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# All About Franchising, Joint Employers and the NLRB

***Alejandro Brito, Daily Business Review***

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For many years, franchisors have repeatedly stated, and courts have generally agreed, that franchisees are independent contractors and not agents of the franchisor and thus franchisees' employees cannot be classified as employees of the franchisor.

As a result, any liability arising from unlawful conduct directed at a franchisee's employee was to be borne solely by the franchisee, while the franchisor was relieved of any such liability. To the extent that any anomalous claim found a franchisor liable to a franchisee's employee, a franchisor would simply transfer such liability to the franchisee under the indemnification provision routinely found in franchise agreements.

However, in July 2014 the National Labor Relations Board drastically altered this landscape through its ruling that McDonald's Corp. was a "joint employer" over franchisees' employees in 43 cases, most of which related

to allegations made by workers who claimed that their rights had been violated when they had participated in protests to obtain increased wages and improved working conditions.

The NLRB's decision was premised upon the determination that McDonald's "engages in sufficient control over its franchisees' operations, beyond protection of the brand," which warranted a determination that McDonald's was a "putative joint employer with its franchisees, sharing liability for violations" and which has exposed McDonald's and its franchisees to 13 formal complaints being filed against it by the NLRB.

## Business Control

Under the law, a joint employment relationship exists when both companies share direct control over the terms and conditions of a worker's employment.

Given the potential liability that franchisors would be exposed to if franchisors are ultimately deemed to be joint employers of a franchisees' employees, it surprises no one to see that franchisors are vehemently fighting the joint employer designation.

Franchisors are claiming that the joint employer designation will leave them with only two equally unattractive alternatives: franchisors will be required to oversee the daily management of franchisees' employment practices, or franchisors will retreat from the franchising model and opt to instead operate a different business model in order to avoid the potential risks that they may face through franchising.

Franchisors are also claiming that these recent actions by the NLRB are fueled by the desire of some to break up franchising as a viable business model and enhance the legal standing and political clout of labor unions. However, in making these sky-is-falling-type arguments, franchisors are failing to recognize that the current situation in generally one of their own creation.

It is important to note the linear progression of control that exists between an independent business, a licensed business and a franchised business, wherein an independent business person has full control over its operation, a licensee maintains substantial control over its business and a franchisee, as franchising has evolved, possesses limited control over its business despite the designation in most franchise agreements that the franchisee is an independent contractor.

Over the recent years, franchisors have so expanded their contractual rights to the extent that courts have not been reluctant to find that franchisors now exert such a level of control over a franchisee's daily business affairs that franchisors have been routinely found to be vicariously liable for the acts of franchisees in claims brought by consumers, such as for personal injury to the consumer.

The joint employer designation and the resulting liability arising from a claim filed by a franchisee's employee appears to simply be a logical extension of the courts' view of the amount and extent of control being exercised by franchisors.

## Other Solutions?

Bearing in mind that the NLRB's ruling placed a heavy emphasis on its finding that McDonald's "engages in sufficient control over its franchisees' operations, beyond protection of the brand," a joint employer

determination would not withstand judicial scrutiny unless the franchise documents, such as the franchise disclosure document, the franchise agreement, and the operation manuals, did not so plainly evidence that the level and nature of control being exercised by the franchisor over the franchisee was substantial, direct and pervasive.

If franchisors were not so adamant about exercising control over even the slightest aspect of their franchisees' businesses under the guise of "system control" or "brand integrity," it stands to reason that any basis to classify them as a joint employer would be substantially muted.

Aren't there other solutions to this situation that don't require the dismantling of franchising as we know it?

Why can't franchisors discharge some of the inordinate amount of control that they possess, and aggressively exercise, over the franchisees without any sacrificing of the quality of the services and goods being offered by the franchisee within the franchise system?

Why can't franchisors abide by the designation listed in franchise agreements of franchisees as independent contractors rather than treating them as glorified employees?

Why must this parent-child relationship continue?

A potential solution to the NLRB situation may exist if franchisors release certain types and amounts of control over their franchisees in their daily business practices. Allowing franchisees to genuinely operate as independent contractors will substantially negate a future determination that any particular franchisor has exercised substantial control over the franchisee's business and will serve to challenge a determination of joint employer status over that franchisor.

Indeed, the sky is not falling. Franchising is merely due for a recalibration of the control exercised by franchisors over their franchisees. A failure to engage in such a recalibration will plainly expose franchisors to substantial liability.

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