
Franchise Times®

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January 2005

Blimpie franchisees sue

Lawsuit accuses corporate and CEO of taking “kickbacks,” starving ad fund

By Mike Mitchelson

What the CEO calls an aggressive attempt to improve a brand is being interpreted by franchisees as poor leadership and a “scheme” to pocket rebates.

Blimpie International franchisees and area developers are charging in two class action arbitration complaints that their franchisor and its CEO, Jeffrey Endervelt, have taken rebates from suppliers—specifically \$6.5 million from Pepsi—that should have gone into an advertising fund. The lost funds and Endervelt’s leadership have driven down profits for franchisees and forced some out of business, the suit alleges. Endervelt claims the system was in decline before he took over, and he is trying to clean it up.

Arbitrators have been selected for the two cases. A third case, involving a Georgia area developer, is “close to settlement,” said attorney Robert Zarco of Zarco Einhorn & Salkowski, who represents the franchisees and area developers in the cases.

“And we intend to proceed (with the other two) unless the franchisor decides to take steps to make the area developers and franchisees whole,” he said.

Background

The franchisees charge that their franchisor and Endervelt, who acquired the chain in 2002, have since that time “engaged in a scheme to force the franchisees to purchase their provisions exclusively from third-party suppliers who are required to pay kick-

backs to the franchisor and its principal Endervelt” according to the complaint.

As a result, the complaint states, franchisees’ businesses are becoming unprofitable because of the increased cost of supplies. Further, the complaint alleges that rebate monies from suppliers intended for an advertising fund are instead being funneled to the franchisor. The second arbitration complaint involves about 40 Blimpie area developers charging that Blimpie International, among other issues, violated subfranchisee contracts.

The complaints also allege specifically that under an agreement with the franchisor and Pepsi, the beverage company would pay Blimpie International a \$6.5 million rebate to replace its current vendor Coca Cola throughout the chain. Because ad fund rebates are instead going to Blimpie International, the lack of advertising and increased cost of supplies have reduced profits and compromised the brand, franchisees claim.

“I think there has been significant corporate greed reflected in rebates paid by vendors not going to the intended recipient—which was the brand building fund—and rather going into Jeff Endervelt and corporate management’s pocket,” Zarco said, when we first talked to him in October.

That’s not the case, Endervelt said then. “A kick-back is an unlawful and illegal transfer of money under the table,” he said. “This is a normal vendor rebate, which is standard in the industry. It’s listed in

Item 8 of our UFOC; we report these things immediately as we're required to, and that's really the end of it."

The rebates are not required to go into the brand fund, Endervelt said, adding, "Under the terms of our franchise agreement and our UFOC, we have a right to vender rebates." Blimpie International, Pepsi, and other vendors gave money to the brand fund in addition to the money they gave Blimpie International, he added. "This is how we run our business and compete with people like Quizno's and other people who do get rebates."

Money from suppliers should be placed in the ad fund, said George Poulos, owner of two Blimpie franchises in Omaha, Neb. Revenues have declined at his stores, and his food costs have climbed from 30 percent to 37 percent, he said. "In the last two and a half years, every (supplier) contract we've signed has driven up our cost in one way or the other," he said. "Two and a half years ago we were approximately 2,300 units, now we're approximately 1,500. Why are we declining, while other participants in our segment are growing? We just don't have market presence anymore."

Standards were dropping, and the brand needed revitalization when he took over, Endervelt said then. "When I came in, one of the first things I said was, 'I'm going to clean up the system.' There's no question that we've closed stores, and that's been my intent in most cases. ...We weren't servicing the customer the way we need to with the quality of product that we insist that we serve."

The product has always been high quality-corporate decisions are dragging down the brand, Poulos said. "My view is if the restaurant was in business three years ago, customers were coming in, and (the franchisee) was paying a franchise fee, they must have been doing something correctly," he said. "They were here yesterday, and they're gone today. What has changed in the process has been new ownership at Blimpie International, new policies and procedures."

Blimpie franchisee Cindy Miller said her problems began with the change in leadership. "Since Endervelt has taken over the company, our percentage of food costs have risen drastically, and our advertising funds have not been done appropriately," she said. "My business is down drastically, and our profit margins are down because of rising food costs."

Sales at her two Terra Haute, Ind., restaurants were flat in the year prior to Endervelt's takeover, "but the flat was at a good level," she said.

The complaints, filed in late July, are "months old," and the complainant's attorneys used the media to "urge me to the table," Endervelt said. "There's no case here."

To say he is using the media to bring about a settlement is an "outrageous and ridiculous statement," Zarco said then. "The media became aware of this as a result of franchisees complaining, and then they came to us."

The case is a class-action lawsuit; the Blimpie franchise system is in "revolt," he said. "The case has complete legal and factual validity." ■