4, at 110.

[44] However, a breach of contract would not be necessary for a plaintiff to prevail. Even if the agreement's express terms permit the discrimination, the discrimination would still be violative of law, public policy, and good faith and fair dealing concepts.

[45] *See infra* Part II (describing the elements that must be met to prove franchise discrimination).

[46] Petereit v. S.B. Thomas, Inc., 63 F.3d 1169, 1185 (2d Cir. 1995); see also Edmands v. CUNO, Inc., No. CV010447171S, 2001 WL 835041, at *7 (Conn. Super. Ct. June 22, 2001).

[47] This deference is demonstrated by courts' application of the business judgment rule to a franchisor's decisions. *See* Robert W. Emerson, *Franchise Encroachment*, 47 AM. BUS. L.J. 191, 266 (2010). *See also* Emerson, *supra* note 6, at 572.

[48] Disparate treatment may not always lead to a successful discrimination claim because the treatment may nevertheless be fair. A franchisee can claim unequal or unfair treatment to prove discrimination, but if the franchisee only claims unequal treatment, and the court agrees but finds that the treatment was fair, the court will not find discrimination. *See* Robert W. Emerson, *Franchise Selection and Retention: Discrimination Claims and Affirmative Action Programs*, 40 ARIZ. L. REV. 511, 523-26 (1998); *see also* Robert W. Emerson, *Franchise Terminations: Legal Rights and Practical Effects When Franchisees Claim The Franchisor Discriminates*, 35 AM. BUS. L.J. 559, 589 (1998).

between franchisor and franchisee.[49] Therefore, if the discrimination claim is not within one of these two industries, the court is left to examine state statutes and any ancillary case law.

Unfortunately for franchisees, while many states have statutes that provide guidance on the franchisor-franchisee relationship, only six states currently have express anti-discrimination provisions: Arkansas, Hawaii, Illinois, Indiana, Washington, and Wisconsin.[50] Even in these states, a franchisee's discrimination claim is not a guaranteed success because: (1) some of the anti-discriminatory statutes only apply to the practice of termination or non-renewal of franchise contracts, instead of a broader range of general behavior; (2) some statutes provide express defenses for the franchisor; and (3) courts have often interpreted anti-discrimination statute provisions against the franchisee.[51] To provide an understanding of this conclusion, the Article reviews the statutes found in the six states mentioned above. Perhaps these anti-discrimination provisions have not been widely adopted by legislatures because they are viewed as unnecessary unless they go beyond the duties of good faith and fair dealing already implied in the contract.

A. The Broadest Anti-Discrimination Provisions: Hawaii, Illinois, Washington, and Indiana

1. Hawaii

Hawaii has perhaps the most expansive anti-discrimination provision of all, as provided within Section 482E-(6)(2)(c) of the Hawaii Revised Statutes Annotated. The provision states in part that it is "an unfair or deceptive act or practice or an unfair method of competition for a franchisor . . . to . . . discriminate between franchisees in the charges offered or made for royalties, goods, services, equipment, rentals, advertising services, or in any other business dealing. . . ."[52] However, despite the section prohibiting discrimination, it does provide several defenses for the franchisor. The section states that such discriminatory actions are prohibited *unless* (1) the franchises were granted at materially different times; (2) the discrimination is related to efforts to cure deficiencies in the operation of the franchises; (3) the discrimination is related to a program that makes franchises available to those lacking certain qualifications; or (4) the discrimination is related to an experimentation with, or variations in, the product or service lines. [53] In addition, the statute provides a broad loophole for franchisors because it permits discrimination "based on other reasonable distinctions."[54]

Therefore, though Hawaii's statute provides an expansive definition of discrimination, its express statutory defenses may reduce the likelihood of a successful action against a franchisor. To avoid a franchisor's taking advantage of these defenses, it would be most advantageous for the franchisee to bring the lawsuit in a state other than Hawaii. Possibly wrongful discrimination but with an almost equally broad set of defenses built into the statute, the typical franchise

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[49] *See infra* Part IV; *see also* Burzych & Matthews, *supra* note 4, at 110-11; Emerson, *supra* note 6, at 562-63.
[50] Burzych & Matthews, *supra* note 4, at 111-13.
[51] *See id.*; *infra* notes 30-68 and accompanying text (concerning, *inter alia*, franchisor defenses to discrimination charges).
[52] HAW. REV. STAT. § 482E-6(2)(C) (West 2012).
[53] *Id.* § 482E-6(2)(C)(i)-(iv). Such exceptions are found in other states, such as Illinois. *Infra* text accompanying note 60. Moreover, it appears to be common internationally. For example, French law also permits such differential treatment based on experimentation. Ferrier, *supra* note 30, at 3 (noting that the franchisor can try "new conditions which could be then applied by the franchisees at a later date").
[54] *Id.* § 482E-6(2)(C)(v).

discrimination case – with perhaps poor behavior on the franchisor's part but *sans* outright, provable malice (e.g., *intentionally* undermining the franchisee's interests) – appears unlikely to succeed in that island state. Hawaii's statute would be more beneficial to franchisees if it punished both intentional discrimination and discrimination evidenced by conduct and a disparate impact. This type of approach is taken with respect to federal employment law, where federal statutes generally prohibit an employer from discriminating,[55] but courts interpret this to include both intentional and disparate impact discrimination.[56] Allowing a franchisee to show either type of discrimination would assist the franchisee who cannot prove the franchisor's intent to discriminate, a piece of evidence typically only in the franchisor's possession, and otherwise would not be able to succeed in bringing a lawsuit under the current requirements of the law.

2. Illinois

Similarly, the Illinois Franchise Disclosure Act stipulates that it is "a violation of this Act for any franchisor to unreasonably and materially discriminate between franchisees operating a franchised business located in this State in the charges offered or made for franchise fees, royalties, goods, services, equipment, rentals or advertising services. . . ."[57] This statute is rather similar to the approach taken by several countries abroad that expressly prohibit a franchisor from engaging in price discrimination.[58] However broad the Illinois statute may be, this statement is immediately followed by two stipulations that limit its application.

First, such discrimination is only a violation of the Illinois Act if it will "cause competitive harm to a franchisee who competes with a franchisee that received the benefit of the discrimination. . . ."[59] Additionally, the Illinois Act provides the same franchisor defenses as listed in the Hawaiian statute: (1) difference in time in which the franchise was granted, (2) part of a program to provide franchises to persons lacking qualifications, (3) related to experimentation or variations, (4) related to efforts to cure deficiencies, or (5) any other reasonable distinction.[60] These defenses make an Illinois lawsuit subject to the same flaws and unlikelihood of success from the standpoint of the franchisee.

3. Washington

The state of Washington's code follows a similar pattern, in which the franchise legislation states that it is an "unfair or deceptive act or practice or an unfair method of competition and therefore unlawful . . . to . . . discriminate between franchisees in the charges offered or made for royalties, goods, services, equipment, rentals, advertising services, or in any other business dealing . . . ."[61] Immediately following the prohibited conduct language, the statute limits the application of the provision by stating that the franchisor can trump the

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[55] 42 U.S.C.A. § 2000e (West).

[56] Duggan v. Local 638, Enter. Ass'n Of Steam, Hot Water, Hydraulic Sprinkler, Pneumatic Tube, Ice Mach., Air Conditioning And Gen. Pipefitters, 419 F. Supp. 2d 484 (S.D.N.Y. 2005) ("A Title VII plaintiff may present statistical findings as circumstantial evidence of intentional discrimination; however, the statistical evidence must be sufficient to create an inference of discrimination.")

[57] 815 ILL. COMP. STAT. 705/18 (2012).

[58] *See infra* Part VII. Comparative Law

[59] *Id.*

[60] *Id.* 705/18(a)(b)(c)(d).

[61] WASH. REV. CODE § 19.100.180(2)(c) (2012).

discrimination claim by proving that the "discrimination between franchisees is: (i) Reasonable, (ii) based on franchises granted at materially different times and such discrimination is reasonably related to such difference in time, or is based on other proper or justifiable distinctions considering the purposes of this chapter, and (iii) is not arbitrary."[62]

As an example of a claim under this state statute, a Washington court determined that a franchisor's offer of lower royalty rates to former franchisees, but not to existing franchisees, did not constitute discrimination under Washington's anti-discrimination statute.[63] The court found that the franchisor had a legitimate business reason for offering the lower rates to former franchisees – to induce the former franchisees to join the new franchise system.[64] The court also pointed out how the franchise systems were established at "materially different times and under different circumstances."[65] This case demonstrates how franchisees are faced with similar obstacles when bringing a lawsuit under a state anti-discrimination statute as they are when bringing a lawsuit under 42 U.S.C. § 1981. Unless a franchisee can show it is being treated differently from other franchisees that were established close in time and under similar circumstances, it seems unlikely that the franchisee will be able to succeed under Washington's statute.

4. Indiana

Indiana's Deceptive Franchise Practice provisions broadly state that it is unlawful for franchisors to engage in the act of "discriminating unfairly among its franchisees or unreasonably failing or refusing to comply with any terms of a franchise agreement."[66] Unlike its counterpart provisions in Hawaii and Illinois, the Indiana provision does not list any defenses. This provision has perhaps the widest reach because it is the least restrictive – that is, it does not have any stipulations. The statute's breadth and lack of enumerated defenses for franchisors makes Indiana a more appealing location for bringing a franchise discrimination claim.

However, even with such a broad provision, courts still appear hesitant to rule in favor of a franchisee's discrimination claim. For example, in *Carrel v. George Weston Bakeries Distribution, Inc.* the court was unwilling to grant a franchisee's motion for summary judgment when the facts indicated that the franchisor had provided different commission rates to various franchisees.[67] The court stated that even if discrimination did occur, it must also be both arbitrary and unfair before it furnishes the franchisee with an actionable claim.[68] Therefore, such a decision weakens the impact of a relatively pro-franchisee statute by allowing franchisors to pursue an extensive set of possible defenses to their allegedly actionable discrimination: as a fallback position once the discrimination itself becomes incontrovertible, the franchisor can still present anything that contributes to showing its actions were pondered or deliberated (not simply arbitrary) and were, in the overall context, just or reasonable.

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[62] *Id.*
[63] Case discussed in 2 FRANCH & DISTR LAW & PRAC § 10:52.
[64] *Id.*
[65] *Id.*
[66] IND. CODE ANN. § 23-2-2.7-2(5) (West 2012)
[67] Carrel v. George Weston Bakeries Distrib., Inc., No. 1:05-CV-1769-SEB-JPG, 2007 WL 2827405, at *26 (S.D. Ind. Sept. 25, 2007).
[68] *Id.*

B. Franchise Discrimination Statutes Limited to Termination or Non-Renewal: Arkansas and Wisconsin

1. Arkansas

Arkansas's anti-discrimination provision is governed by the Arkansas Franchise Practices Act.[69] The statute states, in pertinent part, that it is a violation for a franchisor to "terminate or cancel a franchise without good cause."[70] Good cause is later defined in section 4-72-202(7)(A) as meaning "failure by a franchisee to comply substantially with the requirements imposed upon him or her by the franchisor . . . which requirements are not discriminatory as compared with the requirements imposed on other similarly situated franchisees, either by their terms or in the manner of their enforcement."[71] Therefore, in Arkansas, a franchisee that a franchisor terminated for failure to comply with its franchise requirements could bring a discrimination claim if either the terminated franchisee was compelled to follow certain requirements not imposed on others or was treated differently – i.e., its franchise came to an end while other franchisees acting the same did not suffer that fate. However, courts have found that "good cause" can only be exemplified by the occurrences actually laid out in the statute.[72]

2. Wisconsin

Wisconsin specifically forbids the termination, cancellation or failure to renew a dealership agreement unless there is good cause on the part of the franchisor.[73] The term "dealership" is defined broadly such that it applies to "a contract or agreement…by which a person is granted the right to sell or distribute goods or services, or use a trade name, trademark, service mark, logotype, advertising or other commercial symbol, in which there is a community of interest in the business."[74] The same chapter defines "good cause" as:

> [F]ailure by a dealer to comply substantially with essential and reasonable requirements imposed upon the dealer by the grantor, or sought to be imposed by the grantor, which requirements are not discriminatory as compared with requirements imposed on other similarly situated dealers either by their terms or in the manner of their enforcement.[75]

The court applied this statute favorably to franchisors in *Brown Dog, Inc. v. Quizno's Franchise Co.*, in which the court concluded that "it is not unlawful discrimination for a grantor to consider each dealer's situation and to decide to keep or terminate a dealer based on whether it has met the newly-imposed goals or has failed to do so."[76] The court elaborated by stating that "dealers have no statutory right to insist on identical treatment."[77] In other words, just as in Indiana, the courts in Wisconsin will go beyond the literal wording of the statute and broadly

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[69] ARK. CODE ANN. § 4-72-204 (West 2012).
[70] *Id.* § 4-72-204(a)(1)
[71] *Id.* § 4-72-202(7)(A).
[72] Volvo Trademark Holding Aktiebolaget v. Clark Machinery Co., 510 F.3d 474, 484 (4th Cir. 2007); Volvo Trademark Holding Aktiebolaget v. AIS Const. Equip. Corp., 416 F. Supp. 2d, 404, 412 (W.D.N.C. 2006).
[73] WIS. STAT. ANN. § 135.03 (West 2011).
[74] *Id.*
[75] *Id.* § 135.02(4).
[76] Brown Dog, Inc. v. Quizno's Franchise Co., No. 04-C-18-X, 2005 WL 3555425, at *182-83 (W.D. Wis. Dec. 27, 2005).
[77] *Id.*

apply concepts of procedural fairness (non-arbitrariness) and substantive fair dealing, not simply examine the allegedly flawed franchise relationship for evidence of uneven handling. As a public policy concern, the court's statement that dealers have "no right to insist on identical treatment" flies in the face of the uniformity that franchise networks are intended to convey to their customers, as described in Part V.[78]

C. Choice of Law Concerns

Whenever an area of law is statutorily governed in some states and not others, or whenever an area of law is applied more or less favorably to plaintiffs in certain jurisdictions, it creates a situation in which plaintiffs, or in this case, franchisees, will be tempted to engage in forum shopping or to convince the court to apply the favorable jurisdictions' laws. Forum shopping is when a franchisee purposefully brings its lawsuit in a jurisdiction that has favorable legislation or case precedent to support its claim. However, the ability to take advantage of forum shopping in a preferred jurisdiction is limited. For example, the franchisee will only be able to file a lawsuit in a court that will have personal jurisdiction over the franchisor, which usually requires a showing of sufficient contacts with that jurisdiction or the franchisor's purposefully availing itself of the jurisdiction's laws. If the franchisee is part of a larger franchise system, then establishing personal jurisdiction may be easier; however, other limitations may prevent the franchisee from forum shopping. Many sophisticated franchisors include a choice of law provision in their franchise agreement, selecting the forum's law that is to be applied if a dispute arises out of the franchise agreement or relationship. Since franchisors typically have more bargaining power, the forum will be more beneficial to the franchisor.[79] Choice of law provisions allow the franchisor to avoid being subject to the laws of other states or even United States law altogether if the franchisor selects a foreign forum.[80]

IV. Alternative Claims for the Franchisee

A. Federal Law Structure Related to Franchise Discrimination Claims

If a state statute does not create a cause of action for franchise discrimination, a franchisee will evaluate whether federal law will provide adequate recourse. As briefly described above, only two U.S. industries, the petroleum and automobile dealership industries, have federal statutes in place that provide substantive laws regarding the relationship between franchisor and franchisee. In the United States, there are no uniform federal franchise laws that govern all franchise relationships outside of the petroleum and automobile dealership sectors.

The Petroleum Marketing Practices Act (PMPA) requires a termination or nonrenewal of a franchise agreement be made in a good faith. This good faith requirement attempts to prohibit franchisors from terminating or not renewing franchise agreements based on discriminatory motives..[81] The requirement "permits franchisor to decline renewal of franchise agreement and sell premises, if the determination is made by the franchisor in good faith and in the normal

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[78] *See infra* Part V.
[79] Paul Steinberg & Gerald Lescatre, *Beguiling Heresy: Regulating the Franchise Relationship*, 109 PENN ST. L. REV. 105, 110 (2004).
[80] *Id.*
[81] 8 CAUSES OF ACTION 627 (originally published in 1985).

course of business;"[82] thus, a franchisor's determination will be respected if it can be shown to result from the franchisor's normal decision making process. For example, a franchisor of a gasoline service station satisfied the statutory requirement to act in good faith when it reached the business decision to sell the gas station premises, and as a result, declined to renew the franchise relationship with the franchisee.[83] The court concluded there was no discrimination despite the fact that the bidding process for selling the premises encouraged third parties to include goodwill belonging to the franchisees because the PMPA does not protect against the loss of goodwill and there was no evidence that the business decision of selling the location involved any discriminatory thought processes.[84]

In the automobile dealership industry, franchisor manufacturers are subject to a similar good-faith requirement. Manufacturers will be found liable under the Automobile Dealers Day in Court Act when they have engaged in conduct that has the implicit purpose of being coercive, intimidating, or threatening to a dealer, the franchisee..[85] Automobile manufacturers are frequently found to satisfy this purpose when they acted in bad faith to refuse to deliver or delayed delivery of automobiles. Additionally, courts often find manufacturers liable if they discriminated against a dealer with respect to the number or models of automobiles supplied.[86] However, courts have found that the refusal to allot "fast-selling popular models" and instead loading a dealer with "unsalable models" and "granting competing franchises in an area contrary to alleged oral representations by manufacturer" did not amount to bad faith.[87] Courts also consider the propriety or reasonableness of the franchise agreement provision that the dealer violated. For example, it is not unlawful for a manufacturer to enforce provisions in franchise agreements establishing sales quotas that were found valid or reasonable.[88]

To satisfy good faith under the PMPA, the franchisor need only show that its decision not to renew or to terminate a franchisee be based on a legitimate business reason, which is a low standard to meet and likely insulates franchisors from liability. An additional obstacle for a franchisee attempting to show that the franchisor has not fulfilled its good faith obligations under the PMPA is the fact that courts will strike down the claim if there is no evidence of active discrimination on the part of the franchisor. Since this type of evidence is usually only in the franchisor's possession or rarely reduced to record as it is part of the decision making process, the franchisee's likelihood of proving discrimination is extremely low. The Dealer's Day in Court Act's good faith requirement requires franchisee to prove that the franchisor acted with a coercive, intimidating, or threating purpose, which is a high standard to meet. Ultimately, the claims brought under federal statutes are met with similar hurdles to those brought under state statutes – the franchisees' likelihood of success on the merits of its claim is limited and full of evidentiary hurdles.

B. The Robinson-Patman Act

Despite the limited federal legislation addressing the topic of discrimination in the franchise relationship described above, franchisees have the ability to bring claims arising from

[82] *Id.*
[83] *Id.* (citing BP W. Coast Products LLC v. May, 447 F.3d 658 (9th Cir. 2006)).
[84] *Id.*
[85] 54 A.L.R. FED. 314 (Originally published in 1981). *See* 15 U.S.C.A. § 1222 (West).
[86] *Id.*
[87] *Id.*
[88] *Id.*

allegations of price discrimination prohibited by the Robinson-Patman Act.[89] The Robinson-Patman Act generally prohibits any seller from discriminating among its customers with regards to price if the effect would be to reduce competition among the seller's customers.[90] In the franchise context, a franchisor who sells its products to various franchisees would be prohibited from engaging in price discrimination among them.[91]

A claim for price discrimination by franchisees under the Robinson-Patman Act[92] can be brought by a franchisee that claims that the franchisor sold products at a lower price to other franchisees and non-franchise retailers. However, claims of discrimination by franchisees regarding disparate treatment when compared with the price of products sold to company-owned units are not within the realm of the Robinson-Patman Act.[93] For example, scholars have emphasized this difference as the franchise "may treat its own units disparately, even if they compete with disfavored franchisees."[94]

According to the court in *Mumford v. GNC Franchising, LLC*, this determination is based on the Supreme Court's holding that "a parent and a wholly owned subsidiary are a single economic unit under the Sherman [Antitrust Act, a decision that] has been construed to apply to the Robinson-Patman Act as well."[95] Therefore, a franchisee can only claim price discrimination with regard to disparate treatment among various franchisees.

To bring a successful claim under the Robinson-Patman Act, a franchisee must satisfy eight jurisdictional elements:

> These elements are: (a) the 'discriminator' is a 'person'; (b) the discrimination arises from at least two consummated and contemporaneous sales transactions; (c) the discrimination is by the same seller; (d) the discriminatory sale involves 'commodities'; (e) the commodities are of 'like grade and quality'; (f) the discriminatory transaction involves interstate commerce; (g) there is a difference in the prices that different buyers pay; and (h) there is competitive injury.[96]

If one or more of the above elements is absent, the franchisee's claim will fail regardless of the effect on competition.[97] While the first six elements are generally "present in most franchise price discrimination cases where the franchisor continuously sells products throughout its system," price differential and competitive injury are often more complex elements to prove.[98]

The complexity associated with proving a difference in the prices that different franchisees pay results from the various reasons for which a franchisor may justify selling at

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[89] *See* 15 U.S.C. § 13(a) (2012); *see also* Emerson, *supra* note 6, at 567-68.
[90] PHILIP F. ZEIDMAN & BRET LOWELL, LEGAL ASPECTS OF SELLING AND BUYING § 9:70 (3d ed. 2011).
[91] The Act was created to protect small buyers from being discriminated against by manufacturers or suppliers who favored large buyers. *Shreveport Macaroni Mfg. Co. v. FTC*, 321 F.2d 404, 408 (5th Cir. 1963). Thus, in the franchise context, the franchisee would be the buyer and the franchisor would be the supplier.
[92] 15 U.S.C. § 13(a) (2012).
[93] Stuart Hershman, *Revisiting the Robinson-Patman Act in the Franchise Supply Setting*, 16 FRANCHISE L.J. 57, 77 (1996); *see* Emerson, *supra* note 6, at 567-68.
[94] *Id.*
[95] Mumford v. GNC Franchising, LLC, 437 F. Supp. 2d 344, 360 (W.D. Pa. 2006) (holding that GNC could not be held liable under the Robinson-Patman Act for selling products to company-owned stores at different and lower prices than those sold to franchise stores).
[96] Hershman, *supra* note 93, at 77.
[97] *Id.*
[98] *Id.*

various prices.[99] These defenses arise both from the language of the Robinson-Patman Act and common law interpretations in which prices are subject to change based on "changing conditions affecting the market for or the marketability of the goods concerned."[100] Further, a franchisor can charge different prices to different franchisees if the franchisor can prove that there are differences in the costs of dealing with certain customers.[101]

Establishing competitive injury can be equally challenging for franchisees, as there must be actual, provable injury in order for recovery of damages.[102] If there is only an inference of injury or injury is likely to result, the franchisee can only recover injunctive relief.[103] Additionally, courts have been unwilling to accept inferences of injury if the discrimination is temporary or insubstantial in amount.[104]

Likewise, in some instances, franchisors have insulated themselves from a franchisee's ability to claim competitive injury by imposing territorial or customer restraints in their franchise agreements.[105] These territorial and customer restraints, which are upheld by courts and circumvent anti-discrimination standards, allow the franchisor to impose different standards among its franchisees. Franchisors can use these restraints to circumvent anti-discrimination claims either by showing a legitimate business reasons for them or thwarting the franchisee's ability to prove the "similarly situated" element, as the franchisees are subject to different standards. The effect of these restraints varies depending on how strict the restraint is.[106] It is even possible that a franchisor could sell its products to franchisees at varying prices without having an actual effect on competition; thus, excluding a claim under the Robinson-Patman Act.[107] For example, an actual effect on competition would not arise if the lower or higher price to a particular franchisee reflected the differences in the price of the product in that particular territory in comparison to other territories. In such a situation, it would be challenging for the franchisee to win on its discrimination claim because it could not prove there was actual competitive injury. The price difference would not be an actual injury when comparing the price paid by the franchisee to the cost of living in the area and profits they received. The court determined that the Louisiana Unfair Trade Practices Act limited relief to either personal consumers or business competitors; the franchisee was neither as he did not actually nor potentially engage in a business that competed with the franchisor.[108]

Scholars have also criticized the Act for limiting further the franchisee's power to sue. For example, courts are unlikely to apply a broad definition to the Act's prohibition of discrimination in the "sale of commodities". Courts have routinely held that grants of intangible rights, such as trademark rights or franchise licenses, do not constitute commodities.[109] When courts interpret the Act in this way, it provides a franchisee no recourse under the Act when faced with the clearly discriminatory action by a franchisor: charging different franchisees

[99] *Id.* at 78.
[100] *Id.*
[101] *See id.*
[102] *Id.*
[103] *Id.*
[104] *Id.* at 79.
[105] ZEIDMAN & LOWELL, *supra* note 90.
[106] *Id.*
[107] *Id.*
[108] Id.
[109] LEGAL ASPECTS OF SELLING AND BUYING § 9:70 (3d ed. 2010)

different franchise or license fees.[110] This type of price discrimination can be just as harmful to a franchisee as the price discrimination in tangible goods that the Robinson-Patman Act intends to prevent.

C. Alternative Claims under Unfair Trade Practices Law

Despite the interpretation of the Robinson-Patman Act, many states have enacted statutes that condemn unfair trade practices.[111] These statutes are far more pervasive in terms of the number of states that have enacted them when compared to specific discrimination statutes. However, they may not always provide the recourse hoped for by the franchisee. For example, in Louisiana, a franchisee sued its franchisor, claiming that the franchisor had installed an operating system that made the franchisee over pay certain fees.[112] The finding that a franchisee was not a consumer has also been held in other states, but is not as hopeless as the situation where the state legislature specifically excludes franchisees from bringing a claim for unfair trade practices. Some state statutes limit relief to certain consumers by drafting the definition of a consumer in a way that specifically excludes franchisees as a category.[113]

D. The Implied Covenant of Good Faith and Fair Dealing

Even if a franchisee's discrimination claim is not in accordance with the requirements of either the state statute on point or the Robinson-Patman Act, the franchisee can allege a general breach of the implied covenant of good faith and fair dealing. This covenant is implied in every agreement and requires the parties to treat one another fairly and to not prevent the other party from performing the contract.[114] As stated in *Bonanza International, Inc. v. Restaurant Management Consultants, Inc.*, this requirement is different from requirements that pertain to discrimination in that the disparate treatment of franchisees has no bearing on the performance of the covenant.[115] Therefore, the franchisee could prove a breach of the implied covenant even if the franchisor's dealings with a third party are deemed to be acceptable.

The implied covenant has direct correlation with the good cause requirement listed in many state statutes related to franchise termination. If an implied covenant of good faith and fair dealing is present in the agreement, a franchisor cannot terminate an agreement unless good cause exists.[116] However, this safeguard is limited by the fact that an express provision within the contract can state that a franchisor may terminate the franchise for no cause, in which case the implied covenant no longer has relevance.[117] Additionally, the franchisor's motive can be irrelevant to a determination of good faith if there is sufficient evidence of good cause, regardless of the true intention.[118] This reality has a limiting effect on the good faith and fair dealing requirement in the termination context. Outside of the termination context a franchisee's ability

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[110] Id.
[111] *Id.;* Emerson, *supra* note 6, at 568.
[112] 1 FRANCH & DISTR LAW & PRAC § 7:36.
[113] *Id.*
[114] Burzych & Matthews, *supra* note 4, at 117; Joel Iglesias, *Applying the Implied Covenant of Good Faith and Fair Dealing to Franchises*, 40 HOUS. L. REV. 1423, 1424-25 (2004).
[115] Bonanza Int'l, Inc. v. Rest. Mgmt. Consultants, Inc., 625 F. Supp. 1431, 1447 (E.D. La. 1986).
[116] *See* 62B AM. JUR. 2D *Private Franchise Contracts* § 315 (2012).
[117] *Id.*
[118] *Id.*

to sue on the implied covenant can vary. For example, in a Pennsylvania case, the court determined that the good faith and fair dealing requirement only applied to the termination of the franchise relationship.[119] However, franchisees have been able to challenge the franchisor's good faith and fair dealing compliance in cases involving encroachment and non-exclusivity issues, and operational decisions.[120] Of course, in all contexts, the covenant will not be applied in a way that would override or modify the terms of the franchise agreement.[121] Thus, if the franchisor's discriminatory action or termination decision was in compliance with other terms of the franchise agreement, such as an open-ended clause granting franchisor discretion in these acts, the implied covenant likely will not be able to save the franchisee.

Even apart from the application to franchise termination, the implied covenant of good faith and fair dealing has limited relevance to claims against franchisors. Specifically, the implied covenant cannot override any express terms written into the franchise agreement.[122] Therefore, franchisor behavior that may be in opposition to the good faith and fair dealing requirement is likely to be permitted by a court if it is in accordance with the contractual conditions. Additionally, most courts have held that the implied covenant does not create a separate cause of action if breached and does not create an individual, substantive right.[123] Therefore, a franchisee's claim for a franchisor's failure to comply with the covenant would have to be based on lack of good faith or a breach of a specific contractual provision,[124] but does not have to pertain to bad faith in accordance with express contractual terms.[125]

Lastly, not every jurisdiction recognizes the implied covenant of good faith and fair dealing.[126] Therefore, as with the state statutes pertaining to discrimination, a franchisee may have a low chance of success bringing a claim of bad faith against a franchisor if the jurisdiction does not recognize the requirement of fair dealing. However, despite its limitations, some argue that the implied covenant of good faith and fair dealing logically extends to the franchise relationship, as the franchise agreement is nothing more than a contract.[127] According to the Restatement (Second) of Contracts, all parties to an agreement have a duty of good faith and fair dealing in its performance.[128] Because this provision applies to all contracts, it should follow that the covenant is implied in all franchise agreements.[129]

E. Preclusion of Third-Party Beneficiary Claims

Under general contract law principles, a third-party beneficiary may have a right to enforce a contract even though the individual is not a named party of the contract.[130]

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[119] Keshock v. Carousel System, inc., 2005 WL 1198867 (E.D. Pa. 2005).
[120] W. Michael Garner, *Good-faith Dealing-In General*, 2 Franch & Distr Law & Prac § 8:25 (September 2014).
[121] *Id.*
[122] *Id.*
[123] Iglesias, *supra* note 114, at 1439-40
[124] *Id.*
[125] The implied covenant of good faith and fair dealing may not always be helpful to litigants, though. For example, in California, the District of Columbia, New York, Pennsylvania, Idaho, and Georgia, the courts do not recognize an independent cause of action for a violation of the implied covenant of good faith and fair dealing as distinct from a breach of contract claim. 17A AM. JUR. 2D *Contracts* § 712.
[126] *Id.* at 1433.
[127] *Id.* at 1431-32.
[128] RESTATEMENT (SECOND) OF CONTRACTS § 205 (1981).
[129] Iglesias, *supra* note 114, at 1432.
[130] 17A AM. JUR. 2D *Contracts* § 425 (2014-2015 ed.).

Enforcement is viewed as an equitable remedy for "someone who is benefited by the performance of the contract", such that they are an intended or incidental beneficiary.[131] This construct does not just give any third-party a cause of action against a contracting party though. In fact, in the context of this paper, courts will not use contract law to require franchisors to implement franchise agreement provisions uniformly throughout the franchised system; that is, a franchisee cannot claim third-party beneficiary status to insist that a uniform franchise agreement's provisions be enforced consistently.[132]

Courts commonly reject third-party beneficiary claims by franchisees on the ground that the franchisees are not intended beneficiaries because the franchise agreement between the franchisor and another franchisee did not reflect intent to benefit the discriminated-against franchisee.[133] The court denied application of the third-party beneficiary doctrine to a franchisee in the case of *Staten Island Rustproofing, Inc. v. Ziebart Rustproofing Co.*, stating that the franchisee-plaintiff could not point to any specific provision in the franchise agreement in which the franchisor agreed to enforce those same franchise agreement standards against other franchisees.[134] Thus, it seems that unless the franchisor is violating a substantive covenant or requirement of the franchise agreement that will amount to an actual breach of contract, contract law as a whole provides no recourse to the franchisee facing discriminatory franchisor practices.

V. Public Policy Perspective

A key asset in the franchising context is the concept of goodwill, the loyalty that a business earns from its customers.[135] The franchisee's ability to use the franchisor's established goodwill is used as a justification for the franchisor to impose strict requirements on the franchisee, whether it be quality control procedures, operation strategies, or something of the like.[136] The usage of the franchisor's goodwill and the requirements imposed upon franchisees to foster that goodwill both require uniformity.[137] Customer loyalty, or goodwill, is founded on the principle that when a customer patronizes a franchise unit, he or she will receive identical service and products, in an identical atmosphere, regardless of the unit's location.[138] This principle imposes the strenuous and continuous responsibility on the franchisee to maintain its franchise location in a uniform manner as compared to all other units.[139] It is clear that uniformity is the hallmark of the franchise system.[140] How is it that uniformity can be mandated in every detail of the franchising venture, which existing and prospective franchisees expect, but not extended to the franchise agreement, where franchisees anticipate continuity and non-discriminatory terms across the system? If franchisees become aware of the idea that they will

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[131] 8 FLA. PRAC., CONSTR. LAW MANUAL § 7:38 (2014-2015 ed.).
[132] Robert W. Emerson, *Franchise Terminations: Legal Rights and Practical Effects When Franchisees Claim the Franchisor Discriminates*, 35 AM. BUS. L.J. 559, 592 (1998).
[133] Christopher J. Curran, *Claims Against A Franchisor Upon an Unreasonable Withholding of Consent to Franchise Transfer*, 23 J. CORP. L. 135, 142 (1997).
[134] Staten Island Rustproofing Inc. v. Ziebart Rustproofing Co., 1985 U.S. Dist. LEXIS 13818 (E.D.N.Y. Nov. 18, 1985). This case is discussed in Bus. Franchise Guide (CCH) ¶ 8,492 (E.D.N.Y. 1985).
[135] Robert W. Emerson, *Franchise Goodwill: Take A Sad Song and Make It Better*, 46 U. MICH. J.L. REFORM 349, 352 (2013).
[136] *Id.*
[137] *Id.* at 405.
[138] *Id.* at 352.
[139] *Id.* at 383.
[140] *Id.*

not be treated as equal to other franchise locations, they may be discouraged from operating a franchise location, which could be injurious to the franchise industry as a whole.

VI. Comparative Law

While courts within the United States place a high degree of deference on the written franchise agreement between a franchisee and a franchisor, the European Union (EU) takes a more active role in the regulation of this business relationship. Article 85 of the Rome Treaty (Article 85),[141] in establishing the European Economic Community, addressed the regulation of franchise agreements for the EU.[142] The policies of Article 85 provide many rights to EU franchisees that may otherwise be prohibited under the express contractual terms of a franchise agreement governed by United States laws.[143] For example, Article 85 allows franchisees to buy products from other franchisees and prohibits franchisors from denying the supplier nomination by a franchisee except in situations in which the franchisor's reputation may be negatively affected.[144] The result is that franchisees are able to "remain independent businesses . . . without undue influence from a franchisor."[145]

The EU approach to franchise agreements limits the potential for abuse by franchisors that may be more prevalent under the U.S. method, which limits the franchisees' actions and decision-making abilities to what is expressly provided in the franchise agreement. While Article 85 does not specifically address the potential for discrimination claims, it is likely that such a claim by a franchisee would have a greater chance of success due to the general protection afforded to franchisees by the regulation.[146] In the EU, franchisors are not permitted to unduly influence the franchisee's business operations and likely have less detailed and extensive franchise agreements.[147] As a result, it would seem that there would be a lesser likelihood of a franchise discrimination claim arising, as there would be a lesser possibility for disparaging treatment.

It may be beneficial for congressional leaders or the federal judiciary to consider implementing or adopting an approach that gives more economic freedom to franchisees so that they can be more independent, or at least an approach that is tilted in favor of franchisees. This could be done through placing limitations, similar to those in the European Union, on the franchisor's ability to influence the franchisee's business.[148] If the franchisor were not allowed to micromanage every minute aspect of the franchisee's business, there would be two major benefits: (1) with less control over franchise operations, there would be a decreased opportunity

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[141] Rome Treaty, art. 85, Mar. 25, 1957, 37 I.L.M. 1002, *superseded by* Amsterdam Treaty, art. 81, Feb. 10, 1997, 37 I.L.M. 56.

[142] James W. Kirkconnell, *Franchise Agreements and Adjudication in the United States and the European Union*, 18 FLA. J. INT'L L. 413, 418 (2006). Actually, Section 85 of the Rome Treaty (1957), which instituted the European Community, has been superseded by Article 81 § 3 of the Amsterdam Treaty, signed February 10, 1997 (prohibiting vertical agreements and concerted practices). Robert W. Emerson, *Franchise Contracts and Territoriality: A French Comparison*, 3 ENTREPREN. BUS. L.J. 315, 325 & 325 n.39 (2009). The effects of the "renumbered" Article appear to be about the same as under Article 85, which still is discussed and turned to for guidance, although it is technically no longer in force.

[143] *Id.*

[144] *Id.*

[145] *Id.*

[146] *Id.*

[147] *Id.*

[148] *Id.*

for the franchisor to discriminate among franchisees; and (2) when discrimination did occur, it would almost certainly be related to a material aspect of the franchise agreement, such that a court would not be able to eliminate the claim on materiality grounds,[149] and have a greater likelihood of success.

In the international sector, some countries have taken independent initiative to address the issue of franchise discrimination. However, the scope of these laws varies. The countries that have taken the broadest stance towards prohibiting a franchisor's discrimination among franchisees are Austria, Lithuania, Malaysia, and Mexico. Austria's Act on Improvement of Local Supplies and Market Conditions ("*Nahversorgungsgesetz*") requires that franchisors apply equal conditions among franchisees, such that a franchisor may not grant or offer different supply conditions to some franchisees, but not to others, unless the franchisor can justify the differential treatment with objective reasons.[150] In Austria, the franchisor's responsibility to refrain from such discriminatory practices is also implicated by the duty of loyalty the franchisor owes to its franchisees – a duty that is not imputed upon the parties to a franchise relationship in the United States.[151] In Austria, when a franchisor unjustifiably discriminates among its franchisees, the franchisee may be allowed to terminate the franchise relationship before the designated ending date in the franchise agreement.[152] This is an interesting concept, as comparatively, American franchisees are most commonly bringing suit for wrongful termination based upon a discriminatory or other purpose of the franchisor, rather than being the party to terminate the franchise relationship.[153]

Mexico enacted a set of amendments to its Industrial Property Law in 2006 with the express purpose of guaranteeing non-discriminatory treatment for all franchisees of the same franchise system.[154] The laws do not succinctly define what is considered to be discriminatory treatment, but in the industry, it is viewed as requiring the franchisor to use the same terms and conditions for all franchisees in a system and to offer the same benefits to all franchisees in the same situation or circumstance. The Mexican Congress had been considering enacting a stricter, more detailed rule directed towards franchise discrimination than what was enacted, but for now, the general prohibition will have to suffice.[155]

Other countries broadly prohibit franchise discrimination, but through competition laws instead. For example, Lithuania's Law on Competition prohibits a franchisor from placing dissimilar conditions on its franchisees that would create a competitive disadvantage for some

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[149] *See Patel*, 948 F. Supp. at 475.

[150] Juris Publishing et al., *Austria*, *in* INTERNATIONAL FRANCHISING RELEASE 3 AUS/10-AUS/11 (Dennis Campbell ed., 2nd ed. 2014).

[151] *See* Jeffrey C. Selman, *Applying the Business Judgment Rule to the Franchise Relationship*, 19 Franchise L.J. 111 (2000) (discussing how applying the business judgment rule to the franchise relationship would result in the duties of loyalty, obedience, and diligence being imputed upon the parties).

[152] Austria, *supra* note 150.

[153] *See* Robert W. Emerson, *Franchise Terminations: Legal Rights and Practical Effects When Franchisees Claim the Franchisor Discriminates*, 35 Am. Bus. L.J. 559, 569 (1998) (describing how franchisees only occasionally challenge a franchisor's practices).

[154] Juris Publishing et al., *Mexico*, *in* INTERNATIONAL FRANCHISING RELEASE 3 MEX/6-MEX/7 (Dennis Campbell ed., 2nd ed. 2014).

[155] William K. Woods & Ann Hurwitz, *Franchising Legislation is Revamped*, DLA Piper Rudnick Gray Cary US LLP (March 14, 2006) *available at* http://www.internationallawoffice.com/newsletters/Detail.aspx?g=6edc0f09-1395-4b6c-bd74-01a71d76f23b.

franchisees, but not others.[156] The portion of the statute that is applicable to the franchise relationship depends upon whether the franchisor is considered to be dominant or non-dominant. Similarly, Malaysia's Competition Act prohibits any franchise agreement or setup that has the object or effect of "preventing, restricting, or distorting" competition by discriminating among franchisees in the same franchise system.[157] Although not strictly in the discrimination context, the EU also prohibits the franchisor from imposing anti-competitive conditions upon its franchisees if the conditions are not tailored to protect goodwill.[158] As demonstrated earlier in the Article, the United States has not used legislation to prevent anti-competitive behavior in the franchise discrimination context. Perhaps changes to these laws would step in and fill the voids where unequal bargaining power between franchisors and franchisees often enable the franchisor to escape liability.[159]

As an additional protection for Malaysian franchisees, Malaysia's Franchise Act builds upon its competition laws by prohibiting franchise discrimination with respect to franchise fees, royalties, goods, services, equipment, rentals, or advertising services if the discrimination would cause competitive harm to the franchisee being discriminated against. However, the franchisor may be justified in its discrimination, and thus not barred, if the discrimination arises because the franchises with differential treatment were established at different times or relates to a program the franchisor has in place for the purpose of making franchises available for individuals lacking the capital or funds to ordinarily become a franchisee.[160]

In comparison, some countries have enacted laws against franchise discrimination that are narrower in scope. Both Canada and Italy have enacted laws making price discrimination among franchisees unlawful in some fashion. Previously, in Canada, franchisors could only offer volume discounts to franchisees if the discounts are available for all competing franchisees to take advantage.[161] Presently, franchisors cannot engage in discriminatory pricing and promotional spending that has an anti-competitive purpose, and "a substantial lessening or prevention of competition in a particular market" is bound to occur.[162] In Italy, franchisors must comply with Italian and European Union competition laws, which both specifically use price discrimination as an example of an act that is most likely to be considered anticompetitive behavior.[163] As an alternative narrow approach, Egyptian law does not generally prohibit discrimination in the business and contractual realm, but it does specifically require that franchisor's draft their franchise agreements in a standard form that is given to all prospective

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[156] Juris Publishing et al., *Lithuania*, *in* INTERNATIONAL FRANCHISING RELEASE 3 LIT/6 (Dennis Campbell ed., 2nd ed. 2014).

[157] Juris Publishing et al., *Malaysia*, *in* INTERNATIONAL FRANCHISING RELEASE 3 MAY/13 (Dennis Campbell ed., 2nd ed. 2014).MAY/13

[158] James W. Kirkconnell, *Franchise Agreements and Adjudication in the United States and the European Union*, 18 Fla. J. Int'l L. 413, 414 (2006).

[159] *Id.* ("The United States tends to disregard relational market power and instead relies on a showing of specific behaviors and contractual remedies, and in so doing de-emphasizes empirical evidence of competitive harm.").

[160] *Id.* at MAY/14.

[161] Bruno Floriani & Marvin Liebman, *Considerations for Franchising in Canada*, Lapointe Rosenstein LLP (March 18, 2008), *available at* http://www.internationallawoffice.com/newsletters/Detail.aspx?g=f53148b4-7d2d-4f95-9e12-f70a2c61085.

[162] Andraya Frith & Dominic Mochrie, *Country Report Canada: Franchising*, International Distribution Institute 12 (February 2014) (on file with author).

[163]Juris Publishing et al., *Italy*, *in* INTERNATIONAL FRANCHISING RELEASE 3 ITA/38 (Dennis Campbell ed., 2nd ed. 2014).

franchisees.[164] Neither of these approaches would likely be implemented in the United States though. The American franchise law structure of evaluating whether a franchisee being discriminated against is similarly situated to other franchisees will always allow for price discrimination to occur if the franchisor can show the franchisees are not similarly situated. While franchisors typically do utilize standard form contracts in entering into franchise arrangements, the values placed upon freedom of contract principles in the United States will stand in the way of standard contracts being mandatory.

While the more limited restrictions above may not offer as many protections as the broader anti-discrimination laws described above, they are certainly more advantageous than if there were no such law in place. On the other end of the spectrum, England actually permits a franchisor to discriminate among its franchisees in the same franchise system.[165] A franchisor is instead barred from discriminating against its franchisees if the parties' franchise agreement specifically includes a clause obligating the franchisor to treat all franchises similarly; otherwise, the franchisor is not obligated to do so.[166] While the English rules may seem unfair, they are not much different than the pro-franchisor approach taken to franchise discrimination in the United States.

VIII. Conclusions

In the United States, an aggrieved franchisee like Fran, introduced in a hypothetical earlier in the Article,[167] may seek a remedy against the franchisor for discrimination. Fran may have multiple avenues to seek a remedy against a discriminatory franchisor, such as a state statute, federal statute, or alternative remedy. However, the ability of Fran and other aggrieved franchisees to succeed on any of these claims is unlikely.

First, state statutes specifically addressing franchise discrimination are limited in number, as only six states presently contain explicit anti-discrimination provisions entitling a franchisee to bring a cause of action.[168] Even if the franchisee is able to take advantage of one of these state statutes, the franchisee is not guaranteed to succeed. Some of the anti-discriminatory statutes are limited in scope and only prohibit discrimination in the context of termination or non-renewal of franchise agreements, instead of a broader range of general behavior.[169] Additionally, the statute may provide express defenses for the franchisor,[170] or the state courts may tend to interpret anti-discrimination provisions against the franchisee.[171] If the franchisee conducts its business in a state without such a law, it will be forced to rely upon common law or a different type of statutory claim to bring its lawsuit. Further, courts may require the aggrieved franchisee be similarly situated with the favored franchisee and that the discrimination relate to a material

[164] Juris Publishing et al., *Egypt*, *in* INTERNATIONAL FRANCHISING RELEASE 3 EGY/18 (Dennis Campbell ed., 2nd ed. 2014).
[165] Juris Publishing et al., *England*, *in* INTERNATIONAL FRANCHISING RELEASE 3 ENG/16 (Dennis Campbell ed., 2nd ed. 2014).
[166] *Id*.
[167] *See supra* Part III.
[168] *See supra* note 37.
[169] ARK. CODE ANN. § 4-72-204 (West 2012); WIS. STAT. ANN. § 135.03 (West 2012); *see supra* Part III.B.1-2.
[170] HAW. REV. STAT. § 482E-6(2)(C) (West 2012); 815 ILL. COMP. STAT. 705/18 (2012); IND. CODE ANN. § 23-2-2.7-2(5) (West 2012); WASH. REV. CODE § 19.100.180(2)(c) (2012); *see supra* Part III.A.1-4.
[171] *See supra* notes 67-68 and accompanying text.

aspect of the franchise.[172] Courts have discretion in analyzing these requirements, making it difficult for franchisees to prove them.[173]

When a franchisee has limited or no remedy under state law, it may attempt to pursue an alternative claim. Alternative claims may exist under a more general theory of contract law and implied covenants,[174] or perhaps fair competition laws.[175] If the franchise relationship relates to the automobile or petroleum industry, federal franchise laws may be available to an aggrieved franchisee.[176] Alternative claims provide the franchisee an opportunity for a remedy despite the lack of a state or federal statutory regulation. Since the state regulation is minimal, a franchisee in the United States is usually better served pursuing one of these alternative claims. However, the likelihood of success only increases marginally with the existence of these alternative claims. For example, the alternative theory of law may not be recognized in all jurisdictions if it is grounded in common law and may not encompass the franchise relationship (i.e. third-party beneficiary claims and federal laws).[177] A secondary concern is that even if these alternative claims are successful, they may not address any future discriminatory practices of the franchisor if they are based upon contract law and good faith principles.

The need for improvement in this area of law pertaining to franchise discrimination becomes apparent when franchisees have no direct statutory claims for the discrimination, have little likelihood of success in the jurisdictions where the cause of action does exist, and have little recourse under alternative avenues as well. The author proposes two courses of action for legislators, policymakers, and judges to consider going forward. The first course would be to implement legislation prohibiting franchise discrimination at the state or federal level that governs all aspects of the franchise relationship. The second course would be to adopt an approach similar to the European Union's viewpoint on franchising, which respects the individual autonomy of franchisees in the operations of their franchise units and precludes undue influence by franchisors.[178]

The first course of action, an enactment of an all-encompassing anti-discrimination statute in every state or federally, would provide franchisees a uniform remedy for discrimination in every jurisdiction. The six states that presently have these types of statutes in place could reevaluate the ways in which judges have been able to act discretionarily in applying the laws and tailor amendments to their codes to prevent these results.[179] To ensure the laws are applied uniformly in the courts, it would also be necessary to consider a predetermined list of criteria for judges to consider in all franchise discrimination claims when evaluating the substantially similar and materiality elements.

The second course of action could be implemented in tandem with the first or on its own. Although a uniform franchise law system as used in the European Union or elsewhere would be greatly beneficial to franchising in the United States, the likelihood of effectuating this great of a change is low. However, as a first step towards this end, placing limits on franchisors' ability to

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[172] W. MICHAEL GARNER, *supra* note 11.

[173] Compare *Implement Serv., Inc.*, 726 F. Supp. at 1181 (finding franchisees were similarly situated based on geographical locations), with *Elkhatib*, 493 F.3d at 830 (finding franchisees were not similarly situated even though all franchisees were located in Chicago).

[174] Burzych & Matthews, *supra* note 4, at 117; Iglesias, *supra* note 114.

[175] *See* 15 U.S.C. § 13(a) (2012); *see also* Emerson, *supra* note 6, at 567-68.

[176] *See* 15 U.S.C.A. § 2802 (1978); 15 U.S.C.A. § 1222 (1956).

[177] Emerson, *supra* note 132; Iglesias, *supra* note 114.

[178] *See supra* notes 142-145 and accompanying text.

[179] *See supra* note 37.

control every aspect of the franchising relationship would have the potential to solve many of the franchising issues in the United States that are not present in foreign jurisdictions. For example, giving greater economic freedom to franchisees and limiting the control power of franchisors would decrease the reasons for which a franchisor may terminate the franchising relationship. While neither of the two approaches may be immediately implementable, they will provide valuable considerations in evaluating the franchise discrimination conundrum.