MESSAGE FROM THE CHAIR

By Joseph J. Fittante
Forum Chair

As an organization, we have undertaken various worthy initiatives over the years. However, there has arguably been no more important initiative undertaken by the Forum than to increase the number of diverse members in the Forum and to encourage their participation in the various Forum activities. This initiative began in approximately 2004, spurred in part by the ABA’s Goal IX Report on racial and ethnic diversity, and in part by Phyllis Alden Truby, the then Governing Committee Liaison to the Women’s Caucus. It was at this time that Forum leadership tasked Phyllis with the job of reaching out to diverse members of the Forum to identify these individuals and encourage their involvement in the Forum. With the support of the Forum’s Governing Committee, Phyllis went about planting the seeds that would lead to the current Diversity Caucus. To that end, Phyllis spearheaded a diversity outreach effort at the 2005 Forum to identify individuals interested in serving on a diversity committee. At that time, the Forum Governing Committee also began an initiative to assist diverse members with identifying leadership opportunities in the Forum. These efforts continued during the 2006 Forum where a program was held on fostering diversity in franchise systems, and further outreach was conducted to those Forum members who self-identified as diverse.

In 2007, recognizing that enhanced diversity would require more of a full-time effort, Forum leadership tasked one of its members in leadership with the full-time job of spearheading Forum diversity efforts. Over the years, this individual has become known as the Forum’s Diversity Officer. At that same time, a community service event held each year at the Forum.

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Do You Know Your Canadian Material? Materiality Under the Arthur Wishart Act

By Frank Robinson and Stefanie Baldassarra
Cassels Brock & Blackwell LLP

Franchise sales in Canada’s most populous province, Ontario, are regulated by the Arthur Wishart Act, S.O. 2000, c. 3 (the “Act”), which requires franchisors to provide pre-sale disclosure (in the form of a disclosure document) to prospective franchisees before a franchise agreement is signed or consideration exchanged. The disclosure document must include prescribed information, as well as all other “material facts.” Furthermore, a franchisor owes a continuing obligation to its prospective franchisees under the Act to disclose any “material change” that occurs between the delivery of the disclosure document and the execution of a franchise agreement.

Courts have acknowledged that the purpose of the Act is to protect franchisees by ensuring that they have the information necessary to enable them to make informed investment decisions, and the Courts have construed the Act liberally to accomplish this purpose. For example, the Ontario Court of Appeal has held that “the purpose of the legislation is to protect franchisees and [that] the mechanism for so doing is the imposition of rigorous disclosure requirements and strict penalties for non-compliance. The legislation must be considered and interpreted in light of this purpose.” 6792341 Canada Inc. v. Dollar It Limited, 2009 ONCA 385, at *72.

In light of the broad definition of materiality, and the judicial inclination to attribute to the Act liberal and purposive meanings, a franchisor engaged in franchise sales in Ontario, and its counsel, should be equipped with an understanding of the meaning and the practical and commercial impact of the materiality concept under the Act. While this article is focused on Ontario’s legislation, the materiality concept is also present in the four other Canadian provincial franchise disclosure statutes.

Section 5 of the Act sets out a franchisor’s obligation to disclose certain information to a prospective franchisee. With respect to the content of the disclosure document, as defined more fully below, the Act imposes the duty to disclose “material facts” (section 5(4)(a)) and “material changes” (section 5(5)).

There are no legislative or judicial guidelines that establish exactly what kinds of facts or changes are “material” in the context of a franchise relationship. In general, Courts have taken a “purposive” approach to assessing materiality, deciding the question on a case-by-case basis against the backdrop of the acknowledged purpose of the Act. As a result, a body of case law has developed to give texture and meaning to the otherwise broad and indefinite legislative concepts.

I. Defining “Material Facts”

The Act, at section 1(1), defines a “material fact” to include “any information about the business, operations, capital or control of the franchisor or franchisor’s associate, or about the franchise system, that would reasonably be expected to have a significant effect on the value or price of the franchise to be granted or the decision to acquire the franchise.”

The Courts have assessed the “material fact” requirement in the context of several franchise disputes. The case law teaches that a broad array of facts and circumstances may be considered “material,” depending on the context and the particular franchise at issue.

For example, in Dollar It, the franchisor had failed to provide a copy of a head lease under which the franchisee was expected to enter a sub-lease. As is common in most sub-leases, the particular sub-lease included a term that the signatory had received a copy of the head lease and was familiar with its terms. The Court found that the head lease was a material fact that ought to have been disclosed. Asked the Court: “How could the franchisee, who is the sub-tenant under the sub-lease, ever comply with its acknowledgement obligation without receiving a copy of the head lease?” Id. at *19. The Court concluded that the head lease “was obviously material and required to be disclosed.” Id.
While the Court only commented on the need to provide a copy of the head lease, the principle from this case, and those which follow, suggests a trend toward interpreting and applying the materiality concept in such a way that a template form disclosure document, which includes the system’s basic information and documents, may not suffice in cases where site-specific circumstances differ from the basic information and documents contained in the template form disclosure document.

“In general, Courts have taken a ‘purposive’ approach to assessing materiality, deciding the question on a case-by-case basis against the backdrop of the acknowledged purpose of the Act.”

The risk in relying on generic disclosure in cases where a franchisor has specific knowledge of unique material facts was exemplified in 1518626 Ontario Inc. v. Tutor Time Learning Centre LLC (2006) 150 A.C.W.S. (3d) 93. In this case, Tutor Time Learning Company (“TTLC”) provided the franchisee with a U.S. Uniform Franchise Offering Circular. The franchisee sued for rescission under section 6 of the Act. The main issue was whether the UFOC satisfied the Act’s disclosure requirements.

The Court found that unlike the UFOC, an Ontario disclosure document is “evergreen” and must be updated to reflect all material facts existing at the date of the use of the document. In this case, TTLC failed to update the UFOC to include two site visit reports, in which a TTLC representative reported serious problems with the overall management of the franchise in question. The Court found that the failure to deliver an Ontario disclosure document which included this information meant that no disclosure document had been given under the Act. The Court concluded that “the UFOC did not provide the material facts pertinent to the Burlington franchise [and] this non-disclosure of material facts in itself meant there was not compliance with the Act as to the required disclosure.” Id. at *75.

The Superior Court came to a similar conclusion in the recent case of Sirianni v. Country Style, 2012 ONSC 881. In this case, the franchisor and franchisee renewed an existing franchise agreement for ten years. When the franchisor forwarded disclosure documents to the franchisee, it failed to disclose the fact that it had reached an agreement with the landlord for early termination of the lease for the premises. The Court found that the term of the lease was “clearly a material fact,” and held that withholding such a material fact made the disclosure completely inadequate. Id. at 124. The plaintiff franchisee was awarded damages under section 6(2) of the Act as well as punitive damages in the amount of $25,000.00 for deliberate withholding of information. In these circumstances, the failure to disclose a single document was held to be tantamount to no disclosure. Id. at 109.

Because there is no definitive scope to the materiality concept, Courts will continue to interpret the concept on a case-by-case basis in order to protect the interests of franchisees. Courts will even go so far as to invalidate an otherwise compliant disclosure document that fails to properly disclose material facts, whether they are system-wide facts or are particular to the franchise for which disclosure is being made.

II. Defining “Material Change”

The Act, at section 1(1), defines a “material change” as “a change in the business, operations, capital or control of the franchisor or franchisor’s associate . . . that would reasonably be expected to have a significant adverse effect on the value or price of the franchise to be granted or on the decision to acquire the franchise.” This includes “a decision to implement such a change” made by the board of directors or by senior management who believe that confirmation of the decision is probable.

The Act’s stated definition of “material change” is focused on operational changes having a significant adverse effect on the value or price of the franchise. The definition applies an objective standard, as the effect must be “reasonably expected.” Such effect must be significant and adverse and must affect the value or price of the franchise or the decision to purchase the franchise. Finally, the material change must be linked to either “the business, operations, capital or control of the franchisor or franchisor’s associate [or] the franchise system.” Id.
The statutory definition of “material change” must be interpreted with reference to the common law test for materiality recently set out by the Supreme Court of Canada in Sharbern Holding Inc. v. Vancouver Airport Centre Ltd., [2011] 2 S.C.R. 175 (“Sharbern”), which established the following five key principles concerning materiality. First, materiality is a question of mixed law and fact, determined objectively from the perspective of a reasonable investor. Id. at 61(i). Second, an omitted fact is material if there is a substantial likelihood that it would have been considered important by a reasonable investor in making his or her decision, rather than if it might have been considered important. Id. at 61(ii). Third, the proof required is not that the material fact would have changed the decision, but rather, that there was a substantial likelihood it would have assumed actual significance on a reasonable investor’s decision. Id. at 61(iii). Fourth, materiality involves a fact-specific inquiry, to be determined on a case-by-case basis in light of all of the relevant considerations. Id. at 61(iv). Finally, materiality must be proven through evidence by the party alleging materiality, except in those cases where common sense inferences are sufficient. Id. at 61(v).

In Trillium Motor World v. General Motors of Canada Ltd., 2012 ONSC 463, the Superior Court applied the Sharbern principles in the context of a franchise class action to determine whether or not a change “would reasonably be expected to have a significant adverse effect” on the value, price or decision to enter the franchise agreement. The Court determined that this was the applicable threshold of “significance.” Id. at 19-24. Similarly, in Emerald Developments Ltd. v. 768158 Alberta Ltd., 2001 ABQB 143 (“Emerald”), the Alberta Court of Queen’s Bench found that the Act’s focus on protecting the franchisee from making the decision to purchase the franchise in the absence of sufficient or accurate information is to be assessed on a substantive, rather than technical, basis. Id. at 18. In other words, not all changes are material; rather, only those changes which, when viewed objectively, would have an effect upon the franchisee’s decision to invest in the franchise are essential to disclosure.

The contextual approach has also been followed outside the franchise setting. Securities cases are emphatic that material changes are to be viewed from a substantive, rather than purely technical, perspective. In Coventree Inc. (Re), 2011 LNONOSC 757, the Ontario Securities Commission ruled that when considering a material change under the Securities Act, “one should not take a supercritical or technical approach to the interpretation of what constitutes a change in the business or operations of an issuer,” but rather, look at whether an undisclosed change would have been considered to be substantively important to the investor when making their decision. Id. at 582.

While the foregoing jurisprudence provides some guidance regarding what is to be considered “material” in the context of franchise disclosure under the Act, the meaning of “material change” remains vague. The challenge posed to practitioners is that the guidelines and standards as provided by current law do not, together, create a “bright line” rule against which to evaluate the myriad of factual situations attendant to any given franchise sale. In any event, whether a fact can be deemed to have a significant adverse effect on either the value or price of the franchise or the franchisee’s decision to acquire the franchise remains a critical question that franchisors must continue to address when preparing and updating disclosure documents in Ontario.

III. Conclusion

Because the case law remains inconclusive about what constitutes either a “material fact” or a “material change” under the Act, it is important for franchisors to closely examine all of the circumstances of the franchise relationship when deciding what documents and information to disclose in advance of a franchise sale transaction. There is a “heavy onus” on the franchisor to determine what information is material and the Courts have been clear that the Act will be interpreted in favour of greater disclosure. Both franchisors and legal counsel should be mindful that a failure to disclose material information could result in an award of damages or rescission of the franchise agreement under section 6 of the Act. While such drastic consequences will be present so long as the Act is in force, it is hoped that a continually maturing and evolving body of case law will help to create more conclusive and reliable principles upon which franchisors and their advisors can rely.
Termination for a Criminal Conviction: Cruel and Unusual Punishment?

By Brigid A. Harrington
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I. Termination for Breach of Specific Franchise Agreement Provisions

Franchise agreements generally contain several provisions that purport to outline parameters for when a criminal conviction constitutes breach. For example, franchise agreements often times contain a clause requiring the franchisee not to be convicted of any crimes, or any specified types of crimes; in the absence of statutory limitations on termination, the fact of a conviction itself regardless of its impact on the business renders the franchisee in breach of these provisions. See, e.g. Shieh v. Kumon N.A., Inc., No. C 05-5285, 2006 WL 2285628 (N.D. Cal. Jan. 6, 2006) (franchisee terminated for pleading “no contest” to battery for inappropriately touching a child where franchise agreement provided for termination for convictions of, or no contest pleas to, crimes against children). Franchise agreements may also require franchisees to “obey all laws” in connection with the operation of the business, which leaves open the possibility that convictions for behavior not related to franchise operations may not necessarily result in termination. See, e.g. Dunkin Donuts v. Gen. Stores Donuts, Inc., 139 F.Supp.2d 147, 154 (D. Mass. 2001). Similarly, provisions requiring a franchisee to refrain from engaging in conduct that results in injury to the franchisor’s “goodwill” often times are deemed to have been breached via a franchisee’s criminal conviction, provided that the franchisor can show that its business or reputation with consumers has been damaged or injured as a result of the franchisee’s criminal conduct and/or conviction. See, e.g. id. at 153. Finally, provisions that require the franchisee to participate in the day-to-day operation of a franchised business may be breached by a franchisee if a criminal conviction is accompanied by a sentence that includes incarceration. See, e.g. Parsippany 2, 2012 WL 4465517, at *4 (termination upheld because franchisee’s three-year prison term meant he could not participate in day-to-day operations of franchise as required under the franchise agreement).

II. Termination Under State Laws

Even if the terms of a franchise agreement do not require a criminal conviction to negatively impact the franchised business in order to constitute grounds for an immediate termination, such requirement may nonetheless be imposed by state- or industry-specific laws. For example, the New Jersey Franchising Practices Act (“NJFPA”)
provides that a franchisor may immediately terminate a franchise agreement based on a criminal conviction only if the crime is “directly related to the business conducted pursuant to the franchise.” N.J. Stat. § 56:10-5. Otherwise, a franchisor may only terminate upon a showing of “good cause” and after giving 60 days’ notice to the franchisee. Id. The question of whether a conviction constitutes “good cause” for an immediate termination of a franchise agreement often hinges on considerations of whether it is harmful to the franchised business, harmful to the franchisor-franchisee relationship or, otherwise renders the franchisee unable to perform his or her obligations under the franchise agreement. See, e.g. General Motors Corp. v. The New A.C. Chevrolet, Inc., 91 F.Supp.2d 733 (D. N.J. 2000) (franchisee’s operation of franchise of a second auto dealership franchise with a different auto manufacturer without original franchisor’s consent sufficient grounds for termination under NJFPA); GlensideW. Corp. v. Exxon Co., U.S.A., 761 F.Supp. 1119 (D. N.J. 1991) (franchisee’s threats against franchisor’s personnel and property sufficient grounds for termination under NJFPA and Petroleum Marketing Practices Act (“PMPA”)). Similar to the NJFPA, franchise statutes in California and Illinois impose similar limitations on a franchisor’s ability to immediately terminate a franchise agreement “without cause,” as do industry-specific statutes such as the PMPA which requires that a crime involve “moral turpitude” in order to form the basis for a termination. See 15 U.S.C. ch. 55; Cal. Bus. & Prof. Code § 20021; 815 Ill. Comp. Stat. 705.

Thus, unless a franchise agreement provides for an immediate termination upon conviction of the crime in question, and there also is no applicable statute regulating the franchise relationship, the propriety of the termination will likely involve an analysis of the conviction’s effect on the franchised business. Indeed, in cases where the conviction relates to activity carried out in the operation of the franchised business, such as tax fraud, the answer is obvious, i.e., a franchisor’s immediate termination of the franchise relationship is valid and proper. See Dunkin Donuts v. Martinez, No. 01-3589-Civ., 2003 WL 685875, at *10 (S.D. Fla. Feb. 21, 2003) (termination for filing false tax returns claiming personal expenses as expenses of the franchised business upheld). But in cases where the crime is committed outside of the premises of the franchised business and does not involve the operation of the business, the question is much more difficult – i.e., can a franchisee’s criminal activity in his or her personal life be said to affect the goodwill or reputation of the franchised business, or the franchisee’s ability to adhere to the terms of the franchise agreement? The answer is often fact-specific, and whether termination is proper often rests on whether the franchisor can meet its burden of showing a negative impact or other clear, material breach of the franchise agreement.

III. The Parsippany Pancake House Decisions – Effect on Franchised Business

The Parsippany Pancake House decisions certainly illustrate the considerations that factor into this analysis. As previously mentioned, in that case, the president and majority owner of the franchisee was convicted of endangering the welfare of a child for sexually assaulting a minor. See Parsippany, 2012 WL 4465517, at *4; Parsippany 1, 2012 WL 2476407, at *1. The criminal conduct did not occur on the franchised premises, and was not otherwise related to the operation of the franchise. Compare Parsippany 1, 2012 WL 2476407, at *1 with Shih, 2006 WL 2285628, (no contest plea for battery against a child was related to the operation of an after-school learning franchise). At the same time, the franchisee was convicted of a felony and was required to register as a sex offender, with an accompanying sentence of at least three years in prison. See Parsippany 1, 2012 WL 2476407, at n. 2. However, the conviction had not been publicized in local news media, and IHOP could make no showing that the franchisee’s conviction had resulted in any damage to IHOP’s reputation. See id. at 3-4. It appeared that his conviction had almost no demonstrable effect on the franchised business, as revenues at the franchised location remained consistent. See
id. Because IHOP was unable to produce any evidence that the conviction impacted the business, the Court prohibited IHOP from immediately terminating the franchise agreement as IHOP had not met its statutory burden of showing that the conviction was directly related to the franchised business. See id. The Court stated that the potential for harm to the business was not enough to support immediate termination under the NJFPA; at the very least, actual harm must be shown. See id.

Once IHOP had given the franchisee 60 days’ notice of termination, however, the Court did enter a preliminary injunction enforcing the termination reasoning that the criminal conviction and its accompanying three-year sentence did constitute “good cause” for termination under the NJFPA. See Parsippany 2, 2012 WL 4465517, at *4. The Court recognized the potential harm of having a convicted sex-offender operate a business with a family friendly reputation – an argument which it had previously rejected as a basis for immediate termination – but also relied on IHOP’s clause that required the franchisee to engage in day-to-day operations of the business, noting that because the franchisee would have to spend three years in prison, day-to-day operation would be impossible. See id.

The Parsippany Pancake House decisions are significant because of their in-depth analysis of the conviction’s actual effect on the franchised business. See id.; Parsippany 1, 2012 WL 2476407, at *3-4. The Court rejected the view that criminal conviction harms a business’ goodwill as a matter of law and looked at the conviction’s actual impact. See Parsippany 2, 2012 WL 4465517, at *4; Parsippany 1, 2012 WL 2476407, at *3-4. Significantly, the Court refused to assume that potential reputational harm to the franchisor was equivalent to actual harm and, instead, required the franchisor to satisfy its burden to demonstrate tangible damage before it could find cause for termination. See Parsippany 2, 2012 WL 4465517, at *4; Parsippany 1, 2012 WL 2476407, at *3-4. Notably, the termination ultimately hinged not on reputational damage caused by conviction of a notorious crime, but rather on the practical consideration that the franchisee could not fulfill his duty to be involved in day-to-day operations of the franchise while incarcerated. See Parsippany 2 Pancake House, 2012 WL 4465517, at *4.

Such an analysis of actual harm to the franchised business is important because once a criminal conviction has been found to harm a franchisor’s business and/or goodwill, it can lead to an incurable breach of the franchise agreement. In Gav-Stra Donuts, for example, the Court found that although non-criminal members of a franchisee partnership took measures to exclude a partner who had engaged in, and was later convicted of, an illegal kick-back scheme with a supplier, the damage that the criminal partner had done to Dunkin Donuts’ goodwill remained grounds to terminate all partners as franchisees. See Gav-Stra Donuts, 139 F.Supp.2d at 154-55. Despite the fact that the non-criminal partners actually reported the criminal partner’s activity to Dunkin and the IRS, recovered illegally diverted revenues, and even obtained a restraining order prohibiting the criminal partner from participating in the business, the Court found that “the genie had been let out of the bottle,” and that the non-criminal franchisees’ good-faith efforts to cure could not remedy the damage caused to Dunkin Donuts’ goodwill via media coverage of their partner’s crimes. See id. at 155. As a result, although the innocent partners did what would seem to be in the franchisor’s and society’s interest by reporting the criminal partner’s illegal activity, they were ultimately punished for their partner’s behavior via a termination of their franchise.

IV. Conclusion

Gav-Stra Donuts illustrates the implications that a franchisee’s criminal convictions can have on potentially innocent partners. Other consequences of termination, such as lost future royalty claims may be equally harsh, and perhaps more punitive than sentences for minor criminal offenses. Because the consequences of termination can be severe, Courts should not automatically assume that a criminal conviction necessitates termination of a franchise relationship. Instead, they should follow the lead of the Parsippany Pancake House Court and require franchisors to show that the conviction negatively impacts their business and that termination comports with applicable law. After all, the health of a franchised business is where a franchisor’s interest rightfully lies. Appropriate punishment for criminal activity unrelated to the franchised business can and should be meted out by the courts, and not by the franchisor.
What All Franchise Lawyers Should Know About the Recent Changes to Ohio’s Business Opportunity Law

By G. Jack Donson
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On June 26, 2012, Governor Kasich signed Substitute Senate Bill 196 into law. This Act amends several sections of Ohio’s Business Opportunity Plan Law, Revised Code Sections 1334.01 et seq. (the “OBOPL”). Originally enacted in 1979, the OBOPL is, like many other state business opportunity laws, not limited to regulating the sale of typical business opportunity plans. Rather, the courts consistently have interpreted the OBOPL to apply to the sale of franchises in Ohio. Peltier v. Spaghetti Tree, Inc., 6 Ohio St. 3d 194, 451 N.E.2d 1219 (1983); 6100 Cleveland, Inc. v. Staff Builders, Int’l, Inc., 127 F. Supp. 2d 877 (N.D. Oh. 1999). And, unlike the FTC Franchise Rule that regulates the sale of franchises, 16 C.F.R. § 436 (2007) (the “FTC Rule”), the OBOPL creates a private right of action. Franchisees may sue for treble damages, rescission, attorney fees, and other relief where the franchisor violates the statute.

As discussed below, the 2012 amendments clarify and modestly expand the coverage of the OBOPL. The 2012 amendments also address, but do not completely eliminate, potential pitfalls facing franchisors that rely upon compliance with the FTC Rule to exempt sales of franchises in Ohio from the OBOPL. Finally, the 2012 amendments make several changes as to the private right of action, some of which benefit franchisors, and some of which benefit franchisees.

The following describes the changes to Ohio’s business opportunity law that it is important for franchise lawyers to know.

1. As alluded to above, the OBOPL subsumes more than traditional business opportunities, such as those involving the sale of rack displays and vending machines. The definition of “business opportunity plan” includes an agreement to obtain the right to sell goods or services, whereby (a) the goods or services are supplied by the seller of the business opportunity, a recommended third party, or an affiliate of the seller, (b) the purchaser is required to make an initial payment of between $500 and $100,000, and (c) the seller represents “there is a market for the goods or services.” Ohio Revised Code § 1334.01(D). As the cited cases confirm, unless exempt, in most cases, the sale of a franchise in Ohio is subject to the OBOPL.

2. Compliance with the OBOPL is relatively straightforward. In addition to complying with the anti-fraud provisions, the seller of a business opportunity must provide a statutorily prescribed disclosure statement to the purchaser at least 10 days prior to the execution of the agreement selling or leasing the business opportunity. Id. at § 1334.02. The mandated disclosure form is similar to that required by other state business opportunity laws. The seller also must provide prominent notice, in the manner prescribed in the statute, that the purchaser has the right to cancel the purchase of the business opportunity without penalty during a five-day “cooling off” period following the signing of the agreement. Id. at § 1334.06. This requirement very clearly is not met by a typical franchise disclosure document. As discussed in #5 below, this has created problems for franchisors that do not provide the Ohio prescribed disclosure statement and notice of cancellation, and instead rely on the exemption in Section 1334.13 for transactions that comply with the FTC Rule.

3. The 2012 amendments both clarify and modestly expand the coverage of the OBOPL. The amendments modify the definition of “initial payment” in Section 1334.01 (G) to make clear that the statute does not apply to traditional wholesale distributorships or retail dealerships. This is accomplished by adding language that initial payment “does not include purchases at bona fide wholesale prices of reasonable quantities of goods or services for resale or lease.” Id. The amendments expand the number of franchisees entitled to the protection of the OBOPL. Previously, a franchisee did not have the protection of the OBOPL where the franchisee’s initial payment exceeded
Courts have ruled that where the seller does not have provided the franchisee with written notice of the five-day cooling off period described above. The amendments increase this amount to $100,000 allowing more franchisees to receive the benefit of the statute. In practice, this represents an increase of more than $50,000, since goods purchased at bona fide wholesale prices no longer would count towards the calculation of the maximum initial payment. Likewise, the exemption at Section 1334.12 (M) for “experienced franchisees” was narrowed so that franchisees having no prior experience with the franchisor or its trademark now fall outside that exemption and have the benefit of the statute. The amendments also update the large franchisor exemption. When adopted in 1979, the large franchisor exemption required, inter alia, a net worth of only $5 million or more. The amendments increase this amount to $15 million to keep pace with the Consumer Price Index increases since 1979. Id. at § 1334.12 (L) (1). This change makes more franchisors subject to the statute.

4. As enacted in 1979, Section 1334.13 exempted from the OBOPL any transaction that “fully complies with the trade regulation rule of the federal trade commission . . . concerning franchising,” 16 C.F.R. 436.1 et seq.” Most franchisors selling franchises in Ohio have relied on this exemption and have not complied with the different disclosure requirements of the OBOPL. The “fully complies” language has proven to be problematic. It has allowed unsuccessful or unhappy franchisees opportunistically to claim that their purchase of a franchise was not exempt because of minor or immaterial failures by the franchisor to comply with the FTC Rule. Having relied on the exemption, the franchisor would not have complied with the OBOPL disclosure requirements and would be subject to claims for rescission, treble damages, attorney fees, and other relief. The 2012 amendments lessen the risk of such opportunistic behavior by replacing the “fully complies” language with “complies in all material respects” with the FTC Rule. The 2012 amendments also update the language of Section 1334.13 to conform to 2007 amendments of the FTC Rule.

5. Court decisions have exacerbated the exposure of a franchisor that faces a claim that the transaction was not exempt pursuant to Section 1334.13 because the franchisor did not comply with the FTC Rule. A franchisor that is relying on the exemption of Section 1334.13 typically will not have provided the franchisee with written notice of the five-day cooling off period described above. Courts have ruled that where the seller does not provide written notice of the five-day right to cancel, the statute of limitation never begins to run. RY/EH, Inc. v. Arthur Treacher, Inc., 685 N.E.2d 316 (Ohio App. 1996); 6100 Cleveland, Inc., supra. The RY/EH, Inc. decision further rules that the five-day right to cancel never begins to run where the seller does not provide the written notice of the purchaser’s right to cancel. These decisions effectively allow the franchisee to sue in perpetuity or to have a perpetual cooling off period where the franchisor does not give written notice of the right to cancel. The 2012 amendments correct this by (i) limiting the right to cancel to one year after execution of the franchise agreement and (ii) limiting the right to sue for damages to five years after execution of the franchise agreement. Ohio Revised Code §§ 1334.05(A) and 1334.10(C).

6. In addition to clarifying the application of the statute of limitations and the right to cancel, the 2012 amendments make other changes to the franchisees’ private right of action for violations of the OBOPL. Franchisors will benefit from the amendment to Section 1334.09 (A). Prior to the amendments, this section allowed the franchisee the full period of the statute of limitations to sue for rescission where the franchisor violated the OBOPL. The amendments limit the period for seeking rescission by requiring the franchisee to give written notice of the claim of rescission within three years after the date of the franchise agreement. This modification recognizes both that (i) rescission becomes increasing impractical with the passage of time, and (ii) the franchisee has other powerful remedies in addition to rescission. Section 1334.09 (C) is modified to provide that exercise of the right to rescind does not entitle the franchisee to unjust enrichment.

7. Franchisees will benefit from the changes to Section 1334.08 and 1334.15. With respect to claims arising under the OBOPL, the 2012 amendments to Section 1334.08 declare void any provision in an agreement restricting jurisdiction or venue to a forum outside of Ohio or requiring the application of laws of a state other than Ohio. Id. at §1334.08 (E). Section 1334.15 reinforces the above including by making void and unenforceable “any venue or choice of law provision that deprives a purchaser who is an Ohio resident of the benefit of the OBOPL.”

Overall, the 2012 amendments clarify and improve the OBOPL in numerous respects and in a balanced manner that provides needed protection to both franchisees and franchisors.
The Importance of 30(b)(6) Designee Decisions

By Trenten P. Bausch
Cline Williams Wright Johnson & Oldfather, L.L.P.

Legally formed organizations are “persons” but can only act through the people that run them. Fed. R. Civ. P. 30(b)(6) (the “Rule”) may be the most effective tool for obtaining an organization’s testimony. Upon receiving proper notice of the matters for examination, the organization must “designate one or more officers, directors or managing agents, or designate other persons who consent to testify on its behalf . . . .” A common misapplication of the Rule is a knee-jerk reaction to designate the primary actor in the dispute. I see at least two problems with this approach. First, the primary actor will likely be deposed personally. Designating the primary actor gives the other side two bites at the apple. Second, the person who committed the act to land the organization in the lawsuit is often not the best choice as the face for the organization.

Upon receipt of proper notice, the organization should conduct an analysis of which person has the skill set to best reflect the organization’s theme. If the result is that no one person can tell its story, then the organization should designate more than one person. Finally, as the Rule contemplates, the best choice as the voice for the organization may not even be currently employed by the organization. The designee decision is an important one. As the last Knight Templar said to Indiana Jones in The Last Crusade, “You must choose, but choose wisely.”

FTC FAQ #37: Complying with Item 12 Territory Disclosures

By Eleanor Vaida Gerhards
Fox Rothschild LLP

New “FAQ #37” released by the Federal Trade Commission (FTC) makes clear that a franchise system reserving the right to develop “non-traditional venues” within territories granted to franchisees must disclose it does not provide franchisees with an exclusive territory.

According to the FTC, a franchisor that reserves the right to open franchised or company-owned outlets at “non-traditional venues,” such as airports, arenas, hospitals, malls, schools, stadiums, theme parks, or parks, physically located within a franchisee’s territory cannot state in Item 12 of its FDD that it grants an “exclusive territory.”

A franchisor may still grant an “exclusive territory” if it reserves the right to other channels of distribution within a franchisee’s territory, including the Internet, telemarketing, or catalogs, because these channels do not require an outlet to be physically located in the franchisee’s territory. However, FAQ #37 clarifies that, as soon as a franchisor reserves rights relating to the location of non-traditional venues within a franchisee’s territory (which is a fairly common, industry-wide practice), the franchisor may not use the term “exclusive territory.”

If you represent a franchise system which reserves the right to locate non-traditional venues within the territories granted to franchisees, you should:

• confirm that the FDD Item 12 disclosure includes the mandated disclaimer that franchisees will not receive an exclusive territory; and
• ensure that the franchisor cease using the term “exclusive” to describe a franchisee’s territory. As an alternative, a franchisor may consider using the term “protected” to describe a franchisee’s territory if a franchisor offers some territorial protection to franchisees but less than full exclusivity.
Under FAQ #29, the FTC will not recommend an enforcement action based on a new FAQ until a franchisor is otherwise required to revise its FDD. Therefore, any changes to Item 12 may be completed during the franchisor’s next required annual update, amendment, or renewal filing (unless state law requires otherwise). Given that the renewal season is starting soon for those franchise systems with a December 31 fiscal year end, franchise attorneys should begin tailoring compliant disclosure language for their franchisor clients or employers now.

**New FTC Business Opportunity Rule May Apply to Some Exempt Franchisors**

By Beata Krakus  
Greensfelder, Hemker & Gale, P.C.

While not all franchise systems are suited for exemption-based franchising, there are a fair number of franchisors that take advantage of the exemptions contained in the FTC Franchise Rule. 16 C.F.R. § 436.8 (2007). However, franchisors relying on the minimum initial payments exemption, 16 C.F.R. § 436.8(a)(1), as well as those (likely few) relying on the no written documents exemption, 16 C.F.R. § 436.8(a)(7), to avoid applicability of the FTC Franchise Rule, need to take a close look at the new FTC Business Opportunity Rule, 16 C.F.R. § 437 (2011), which went into effect on March 1, 2012. The new FTC Business Opportunity Rule contains an exemption for franchises subject to the FTC Franchise Rule, but this exemption specifically excludes those franchises exempted from the FTC Franchise Rule because of the two exemptions described above. 16 C.F.R. § 437.8. This is not to say that all franchises falling outside the franchise exemption will necessarily be subject to the disclosure requirements of the FTC Business Opportunity Rule. The definition of a business opportunity may still not apply to the franchise system, and thus the franchisor can escape the relatively light disclosure obligations of the FTC Business Opportunity Rule. Franchise practitioners, however, will definitely want to analyze this issue for any franchisors relying on either the minimum initial payments exemption or no written documents exemption to ensure that they are not subject to any additional disclosure requirements under the FTC Business Opportunity Rule.
Annual Forum Community Service Event

What does unqualified success look like? The Community Service Event held on October 13, 2012, at the Los Angeles Food Bank and co-sponsored by the Corporate Counsel Committee, Women’s Caucus and Diversity Committee. Participants in the event helped to demonstrate the Forum’s continued commitment to giving back by packing bags of donated food, including everything from rice and beans to cans of fruit, to fight hunger in the Los Angeles community. The collegial atmosphere allowed in-house and outside counsel to get to know each other better, sometimes while comparing memories of the great 70’s and 80’s music playing in the background, or engaging in robust discourse over the optimal food packing techniques. For those of you who participated, the Los Angeles Food Bank and the Forum give their sincerest thanks. For those who did not participate, next year is another opportunity to take a moment and give back. And so, we leave you with this question: How many lawyers does it take to pack more than 1,000 bags of food for those in need? Answer: None. It takes about twenty, fantastic, giving, caring people. Until next year!

It is my honor to report that the Forum’s commitment to diversity has resulted in the Forum’s receipt of the 2012 Diversity Award by the ABA’s Center for Professional Development. The Diversity Award is given to the ABA entity with the highest percentage of diverse faculty members presenting in programs facilitated by the Center. As measured against the other ABA entities, the Forum won the 2012 Diversity Award with a 78% rating, which exceeds last year’s high of 61.54%. This honor was presented to the Forum in early November at a reception held at the ABA’s headquarters in Chicago. I would like to extend a special thank you to Kerry Bundy who, as the Forum’s Program Officer, has worked to ensure that our teleseminar and local programming panels reflect a diverse mix of presenters.

This recent award would not have been possible without the work of many over the last number of years, both in and outside of Forum leadership. Thank you for all of your efforts to date. Although much has been accomplished, there remains much to be done on this front. We must continue to ensure that diversity in leadership, as well as participation, remains one of our top priorities.

Message From the Chair
Continued from cover
Tribute to Charles Cannon

Joyce Mazero
Haynes and Boone, LLP

Charles Cannon - remarkable scholar, sought after counselor and peacemaker, loving father and husband, dedicated partner and friend passed away on December 3, 2012 in Austin, Texas.

His life is distinguished by notable accomplishments in academia, having graduated from prestigious Yale Law School and Yale Divinity School, and in his numerous writings and law and mediation practices, giving his readers and his clients the benefits of his thoughtful analysis of issues through his wit, wisdom and experience. His life is distinguished by a unique ability to connect to people and effectively bring their problems to resolution. Charles had a giving spirit, exemplified in volunteering to teach young children the game of golf, his many pro-bono mediation activities and as an organ donor. His life is distinguished by love and loyalty as husband to Gayle Cannon and father and grandfather to children and grandchildren, who clearly returned that love.

One of the endearing memories I have is seeing Charles and Gayle, married for over 34 years and having practiced law together for almost as many, coming to ABA Forum events, always together, united in growing their business and firmly invested in each other's professional success. As a former partner of Charles, I remember fondly how much I enjoyed dining out with Charles and clients—he was a “foodies” and truly a wine expert, admired for his ability to select the very best in food and wine, making each event seem like it was customized just for the guests.

Charles always had a ready hand to shake, was competitive but always professional, and was witty to a fault, soothing others with humor and his calm, but clear thoughts, whenever he was asked to help.

Charles passed away on a beautiful day while playing golf with his best friends at his side. At his service, I was impressed by the consistent theme that was in some way reassuring - Charles’ family, friends and colleagues knew so well how much he loved and cared for them and those special relationships will carry on.

— Joyce Mazero, December 19, 2012
COVENANTS AGAINST COMPETITION IN FRANCHISE AGREEMENTS
THIRD EDITION

Michael R. Gray and Natalma M. ("Tami") McKnew, Editors

Save time drafting, negotiating and litigating franchise agreements with the updated Covenants Against Competition in Franchise Agreements, Third Edition. Since franchising has become an international industry in the past decade, this updated Third Edition has been expanded to include chapters on Canada and Mexico, making this a complete North American publication.

This publication provides a framework for comparative analysis of this critical topic in the franchise context throughout North America. This book gives franchisors, franchisees and their counsel a single source for the most current franchising statutory and decisional law in each of the 50 states, Washington, DC, Puerto Rico, U.S. Virgin Islands, Canada and Mexico.

An outline of issues addressed for each country and state includes:

- Have the courts articulated the "legitimate interests" of the franchisor that will support enforcement of a covenant against competition contained in a franchise agreement?
- What time limitations have courts recognized as reasonable in the franchise context?
- What geographic limitations have courts recognized as reasonable?
- What limitations on activities have courts recognized as reasonable in the franchise context?
- Does the state recognize a difference between in-term and post-term covenants?
- Has the state allowed enforcement of covenants against non-signatories?
- Will the state modify, "blue pencil" or otherwise reduce a covenant found to be overbroad?
- When does a non-compete period begin to run?
- Are there additional nuances in the state’s treatment of covenants in the franchising context?

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Susan Grueneberg and Ann Hurwitz, Editors

The FTC Franchise Rule, Second Edition, serves as an analytical tool and a comprehensive, practical guide for franchise law practitioners, including “old hands” and those who are new to the practice of franchise law. It is not only an important resource for understanding the latest interpretations of the FTC Franchise Rule, but also includes updated, additional source materials essential to the interpretation of the FTC Franchise Rule’s disclosure requirements.

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Jeffrey A. Brimer, Editor

The Franchise Law Compliance Manual, Second Edition, represents an essential addition to every franchise lawyer’s library. Designed as a working tool for corporate franchise lawyers, outside counsel, and franchisee counsel, the updated Second Edition is a practical, comprehensive guide to establishing and maintaining a successful corporate compliance program.

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