



American Association of Franchisees & Dealers *The Center for Total Quality Franchising*

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February 11, 2019

Roxanne Rothschild, Executive Secretary
National Labor Relations Board
1015 Half Street SE
Washington, D.C. 20570-0001

VIA E-FILING

Re: 3142-AA13; Proposed Rule Regarding the Standard for Determining Joint Employer Status—Response to IFA Rebuttal of January 28, 2019

Dear Ms. Rothschild:

On behalf of the American Association of Franchisees and Dealers (“AAFD”) and its members, we submit these comments in response to the Rebuttal of the International Franchise Association (“IFA”) submitted on January 38, 2019 to the Notice of Proposed Rulemaking (“NPRM”) on the Standard for Determining Joint Employer Status published in the Federal Register on September 14, 2018.

AAFD is the oldest and largest national not for profit trade association advocating the rights and interests of franchisees and independent dealer networks. The AAFD supports more than 40 independent franchisee associations and trademark specific chapters, representing thousands of franchisee operated business outlets. Since our establishment in 1992, the AAFD has focused on its mission to define, identify and promote collaborative franchise cultures that respect the legitimate interests of both franchisors and franchisees, cultures we describe as embracing our vision of *Total Quality Franchisingsm*. The AAFD came into existence in response to a franchising community that has been evolving towards increasingly one-sided and controlling franchise agreements and cultures whereby franchisee equity and business ownership has been continually eroding such that many modern franchise systems have lost all vestiges of business ownership.

In 1994, the undersigned published *The Franchise Fraud: How to Protect Yourself Before and After You Invest* (Wiley 1994), republished and updated in 2007. The premise of my book was that the *franchising industry* falsely promotes modern franchising as a safe and secure path to business ownership, but that modern franchise businesses are rarely business ownership and that a higher percentage of franchised

**Re: 3142-AA13; Proposed Rule Regarding the Standard for Determining Joint Employer Status
AAFD Comment of February 11, 2019**

Roxanne Rothchild

businesses fail than independent start-ups due to the controlling influence of franchisors who dictate labor and controllable business costs in a manner denies the traditional right of a business owner to manage its affairs.

In 1993, the AAFD promulgated its Franchisee Bill of Rights (attached and incorporated in this response) as a statement of fundamental rights necessary to respect a franchisee's ownership interests and expectations regarding franchisor support.

In 1994, the AAFD commenced an effort to negotiate a body of AAFD Fair Franchising Standards. The AAFD's Fair Franchising Standard Committee included franchisor executives, franchisee advocates and lawyers representing both franchisors and franchisees and was tasked to build a body of balanced standards that respect the legitimate interests of both franchisors and franchisees. In order to pass a standard, the standard had to be approved by a majority of each of our franchisor, franchisee and franchise attorney constituencies, and then pass the entire committee by a two-thirds vote. Over a 15-year effort, the AAFD Standards Committee has promulgated 140 standards that touch every aspect of the franchise relationship.

For the reasons set forth below, AAFD responds to the IFA Rebuttal and urges the National Labor Relations Board ("NLRB" or "Board"), to adopt a joint employer standard that respects Board's decision in *Browning-Ferris Industries of California, Inc., d/b/a BFI Newby Island Recyclery*, 362 NLRB No. 186 (2015).

IFA Misdirection Regarding the Definition and Foundation of Joint Employment Status.

We have had an opportunity to review the Rebuttal of the International Franchise Association, dated January 28, 2018. It may surprise the Board that the AAFD members share a desire to avoid a recognition of joint employer status from their franchisors. Franchisees respect a franchisor's ownership and control of its brand and right to enforce system standards to protect the brand, and franchisees depend and rely on the list of benefits and support services enumerated in the IFA's response. We do not believe that the many services franchisors historically provide to franchisees, and which are now being disingenuously withdrawn under the 'guise' of the joint employer threat are, or should be, the focus of the joint employment standard.

Rather the 'test' of joint employer status should be determined based upon the amount of economic control a franchisor *directly* exerts over its franchisees and which negatively impact and eviscerate a franchisee's equity ownership in the franchised business.

We believe that the IFA is engaging in the art of misdirection in its arguments, tending to avert attention from the real economic basis for a finding of joint employment. The real concerns are economic control, not the enforcement of legitimate brand standards, and include:

**Re: 3142-AA13; Proposed Rule Regarding the Standard for Determining Joint Employer Status
AAFD Comment of February 11, 2019**

Roxanne Rothchild

1. The claim that all of the goodwill of the franchised business belongs to the franchisor, without any recognition of equity ownership by the franchisee whose capital and sweat equity are a major component of a franchise unit's existence and success.
2. Control over the ownership of the franchise location whereby the franchisor owns or controls the real estate which is leased or sublet to the franchisee impacting the franchisee's ownership of the business.
3. Abusive control or ownership of the assets of the business, such that a franchisee is little more than a sharecropper running the business for the benefit of the franchisor. Indeed, (in the case of) McDonalds no longer refers to franchisees in its agreements. In full claim of ownership, a McDonald's licensee is referred to legally as an 'operator' of a business that McDonald's fully owns.
4. The exercise of abusive control over the suppliers and supply chain of the of the operation. Far and beyond the enforcement of necessary system standards, many franchisors dictate sole sources of supply for the purpose of marking up the goods and services being purchased by franchisees, and regardless of the connection to the brand or brand standards. Franchisors now dictate where to buy insurance, process and control customer payments, and even business supplies, as well as dictating the source of brand related commodities that could be purchased at lower cost from competitive sources.
5. Control over the cost of labor by setting hours of operation that are not realistic for a particular franchise unit.

Historic Government Concern over Franchisor Excessive Control

It should be noted that Federal and state concerns over a franchisor's excessive control are not new. For more than thirty years the US Small Business Administration, the IRS, the Department of Labor, and the Federal Trade Commission have all raised concerns and red flags when a franchisor's control over the franchised business has crossed the line regarding whether the franchisee or the franchisor is the true owner of the business, often concluding that the franchisee is more employee than independent contractor.

The SBA has long refused to grant SBA loans to franchisees of franchise systems where the franchisor's control over the enterprise challenged a finding that the franchisee actually is the owner of a small business. Indeed, in the late 1990's the AAFD participated in an SBA joint task force that led to the creation of the SBA's registry of franchise systems that meet the its control criteria. Similarly, the SBA manages a federal program whereby a portion of government contracts are 'set aside' for small businesses, and these funds have been denied to franchise owners when a franchisor's control of the business was so great that it was deemed to be a virtual ruse to garner contracts for a big business masquerading as a small business. (*Cite to In Re Norell Temps, ca. 1997 – citation pending*).

Similarly, the Department of Labor and the IRS have on numerous occasions found that a franchise relationship crossed the line from independent contract to employment which we argue is merely an extension of the same concerns that have led to the *joint employer* classification.

**Re: 3142-AA13; Proposed Rule Regarding the Standard for Determining Joint Employer Status
AAFD Comment of February 11, 2019**

Roxanne Rothchild

Much of the Federal Trade Commission's Rule on Franchising is concerned with disclosing the extent to which a franchisor exercises control over a franchised business. Although the FTC has declined to exercise oversight over the franchisor/franchisee relationship, it has made clear that franchisees should be concerned over the amount of control exercised by a franchisor in making an investment decision.

The Solution to the Browning-Ferris Joint Employer Dilemma

The AAFD and its members share the IFA's concerns that a franchisor should not face the threat of being a joint employer as a result of establishing and enforcing brand standards or providing essential guidance and training to support brand standards. We join the IFA in urging the Board to recognize the legitimacy of protecting brand standards, and to place its definition of *joint employment* on the real matter of 'who owns the franchised business equity.'

In establishing its test for Joint Employment, we urge the Board to Focus on minimum equity concerns:

1. The right to grow the business and manage its costs of operations, including the management and control of labor, goods, products and services purchased for operations.
2. The right to stay in business, or to sell the business, or to transfer the business to heirs.
3. *The right to manage the business finances, especially the right of the franchisor to pull funds from the franchisee's bank accounts, or whether the franchisee has the power over its own checkbook.*
4. *The very important, albeit sensitive, right to control the cost of supplies and suppliers. A significant promise of franchising is the power of volume purchasing, but the ability of a franchisor to dictate suppliers is fraught with the potential for abuse. A key inquiry to determine whether a franchisor has crossed the line of control over the business is whether the franchisee's interests are respected and protected where a franchisor reserves significant control over the franchisee's source of supplies.*
5. Similarly, the control over the marketing budget is critical to a successful franchise system. A franchisor may control most of the marketing fund, but a line is crossed when a franchisee retains no ability to influence and direct its marketing dollars.

Quite simply, the solution to the joint employer 'threat' for franchise systems is to recognize franchisee equity ownership to franchisees in a sufficient amount that the franchisee is deemed to be the 'owner' rather than a mere 'operator' of the franchised business.

The AAFD's Franchisee Bill of Rights Provides the Appropriate Tests for Excessive Control

We submit both the AAFD Fair Franchising Standards, and especially the Franchisee Bill of Rights, as appropriate criteria to measure and test whether a franchisor has crossed the line of excessive control. The Franchisee Bill of Rights provide 14 indicia of a franchise system that respects the equity interests of franchisees. Although the product of true collective bargaining, the AAFD Fair Franchising Standards are

**Re: 3142-AA13; Proposed Rule Regarding the Standard for Determining Joint Employer Status
AAFD Comment of February 11, 2019**

Roxanne Rothchild

perhaps too extensive to serve as a useful tool, except for the purpose of analyzing relative rights of the parties to a franchise relationship.

Here are the AAFD Franchisee Bill of Rights:

1. The right to equity in the franchised business, including the right to meaningful market protection.
2. The right to engage in a trade or business, including a post-termination right to compete.
3. The right to the franchisor's loyalty, good faith and fair dealing, and due care in the performance of the franchisor's duties, and a fiduciary relationship where one has been promised or created by conduct.
4. The right to trademark protection.
5. The right to full disclosure from the franchisor, including the right to earnings data available to the franchisor which is relevant to the franchisee's decision to enter or remain in the franchise relationship.
6. The right to initial and ongoing training and support.
7. The right to competitive sourcing of inventory, product, service and supplies.
8. The right to reasonable restraints upon the franchisor's ability to require changes within the franchise system.
9. The right to marketing assistance.
10. The right to associate with other franchisees.
11. The right to representation and access to the franchisor.
12. The right to local dispute resolution and protection under the laws and the courts of the franchisee's jurisdiction.
13. A reasonable right to renew the franchise.
14. The reciprocal right to terminate the franchise agreement for reasonable and just cause, and the right not to face termination, unless for cause.

It is instructive to note that the Franchisee Bill of Rights actually recognize, even require, a franchisor to provide and support brand standards. Providing the expected 'control' over brand standards should not be the determinative criteria for joint employer. We urge the focus on relative equity: the determination of whether the agreement and relationship fairly recognizes that the franchisee has a significant equity right in the franchised business.

Conclusion:

The AAFD appreciates the concerns of the Board and the Court of Appeals, and of the IFA, with respect to creating an appropriate 'test' for when a franchise system has crossed a line and become the 'joint employer' of a franchisee's *putative* employees. We believe that many franchisors exercise so much control over the franchised business that the franchisee retains limited if any equity ownership in the franchised business. In such circumstances it is appropriate to deem the franchisor as the joint (and sometimes even

**Re: 3142-AA13; Proposed Rule Regarding the Standard for Determining Joint Employer Status
AAFD Comment of February 11, 2019
Roxanne Rothchild**

the sole) employer of the franchised business employees. But we also believe that the establishment, support and enforcement of brand standards are not the appropriate target of any control test. Rather the inquiry should be focused on the economic rights of business ownership that is promised and expected in a franchise relationship. Fair and balanced franchise agreements and relationships that respect the Franchisee Bill of Rights will provide and meet an appropriate test for the Board, and we urge this approach to determining if and when joint employer status has occurred.

Respectfully submitted,



Robert L. Purvin, Jr,
Chair, Board of Trustees
American Association of Franchisees and Dealers.



The Franchisee Bill of Rights

The Franchisees of America, representing the best of the American entrepreneurial spirit, hereby recognize and demand a basic minimum of commercial dignity, equity and fairness. In recognition thereof, the franchisees of America do proclaim this Franchisees' Bill of Rights.

As the minimum requirements of a fair and equitable franchise system.

- The right to equity in the franchised business, including the right to meaningful market protection.
- The right to engage in a trade or business, including a post-termination right to compete.
- The right to the franchisor's loyalty, good faith and fair dealing, and due care in the performance of the franchisor's duties, and a fiduciary relationship where one has been promised or created by conduct.
- The right to trademark protection.
- The right to full disclosure from the franchisor, including the right to earnings data available to the franchisor which is relevant to the franchisee's decision to enter or remain in the franchise relationship.
- The right to initial and ongoing training and support.
- The right to competitive sourcing of inventory, product, service and supplies.
- The right to reasonable restraints upon the franchisor's ability to require changes within the franchise system.
- The right to marketing assistance.
- The right to associate with other franchisees.
- The right to representation and access to the franchisor.
- The right to local dispute resolution and protection under the laws and the courts of the franchisee's jurisdiction.
- A reasonable right to renew the franchise.
- The reciprocal right to terminate the franchise agreement for reasonable and just cause, and the right not to face termination, unless for cause.

THE AMERICAN ASSOCIATION OF FRANCHISEES AND DEALERS HAS DEVELOPED THE FRANCHISEE BILL OF RIGHTS AND WORKS TO PROMOTE AWARENESS AND ACCEPTANCE OF IT AMONG THE FRANCHISING COMMUNITY AND THE GENERAL PUBLIC.