Vicarious Liability in Developing Areas: Damned If You Do and Damned If You Don’t!

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FUNDAMENTAL PRINCIPLES OF VICARIOUS LIABILITY LAW WITHIN FRANCHISING

• Shift of control away from the franchisor to the independent owner-operator
• Licensing of intellectual property – usually in the form of the franchisor’s trademark
• Franchisor is required to exercise sufficient control over a franchisee’s use of its mark, or else the franchisor will be deemed to have abandoned its mark
• Vicarious liability holds one party liable for acts or omissions of another
• Hinges upon the extent of control exerted by the franchisor over the franchisee and its operation of the franchised business
• Unique to the franchise relationship is the fine line a franchisor must walk between ensuring quality, uniformity and adherence to system standards, protection of its intellectual property, and good will – while minimizing its level of control in the relationship
• Actual agency v. apparent agency


• The instrumentality rule – *Hong Wu v. Dunkin’ Donuts, Inc.*, 105 F. Supp. 2d 83 (E.D.N.Y. 2000)
JOINT EMPLOYER

The *Browning-Ferris* Decision – NLRB, August 2015

“Having fully considered the issue and all of the arguments presented, we have decided to restate the Board’s legal standard for joint-employer determinations and make clear how that standard is to be applied going forward.

* * *

[W]e will no longer require that a joint employer not only possess the authority to control employees’ terms and conditions of employment, but must also exercise that authority, and do so directly, immediately, and not in a “limited and routine” manner . . . The right to control, in the common-law sense, is probative of joint-employer status, as is the actual exercise of control, whether direct or indirect.”

*Browning-Ferris Industries*, Case 32-RC-109684, at 15-16 (Emphasis added)
Freshii Decision – Advice Memorandum of the Associate General Counsel – NLRB

- Not responsible for setting the wages, raises or benefits of the franchisee’s employees
- No role in the decisions of its franchisee with respect to hiring, firing, disciplining or supervising employees
- Not involved in the franchisee’s scheduling and setting work hours of its employees
- Sections of the operations manual offered as “recommendations” rather than “mandatory” requirements
• Inspections limited to ensuring compliance with mandatory brand standards and not any employment-related policies

• Franchise agreement specified that the system standards of the franchise did not include “any personnel policies or procedures” but that such policies and procedures were for franchisees’ optional use
Franchise agreement stated that Freshii “neither dictates nor controls labor or employment matters for franchisees and their employees”

Provides franchisees with a sample employee handbook that contained personnel policies but did not require franchisees to use the handbook or policies

Not actively involved in the point-of-sale systems or any scheduling software

Did not use termination right to affect the terms and conditions of the franchisee’s employees

_Nutritionality, Inc. d/b/a Freshii, 13-CA-134294, 13-CA-138293, and 13-CA-142297 at 2-3_
"Does a franchisor stand in an employment or agency relationship with the franchisee and its employees for purposes of holding it vicariously liable for workplace injuries allegedly inflicted by one employee of a franchisee while supervising another employee of the franchisee? The answer lies in the inherent nature of the franchise relationship itself."

*Patterson v. Domino’s Pizza, LLC, 333 P.3d 723, 725 (Cal. 2014)*
Court found no reasonable inference that Domino’s retained or assumed the traditional right of control as an employer over employment aspects:

• Not in control with respect to training employees on how to treat each other at work and how to avoid sexual harassment

• The training programs on the computer system did not cover these employment issues

• Franchisee implemented his own harassment policy and training program for his employees
Authority to impose discipline for any violations and control over that was with the franchisee.

Franchisee encouraged the reporting of sexual harassment complaints directly to him.

Domino’s had no procedure for monitoring or reporting sexual harassment complaints between the employees of franchisees.

Was the franchisee – not Domino’s – who took unilateral disciplinary action against the alleged harasser as a result of the plaintiff’s complaint?

*Id.* at 741-742
Ochoa v. McDonald’s Corp., 133 F. Supp. 3d 1228, 1233 (N.D. Cal. 2015)

Applied the three tests under California precedent for determining whether a person is an “employer”:

“a person who ‘directly or indirectly, or through an agent or other person, employs or exercises control over the wages, hours, or working conditions of any person.’” (Emphasis added.) “Employ,” according to the court, means:

1) ‘to exercise control over . . . wages, hours or working conditions,’
2) ‘to suffer or permit to work,’ or
3) ‘to engage, thereby creating a common law employment relationship.’”
Held that the following factors did not amount to sufficient control to render McDonald’s a “joint employer”:

- the power to terminate/non-renew/deny expansion for systems standards violations
- suggestions for crew scheduling and staffing
• monitoring of customer service metrics, even if enforced by sanctions against the franchisee

• McDonald’s-provided software (POS and timekeeping, crew scheduling/inventory control)

• business consultant advice/monitoring

• McDonald’s ownership or leasehold interest in the restaurant property

_Id. at 1236-38_
Court did deny summary judgment to McDonald’s on the “ostensible agency” claim:

“(1) the person dealing with the agent does so with reasonable belief in the agent’s authority; (2) that belief is ‘generated by some act or neglect of the principal sought to be charged,’ and (3) the relying party is not negligent.”


Subsequently, certified a class of more than 800 current and former employees of the McDonald’s franchisee on this claim
Is this type of control by Franchisor necessary to protect the brand and quality of the system?

- Minimum number of hours of training regarding service offered to customers
- Hours of operation of the business
- Requiring minimum number of employees at certain times of day
- Employees must wear uniform with logo
- No employee shall engage in sexual harassment of any other employee
- Franchisee shall not hire anyone under the age of 18
- Franchisee shall not hire anyone with a previous felony conviction
- Franchisee must not discriminate in pay between males and females
- Franchisee must offer employees a health insurance plan
• Franchisee can only hire employees with a high school diploma
• Marketing material needs approval of franchisor
• Franchisees cannot have individual websites
• Franchisees must not post anything regarding franchise on social media sites
• Franchisees must not require employees to work on their religious holidays
• Franchisees must keep record of time employees have worked
• Franchisees must prohibit employees surfing the Internet during work hours
• Employees of franchisee must pay $50 for each customer complaint against them
Data breaches are occurring with increased frequency in various industries and government:

- Yahoo
- ADP
- Ashley Madison
- Blue Cross/Anthem
- LinkedIn
- Sony
- Target
- FBI
- IRS
- Office of Personnel Management

Franchising is not immune to data breaches:

- Wendy’s
- Wyndham
No reported decisions addressing a franchisor’s potential liability for data breaches at franchisee locations

- Analogies to vicarious liability in physical security cases
- Key issue is one of degree of control and nexus between control and the claim at issue
  - Primary theme had been: “recommend” don’t “mandate”

But more difficult to do when it comes to computer systems because of the need to integrate franchisee operations with the overall system
- Particularly difficult where reservations are made at the national level
Federal Trade Commission v. Wyndham Worldwide Corporation, 799 F.3d 236 (3rd Cir. 2015)

• FTC alleged that Wyndham Hotels and Resorts (“Wyndham”) had “failed to provide reasonable and appropriate security for the personal information” collected and maintained by independently owned Wyndham-branded hotels

• Alleged that there had been 3 occasions on which intruders gained access to consumer data on the Wyndham-branded hotels’ computer networks
FTC asserted various alleged actions by Wyndham that the FTC claimed violated Section 5(a) of the FTC Act, including not employing certain methods to require user ID’s and passwords that are difficult for hackers to guess, and inadequate use of firewalls to limit access between and among the hotels’ management systems.

Primary issues before the Third Circuit were:

1) whether the FTC had the authority under Section 5(a) to assert an “unfairness” claim in the data-security context

2) whether the FTC provided fair notice of what the law requires before bringing its “unfairness” claim

§ 5(a)
Third Circuit held:

1) that the FTC does possess the authority to file suits against private companies for data security practices; and

2) that Wyndham possessed fair notice that cybersecurity practices could fall within the statutory standard.
FTC reached settlement with Wyndham:

- Wyndham is required to implement and maintain for twenty years a comprehensive information security program reasonably designed to protect the security, confidentiality and integrity of customers’ cardholder data collected or received by Wyndham in the U.S.

- Franchised hotels and resorts are excluded from the coverage
• But Wyndham is required to have safeguards to control risks emanating from certain Wyndham-branded franchised hotels to the cardholder data Wyndham itself collects or receives.

• So long as Wyndham collects or receives cardholder data (but for no more than twenty years), it is required to obtain annual independent assessments and certifications of the extent of its compliance with specified data security standards, which at Wyndham’s election may include the Payment Card Industry Data Security Standard (“PCI DSS”).
• As part of the annual assessment process, the assessor also must certify whether Wyndham places certain restrictions on connections from certain franchisee computer networks

• If Wyndham obtains the assessments and those assessments certify compliance with PCI DSS (or another approved standard) each year, it will be deemed to be in compliance with its comprehensive information security obligations
• If there is a data breach of Wyndham’s own systems involving more than 10,000 credit card numbers, Wyndham must obtain an assessment of the breach and provide such assessment to the FTC
• No admission of liability on the part of Wyndham
• No payment of any monetary penalty by Wyndham

KEY TAKEAWAY

Obtaining assessments each year certifying compliance with the Payment Card Industry Data Security Standards (or another approved standard) may provide a “safe harbor” for franchisors.
STATUTORY OBLIGATIONS

- Telephone Consumer Protection Act ("TCPA")
- Americans With Disabilities Act ("ADA")
- Fair and Accurate Credit Transaction Act ("FACTA")
Telephone Consumer Protection Act ("TCPA")

- *Dish Network, L.L.C. v. FCC*, 552 F. App’x 1 (D.C. Cir. 2014)
- *Thomas v. Taco Bell Corp.*, 582 F. App’x 678 (9th Cir. 2014)
- Limits on the liability standard — “apparent authority” and ratification
- “On whose behalf” standard
Americans With Disabilities Act (“ADA”)

- Title III – Places of Public Accommodation
  - Franchisor’s element of control over the franchisee
  - Usefulness of ADA compliance provisions in franchise agreements
Fair and Accurate Credit Transaction Act ("FACTA")

- Applying common law agency principles to conclude vicarious liability
- Balance of control – guidance vs. master-servant relationship
- Indemnity provisions
NEW AREAS WHERE VICARIOUS LIABILITY MAY APPLY

• The Sharing Economy – Uber, Airbnb, Lyft, Couchsurfing, and others

• *Doe v. Uber Techs, Inc.*, 2016 U.S. Dist. LEXIS 60051, at *5 (N.D. Cal. May 4, 2016) – whether an individual is classified as an employee or an independent contractor depends upon whether the person to whom service is rendered has the right to control the manner/means of accomplishing the result desired

Uber’s liability depended upon whether it was, or presented itself as, the driver’s employer


Class actions brought by Uber drivers claiming that, although Uber classified them as independent contractors, they were actually employees and were entitled to benefits and protections accordingly
HOW SHOULD FRANCHISORS LIMIT THE POTENTIAL FOR, AND RISKS ASSOCIATED WITH, CONTROL OF THE FRANCHISEE’S BUSINESS?

• Level of control must be closely monitored
• Governing franchise agreement and system standards must be explicit – franchised business must identify and present itself as an independent contractor
• Conduct periodic inspections to ensure enforcement of same
• Include strong indemnification and insurance provisions in governing contract
Questions & Answers