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## Should franchisors be held liable for tortious interference when disapproving franchise sales?



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By Robert Zarco

Contrary to Mr. Joblove's opinion, while a franchisor may exercise discretion in the approval or disapproval of a purchaser of restaurants, it is not the mere disapproval by the franchisor of the sale of restaurant gives rise to a breach of contract or tortious interference claim. It is the franchisor's unreasonable withholding of its approval of the sale of a franchise to a qualified purchaser that constitutes a breach of contract and breach of the implied covenant of good faith and fair dealing. Further, it is the franchisor's affirmative conduct that extends beyond mere disapproval of the transaction which gives rise to a claim for tortious interference.

Franchisors claim that they should have unfettered discretion as to whom franchisees may sell their restaurants. While it is true that franchise agreements characteristically provide that the franchisor may, in its "sole judgment," refuse to consent to the sale of franchises to a prospective purchaser, when the agreement also expressly provides that its consent to the sale of restaurants by franchisees to qualified purchasers "shall not be unreasonably withheld," the franchisor's claim of unfettered discretion flies in the face of the law.

Even when a franchisor reserves "sole" or "substantial" discretion to itself in the franchise agreement, it must exercise that discretion reasonably and in good faith. This duty to act in good faith limits the franchisor's ability to act arbitrarily or capriciously to contravene the reasonable contractual expectations of the other party. When the contract specifically provides that the consent shall not be unreasonably withheld, an action for breach of contract and of the covenant of good faith arises out of those express terms.

The law cited by Mr. Joblove only stands for the proposition that the act of disapproval alone does not constitute breach of contract. Such a contention does not apply where a prospective purchaser clearly satisfies all of the franchisor's qualification standards. However, despite these qualifications, the franchisor wrongfully and in bad faith rejects the sale. A cause of action is even readily apparent if the franchisor's stated reasons for refusal to consent to the sale were in fact pretextual and false and were part of a scheme to force the franchisee to sell its restaurants at a drastically reduced price to

buyers handpicked by the franchisor. In such a situation, the franchisor should be held accountable not merely because the franchisor disapproved the transaction. Rather, it is the franchisor's unreasonable, arbitrary, and capricious withholding of its consent to the sale that constitutes a breach of contract as well as a breach of the covenant of good faith and fair dealing.

### Tortious interference

Again, contrary to Mr. Joblove, it is not the act of disapproval that constitutes tortious interference. It is the franchisor's affirmative conduct for which it should be liable. Mr. Joblove contends that a franchisor may interfere in these transactions because it is a party to the franchise agreements that the franchisee seeks to assign. However, the issue is not whether the franchisor tortiously interfered with its own franchise agreement; it is whether the franchisor tortiously interfered with the purchase agreement, to which it was not a party. If the franchisor interferes with the purchase agreement, it must establish that its conduct is privileged or justified. However, that privilege is not unlimited. If the franchisee can show bad faith or improper motives for the interference, the privilege defense is inapplicable.

In the cases cited by Mr. Joblove, it was not contended that there was affirmative conduct by the franchisor beyond the act of disapproval. In the situation I presented above, suppose that the franchisor, upon reviewing the purchase agreement, advised the prospective buyer that it was paying too much for the restaurants, and that the franchisor did so because it wanted the franchisee to sell the restaurants at a drastically reduced price to buyers of the franchisor's choosing. Clearly, such affirmative conduct by the franchisor would constitute tortious interference, and the improper purpose for that interference would render the privilege defense inapplicable.

When dealing with qualified purchasers, franchisees should be free to negotiate the best price it can get for the restaurants. In the same way, while the franchisor should have the right to protect its brand by having substantial discretion in deciding who may be franchisees, that discretion can not be absolute, especially when that discretion is colored with bad faith and improper motives. In those situations, the franchisor must be held liable for its actions.

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