BUSINESS LAWS AND REGULATIONS THAT AFFECT FRANCHISE SYSTEMS

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BUSINESS LAWS AND REGULATIONS THAT
AFFECT FRANCHISE SYSTEMS

I. INTRODUCTION

This paper discusses a variety of non-franchise-specific laws that affect the franchise relationship and what every franchise lawyer, whether in-house or outside counsel, and whether franchisor or franchisee oriented, should know about them.

Our goal is to increase the franchise lawyer’s knowledge and awareness of these laws, and the issues that they create. We do not intend to make experts out of the reader because we can only provide a brief introduction to these disparate and myriad laws. But we have provided the reader with tools needed to undertake further research and/or make a state-specific analysis.

The paper addresses three broad categories of laws: (1) hospitality industry related laws, (2) consumer focused laws, and (3) general operational laws. Those laws may affect both the franchisor and franchisee directly, or they may be primarily imposed on the franchisee’s operations, but with a risk that the franchisor could be exposed to vicarious liability for the franchisee’s failure to comply.¹

II. IMPACT OF BUSINESS LAWS ON THE FRANCHISE RELATIONSHIP

All franchised businesses are subject to a wide variety of non-franchise-specific laws and regulations. But certain laws may raise particular issues for franchisors and/or franchisees, or may affect the franchise relationship. While a violation of a federal, state or local law may create liability for the franchisee or the franchisor-operator of a business, it may also cause negative publicity or adversely impact sales. A franchisor may be vicariously liable for the illegal actions of its franchisees. The existence of certain laws may suggest a need for specific franchisee training to insure compliance and/or improve operations at the unit level. And, in some cases, the franchisor must describe certain business laws and regulations in the Franchise Disclosure Document (“FDD”) and/or franchise agreement. While the potential franchise-specific effects do not arise with respect to all business laws and regulations, counsel should be mindful of these issues when evaluating the laws and/or counseling clients. The business laws that are addressed in this paper may impact the franchise relationship, or may raise franchise-related issues, in one or more of the following areas:

A. Compliance and Liability – Generally

For franchisees, and for franchisors (or affiliates) that operate outlets, it is axiomatic that failure to comply with business laws and regulations may give rise to liability to third parties (e.g., claims by a patron who is denied service because he/she attempts to enter the premises with a service animal; or a complaint lodged by a consumer who was unfairly prevented from canceling a membership contract). In addition, for a franchisee, a failure to comply with

¹ The authors wish to thank Shelly Gopaul (an associate at Bryan Cave LLP, Santa Monica, CA), Christopher Feldmeir (an associate at Greensfelder, Hemker & Gale P.C., St. Louis, MO) and Meg Loveless (a paralegal at Plave Koch PLC, Reston, VA) for their respective contributions to this paper.
applicable laws and regulations may be grounds for default under and termination of the franchise agreement. Compliance with applicable laws is necessary for operational survival.

B. Brand Goodwill

Compliance with business laws and regulations – or more appropriately, a failure to comply – may have significant and possibly long-term consequences for a franchise network. Clearly, a single franchisee’s compliance or lack of compliance with laws could impact his/her/its business, with consequences that could legally or financially ruin the business. But a failure to comply with a law or regulation could have wider consequences. If the press reports on even a single legal infraction by one outlet, the entire network may be tarred by the bad publicity, with a negative impact on store or unit-level sales and on future franchise sales. For example, if one franchise outlet is reported as engaging in unfair or deceptive advertising practice, or violating a usury law, or failing to comply with telemarketing and “do-not-call” rules, the press and the public may not distinguish between one franchise and the franchised system, and the one bad apple could spoil the bunch. Therefore, franchisors and their franchisees have a stake in ensuring that all operating outlets, including franchisee and company-owned outlets, comply with applicable laws.

C. Vicarious Liability

Franchisors may be vicariously liable due to the actions of their franchisees. Vicarious liability may arise due to allegations that the franchisee was the actual, apparent or ostensible agent of the franchisor, and the franchisor is therefore responsible. Other cases have focused on the question of whether the franchisor “controlled the instrumentality” that caused the harm. Vicarious liability claims often arise in the context of (a) injuries to patrons of the franchised business (e.g., “slip and fall;” violent crime; etc.), and will be discussed below in the context of dram shop or liquor liability; and (b) in employment matters, and will be discussed below in the context of wage/hour/tip rules, and drug testing of employees. Consequently, for franchisors, the franchisees' compliance with certain business laws and regulations may have a direct and possibly significant impact on the franchisor, beyond an impact to the image of the brand.

D. Training and Operational Standards

Franchisors and their franchisees need to understand not only the laws applicable to their businesses, but the manner and method by which each outlet, and each manager and employee, must comply with the law. Legal compliance information should become part of the franchisor’s operational standards, which will be communicated through the operations manual and in the training programs. In many cases, the laws and regulations governing a certain specific operational aspect will be subject to different requirements due to variations in state laws (e.g., menu labeling (until implementation of Federal law), service animals, alcohol beverage licensing, and drug testing). In these situations, it may not be practical for a franchisor

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2 Vicarious liability for franchisors is, and has been, a source of significant case law as well as professional writings in the franchise bar. Due to the subject matter and space limitations of this paper, the authors are not able to discuss in detail or summarize the jurisprudence of vicarious liability in the franchise context. However, a few of the many papers and presentations on the topic, which provide more detailed explanations and case citations, include: Klaus, Cynthia M., Murray, Jason M., and Smedstad, Heather, “Vicarious Liability,” ABA Forum on Franchising, 2008, 31st Annual Forum (W-10); Fredric Cohen, Marc Merriweather & Amy Powers, “Keeping Your Distance: How to Avoid or Survive Vicarious Liability Claims While Enforcing System Standards,” 42nd Annual IFA Legal Symposium, May 17-19, 2009; and Dean F. Fournaris, “The Inadvertent Employer: Legal and Business Risks of Employment Determinations to Franchise Systems,” 27 Franchise L.J. 224 (spring 2008).
to describe all of the variations, create a training program that addresses all of the variations, and/or establish brand or operating standards. However, the franchisor should advise franchisees of these variations, and provide the information necessary for each franchisee to comply with the laws that are applicable to its business and locale. For laws and regulations that are critical to the operations of the business, the legal requirements, or at least the parameters of the legal obligations, should be included in the franchise system operational standards, and can be referenced in outlet reviews and reports of field service managers and inspectors.

E. FDD and Franchise Agreement

While franchise agreements require that franchisees “comply with all laws,” certain laws and regulations must be disclosed in the FDD and may need to be referenced with specificity in the franchise agreement. Under the FTC’s Franchise Rule, a franchisor must disclose in Item 1 of the FDD “any laws or regulations specific to the industry in which the franchise business operates.” The FDD Guidelines adopted by NASAA, and adopted and/or utilized by the states, have the same requirement. References to laws of general applicability should not be included (e.g., tax regulations, insurance regulations, or general business licensing laws). But, a detailed description, or a state-by-state list, of these industry-specific laws is not required either. The FTC has stated in its Franchise Rule Compliance Guide: “[i]n any case where industry-specific laws are disclosed, statutory citation and identification are unnecessary. The disclosure should simply state that a specific type of regulation exists and that prospective franchisees should investigate the matter further.” In addition, with the myriad federal and state laws, the variations among state laws, and the variations in local laws within a state, such a detailed disclosure would be impractical and burdensome to prepare. Nonetheless, the authors are aware of state franchise examiners that have requested that franchisors include a detailed list of industry laws or regulations in the FDD. Item 1 may not be the only FDD Item where business laws are disclosed. For example, the costs of complying with specific laws or regulations may need to be disclosed in other items of the FDD.

In addition to FDD disclosures, if a law or regulation is significant enough that a failure to comply with the law will be grounds for termination, a franchisor may wish to specifically reference the law or the type of law in the franchise agreement and/or in the manual. The law may be significant because violation of the law could create negative systemwide publicity (e.g., menu labeling) or the failure to comply could put the franchise temporarily out of business (e.g., liquor licensing). The franchisor’s argument for termination due to a violation of a law is buttressed if the franchisee had been on notice of the significance of legal compliance in the franchise agreement and/or in the manual.

In short, these business laws create multiple cross-currents that must be navigated by both franchisors and franchisees.

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3 16 C.F.R. Part 436.
4 Id. at §436(a)(6)(v).
7 See, e.g., discussion in Part III.A.3 (below) of the disclosure of liquor licensing application costs in FDD Item 7.
III. BUSINESS LAWS AND REGULATIONS

A. Hospitality Industry Related Laws

1. Menu Labeling

Regulation of food and sanitation in the United States dates back to the time of Abraham Lincoln. Early laws were designed to regulate food and ingredient safety. More recent legislation – the Nutrition Labeling and Education Act (“NLEA”) - was designed to provide consumers with standardized information to assist in their purchase decisions. The NLEA “requires all packaged foods to bear nutrition labeling and all health claims for foods to be consistent with terms defined by the Secretary of Health and Human Services.” The NLEA standardized the food ingredient panel; serving sizes; and certain terms, such as low fat and light. The standards and rules established by the NLEA define the nutrition label as we know it today. The NLEA presently expressly exempts food “serviced in restaurants” from the mandatory labeling requirement.

The last few years have seen an increased awareness of increasing rates of obesity in Americans. In fact, First Lady Michelle Obama launched her “Let’s Move” campaign in February 2010 to solve childhood obesity within a generation. There have also been legislative responses to American obesity rates. Legislative responses have included policy changes to encourage citizens to make healthy choices. Yet, even with the additional information provided to consumers purchasing packaged foods, “[o]besity rates have increased over the past twenty-five years.”

Supporters of menu label laws often argue that consumers need more access to nutritional information and without it they are forced to guess. Indeed, when adopting the state’s menu label law, the California State Legislature found that “broader availability of nutrition information regarding foods served at restaurants and other food service establishments would allow customers to make more informed decisions about the food they purchase.” For example, relatively informed consumers will probably know that the boiled chicken and steamed broccoli has fewer calories than the double bacon cheeseburger but may not realize that a Dunkin Donuts plain bagel and plain cream cheese has more calories than two plain glazed Dunkin Donuts.

Legislators and health advocates are convinced that more conspicuously visible information is part of the solution to the U.S. obesity problem because a significant portion of the daily caloric intake of individuals comes from foods purchased and prepared outside of the

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8 N.Y. State Rest. Ass’n v. N.Y. City Bd. of Health, 556 F.3d 114, 118 (2d Cir. 2009).
9 FDA, Milestones in Food and Drug Law History, www.fda.gov/AboutFDA/WhatWeDo/History/Milestones/ucm081229.htm.
12 Ctrs. for Disease Control, New CDC Study Finds No Increase in Obesity Among Adults; But Levels Still High (Nov. 28, 2007), available at www.cdc.gov/nchs/pressroom/07newsreleases/obesity.htm.
14 M.S. Enkoji, Retail Watch: California Calorie Law Alters Chains’ Fare, SACRAMENTO BEE, July 14, 2009, at 9B; https://www.dunkindonuts.com/aboutus/nutrition/
home. For example, a New York City survey that found that only one in thirty-two customers (3.1 percent) in thirteen major chains saw and used voluntarily disclosed nutritional information, such as pamphlets and wall signs. In addition, initial indications are that the required nutritional disclosure is causing restaurants to alter menus and recipes to reduce the caloric content of some dishes. For example, one restaurant chain reduced the caloric content of a scallop and spinach salad from almost 1,300 calories to 390 calories.

A legislative solution has quickly led to a patchwork of laws requiring the disclosure of nutritional information in chain restaurants and food establishments. With the passage of the Patient Protection and Affordable Care Act on March 23, 2010, Congress amended the Federal Food, Drug and Cosmetic Act to create a national menu label disclosure requirement (the “Federal Act”). The Federal Act became effective on March 23, but mandatory requirements will not go into effect until after the federal Food and Drug Administration (“FDA”) issues regulations telling persons subject to the law how to comply. The FDA must issue the regulations by March 23, 2011 and on July 7, 2010 solicited input from the public regarding the development of the regulations. Thus, the precise date of that implementation of the Federal Act will become mandatory is unknown at this time. Further, although the Federal Act expressly preempts state and local laws, affected industries are reluctant to challenge enacted state and local laws until the implementation of the Federal Act.

The following identifies and describes several implemented and passed state and local menu label laws and the recently enacted Federal Act. The following is not an exhaustive list of state and local laws, but provides an overview of many of the notable pieces of legislation. The laws are more complex and nuanced than a brief summary, such as the following, could analyze. Because of the passage of the Federal Act, which is also described below, we do not anticipate additional menu label legislation to be passed.

a. **New York City**

The New York City Board of Health was the first governmental body to adopt menu labeling requirements. After an initial challenge, the Second Circuit found that Congress intended to exempt restaurants from the NLEA and left authority to state and local governments to require calorie counts and other information. In doing so, the court rejected the restaurant association’s claim that the regulations violated the First Amendment, finding that “[t]he First Amendment is not violated, where as here, the law in question mandates a simple factual disclosure of caloric information and is reasonably related to New York City’s goals of combating obesity.”

The New York regulations require food service establishments, which are defined as part of a group of fifteen or more food service establishments nationally, to list calories for standard menu items on menu boards, menus, or food item display tags, including drive-through

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16 Id.
17 Enkoji, supra note 14.
18 Id.
19 21 U.S.C. § 343(h)
21 N.Y. CITY BD. OF HEALTH, supra note 15.
22 Id. at 120.
23 Id. at 118.
But unlike California’s law, discussed below, there are no exclusions for grocery stores and similar venues. To qualify as a group of fifteen or more food service establishments, the establishments do not need to operate under the same name. A group of fifteen commonly owned, controlled, or franchised restaurants that “[o]ffer substantially the same menu items in servings that are standardized for portion size and content” are covered, regardless of the names under which they operate.25

The regulations require all menu boards and menus to bear the total number of calories for each menu item.26 The disclosure must be clear and conspicuous and either adjacent to or in close proximity and clearly associated with the menu item.27 The “[f]ont and format used for calorie information must be at least as prominent in size as is used for the name or price of the menu item.”28 The regulations do not preclude any establishment from providing a disclaimer stating that there may be variations in calorie content based on serving variations, quantity of ingredients, or special ordering.29

Calorie information does not need to be disclosed for items that are on the menu for less than thirty days in a calendar year or those that are not served in standardized portions.

b. California

California’s Senate Bill 1420 was enacted in 2008 and the initial phases of the law went into effect on July 1, 2009. The law’s full implementation is required by January 1, 2011.30 The law requires food facilities that are part of a chain of twenty or more locations in California to disclose certain nutritional information for all standard menu items.31

The term food facility in California is any food facility that “operates under common ownership or control with at least 19 other food facilities with the same name in the state that offer for sale substantially the same menu items, or operates as a franchised outlet of a parent company with at least 19 other franchised outlets with the same name in the state that offer for sale substantially the same menu items.”32

A food facility does not include certified farmers’ markets; commissaries; health care facilities; mobile support units; public and private school cafeterias; restricted food services facilities; retail stores where the majority of the sales are from a pharmacy; vending machines; or grocery stores, except for “separately owned food facilities to which this section otherwise applies that are located in the grocery store.”33 Convenience stores are considered grocery stores. Other than grocery stores, the California law does not further define these terms.

The law requires disclosures regarding each standard menu item, which includes any “food or beverage item offered for sale . . . through a menu, menu board, or display tag at least

24 N.Y. CITY BD. OF HEALTH, supra note 15.
25 N.Y. CITY HEALTH CODE § 81.50(a)(1).
26 Id. § 81.50(c).
27 Id.
29 N.Y. CITY HEALTH CODE § 81.50(c).
30 CAL. HEALTH & SAFETY CODE § 114094(a), (b) (West 2009).
31 Id.
32 Id. § 114094(a).
33 Id.
180 days per calendar year. It is also important to note that the measure is any 180 days, not 180 consecutive days. A standard menu item is not (a) “[a] food item that is customized on a case-by-case basis in response to an unsolicited customer request”; (b) certain alcoholic beverages; (c) packaged food that is subject to NLEA; (d) food items “served at a consumer self-service bar”; and/or (e) food or beverage items “served at a consumer self-service buffet.”

From July 1, 2009, to December 31, 2010, food service facilities are required to “provide a brochure placed at the point of sale that includes[,]” at a minimum, information about calories, sodium, saturated fat, and carbohydrates for each standard menu item. “For sit-down restaurants, the information must be provided at the table,” on the menu next to each standard menu item, in an index to the menu, in a menu insert, or on a table tent. “Drive-thrus are required to have brochures available upon request and have a notice of the availability at the point of sale.”

Alternatively, compliance can be achieved by providing the calorie content information that is required during the law’s second and final implementation stage, which begins on January 1, 2011. This stage requires calories to be listed on menus, menu boards, and food display tags next to the standard menu item. “Drive-thrus [must] continue to [provide] a brochure . . . upon request and must have a notice that the information is available.” Thus, prior to January 1, 2011, calorie count plus additional information must be available on or about the menu, and after that date the calorie count must be on the menu next to the item.

The nutritional/calorie information must be determined on a reasonable basis, i.e., “any reasonable means recognized by the federal Food and Drug Administration [(FDA)] of determining nutritional [and calorie] information, . . . including . . . nutrient databases and laboratory analyses.” The statute provides that a “reasonable basis” is “required only once per standard menu item” if the portion size is consistent, the food service facility follows a standardized recipe, and its staff is trained to follow a “consistent method of preparation.” Unlike the NLEA, the California law does not provide a 20 percent margin of error for the nutritional information. Therefore, it will be left to argument as to whether there was reasonable basis for the data disclosed.

The California law contains several provisions that appear to protect food service facilities. First, it preempts all local law on this subject. Second, it expressly states that it does not “create or enhance any claim, right of action, or civil liability that did not previously exist under state law.” Thus, although general principles of unfair competition, fraud, advertising claims, and other consumer remedies will continue to apply, the law provides for no new private cause of action. Third, the law provides that the “only enforcement mechanism of the section is

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34 Id. § 114094(a)(7).
35 Id.
37 Id.
38 Id.
39 CAL. HEALTH & SAFETY CODE § 114094(c).
41 CAL. HEALTH & SAFETY CODE § 114094(a)(8).
42 Id. § 114094(f).
43 Id. § 114094(j).
44 Id. § 114094(h). The statute also provides that it does not limit any claim, right of action, or civil liability that otherwise exists under state law.
the local enforcement agency\textsuperscript{45} and that violations are punishable by fines of $50 to $500, but only once per inspection visit (not per menu item). Finally, “[m]enus and menu boards may include a disclaimer . . . that there may be variations . . . across services . . . and based upon special ordering.”\textsuperscript{46}

c. **King County (Seattle), Washington**

The King County Board of Health adopted regulations requiring chain restaurants with fifteen or more national locations [offering substantially the same menu items] and $1 million in annual sales (collectively for the chain) to display calorie, saturated fat, sodium, and carbohydrate information for foods and beverages on menus.\textsuperscript{47} Nutritional information may also be disclosed at the point of ordering, as long as the menu prominently states on each page where and how the nutrition information is provided.\textsuperscript{48}

d. **Maine**

In June 2009, the Maine legislature passed and the governor signed Maine’s version of a menu label law.\textsuperscript{49} The law will go into effect February 1, 2011, and requires chain restaurants to clearly and conspicuously state on a food display tag, menu, or menu board the total number of calories per serving of each food and beverage item listed for sale. The law defines *chain restaurant* as a restaurant “that does business under the same trade name in 20 or more locations” (only one of which must be in Maine), regardless of ownership, “that offer[s] predominantly the same type of meals, food, beverages or menus.”\textsuperscript{50} Chain restaurants do not include movie theaters, grocery stores, hotels, or motels “that provides a separately owned eating establishment but do include the separately owned eating establishment if the establishment meets the [foregoing] criteria.”\textsuperscript{51} Chain restaurants are not required to provide applicable information for (1) “[f]ood items served at a self-service salad bar or buffet”; (2) items that are on menus for less than sixty days per year; (3) “[a] condiment or other item offered to a customer for general use without charge”; (4) “[a]n item sold to a customer in a manufacturer’s original sealed package that contains nutrition information as required by federal law”; or (5) “[a] custom order for a food or beverage item that does not appear on a menu, menu board or food display tag.”\textsuperscript{52}

Unlike other jurisdictions, the Maine law requires the following statement: “To maintain a healthy weight, a typical adult should consume approximately 2,000 calories per day; however, individual calorie needs may vary.”\textsuperscript{53} The law also permits a disclaimer to be included as long as it is the same or substantially similar to the following: “Nutrition information is based upon standard recipes and product formulations; however, modest variations may occur due to differences in preparation, serving sizes, ingredients or special orders.”\textsuperscript{54}

\textsuperscript{45} Id.
\textsuperscript{46} Id. § 114094(g)(2).
\textsuperscript{48} Id.
\textsuperscript{50} Id. (amending § 2491(2)(B)).
\textsuperscript{51} Id. (amending § 2491(2)(B)).
\textsuperscript{52} Id. (amending § 2500(A)(5)).
\textsuperscript{53} Id. (amending § 2500(A)(3)).
\textsuperscript{54} Id. (amending § 2500(A)(3)).
e. **Oregon**

In June 2009, the Oregon legislature passed and the governor signed a menu label law that requires chain restaurants of fifteen or more restaurants in the United States that serve standard menu items and that operate under the same name to disclose caloric content on menus and menu boards and have other nutritional information available on request for standard menu items.\(^{55}\) Like other states, Oregon does not include movie theaters, certain health care facilities, and cafeterias of educational institutions in its definition of *chain restaurant*.\(^{56}\)

f. **The Federal Act**

The Federal Act requires nutritional disclosures on menus and menu boards of restaurants or similar retail food establishment. The Federal Act applies to establishments that are part of a chain with 20 or more locations doing business under the same name (regardless of the type of ownership of the locations) and offering substantially the same menu items.\(^{57}\) The law also applies to vending machine operators.

The law requires disclosure of various nutritional information regarding standard menu items. First, disclosure is required on the menu or menu-board\(^{58}\) of (i) the number of calories in each standard menu item, as usually prepared and offered for sale; and (ii) a statement concerning suggested daily caloric intake (as will be specified by the Secretary of Health and Human Services). The calorie disclosure must be adjacent to the menu item so as to be clearly associated with the menu item and the daily caloric intake disclosure must be prominently displayed on the menu or menu-board.\(^{59}\) Second, disclosures of other nutritional information regarding each standard menu item is required to be available on request and notice of such availability must be displayed on the menu.\(^{60}\) Required information includes data on: calories; calories from fat; total fat; saturated fat; cholesterol; sodium; carbohydrates; sugars; dietary fiber protein; and other nutrients required by the FDA (such as trans-fats). It is anticipated that the FDA will provided additional guidance as to how to comply.

Calorie count disclosures (only) must be posted for self-service items and food or beverage items on display. Restaurateurs must post signs adjacent to each standard menu item offered on a buffet, salad bar or similar self-service line where the foods or beverages are on display and visible to consumers. The sign must disclose calories per item or per serving or displayed food item.\(^{61}\)

For items that come in different flavors or varieties, such as soft drinks, ice cream, pizza, doughnuts and children’s combination meals, the Federal Act gives the FDA flexibility to define how restaurants can determine and disclose nutrition data for those menu items. The FDA could

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\(^{55}\) H.B. 2726, ch. 314 (Or. 2009).

\(^{56}\) Id. § 2(b).


\(^{58}\) 21 U.S.C. § 343(q)(5)(H)(xi).  A “menu” or “menu board” is the “primary writing of the restaurant or other similar retail food establishment from which a consumer makes an order selection.”

\(^{59}\) 21 U.S.C. § 343(q)(5)(H)(ii)

\(^{60}\) 21 U.S.C. § 343(q)(5)(H)(iii), (iv)

\(^{61}\) 21 U.S.C. § 343(q)(5)(H)(iii)
decide, for example, to require restaurants to provide nutrition data in ranges or averages for such items.\footnote{21 U.S.C. § 343(q)(5)(H)(v)}

The Federal Act requires the restaurant or establishment to have a reasonable basis for its nutritional disclosures. The Federal Act states that these may include nutrient databases, cookbooks, laboratory analysis, and other means as described in the Federal Code of Regulations or guidance provided by FDA.\footnote{21 U.S.C. § 343(q)(5)(H)(iv)} The reasonable basis standard is the current standard developed by the FDA for current voluntary disclosures.

All “standard” menu items will require mandatory nutrition labeling. The Federal Act defines standard menu items as items offered for sale for at least 60 days per calendar year. The law exempts some menu items, including: temporary items appearing on the menu for fewer than 60 days per calendar year; items not listed on menus or menu boards (for example, condiments and items placed on the table or counter for general use); daily specials; custom orders; and customary test market items appearing on a menu for fewer than 90 days.

Restaurant operators that are part of a chain with fewer than 20 locations can voluntarily participate in the Federal Act by registering with the FDA.

Questions and issues that will need to be resolved in the FDA regulations:

- What is the scope of a “similar retail food establishment?” Are grocery stores; school cafeterias; hotel room-service kitchens; farmers’ markets; commissaries; health care facilities; mobile support units; restricted food services facilities; or retail stores where the majority of the sales are from a pharmacy “similar retail food establishments?”
- Are “express” units that offer a more limited selection of the same menu items that are typically served at the “full-service” unit offering substantially menu items counted as part of the 20? What is the scope of the menu or name variation that can make the restaurants different?
- Will the “primary writing” upon which the customer makes an order selection vary among restaurant types (e.g., those that offer primarily take-out must have the required information on the take-out menu rather than an in-store menu board as opposed to a full service restaurant which must have the required information on its primary menu rather than its take-out menu)?
- What are the required font sizes? What does it mean to be associated with a menu item or prominently on the menu? May a restaurant located in a jurisdiction that restricts the size of drive-through menus include the required information by other means?
- Will the regulations regarding a “reasonable basis” for nutritional disclosures address ingredient, cooking and human variation? Will a statement regarding variation in ingredients, preparation and cooking techniques and human variation be permitted?
- What are custom orders and what are test market items?

g. Effects on Franchising

Most franchise systems that are in the food service industry will have to adapt to the requirement of the Federal Act. Franchisees that are part of a covered system will have the legal obligation to comply and disclose the appropriate nutritional information. The requirement to comply with the Federal Act may need to be included in Item 1, though it may be considered to be a law of general applicability. But will the franchisor want each individual franchisee to determine the nutritional information on their own? Answer is probably no. The franchisor is in the best position to determine the nutritional information and accept the associated liability if the information is wrong.

2. Wage / Hour And Tip Laws

In the traditional franchise agreement, the franchisor explicitly shifts the responsibility for all employment decisions to the franchisee. As a result, the question of whether a franchisor could be held liable for the employment practices of its franchisees depended upon whether the franchisee is the agent of the franchisor and/or whether there is a joint employment relationship between the franchisor and the franchisee. The employees of franchisees often attempt to draw a franchisor into wage and hour litigation under these principles. Attempts to impose liability on franchisors through agency principles have not been particularly successful. However, as discussed in more detail below, in recent years, franchisees have successfully argued that they are the employees of their franchisors and entitled to all applicable protections of their states’ employment laws.

In Chen v. Domino’s Pizza, Inc. et al., the plaintiffs filed a purported class action alleging that they were not paid for all hours worked, not paid overtime and were required to purchase their own uniforms and maintain their own automobiles for business purposes. The plaintiffs asserted claims under the Fair Labor Standards Act (“FLSA”) and the New Jersey Wage and Hour Law (“NJWHL”) against several defendants, including Domino’s Pizza, Inc. and Domino’s Pizza, LLC (“Domino’s”). Domino’s moved to dismiss the complaint on the grounds that it was not an employer for purposes of the FLSA or the NJWHL. The court noted that under the FLSA and the NJWHL, liability is only imposed on an “employer.” Further “courts have consistently held that the franchisor/franchisee relationship does not create an employment relationship between a franchisor and a franchisee’s employees.” In dismissing the plaintiffs’ complaint, the court concluded that “Plaintiffs have not pled facts sufficient to show that an employment relationship exists between them and Domino’s,” particularly since the complaint specifically alleged that one of the other named defendants was the plaintiffs’ employer. Although the plaintiffs in Chen were not successful in advancing their employment claims, as discussed below, other courts have been willing to allow claims against the franchisor to proceed.

64 2009 WL 3379946 (D.N.J. 2009)
65 Id. at 3.
66 Id.
67 Id. at 4.
One recent trend that has emerged is that franchisees will claim that, contrary to their franchise agreements, they are not independent contractors, but rather they are the employees of their franchisors. Although these claims typically involve franchises with very little start-up costs and franchisees that are relatively unsophisticated, the law that has emerged as a result of these claims presents novel and difficult challenges for all franchisors. Recent decisions indicate that merely labeling a franchisee an “independent contractor” will not necessarily withstand scrutiny if the franchisee falls under the state’s common law or statutory definition of an “employee.” Because some states go so far as to create a presumption of employment, franchisors must be particularly diligent about ensuring that their franchisees do not fall under the statutory definition of an employee. This will be a factual determination that will depend in large part on the particular jurisdiction in question.

In Coverall North America, Inc. v. Commissioner of the Division of Unemployment Assistance, the Massachusetts Supreme Court affirmed a decision from the division of unemployment assistance (the “Division”) finding that a Coverall franchisee was an employee under Massachusetts law.69 The court in Coverall noted that under Massachusetts law, “the employer bears the burden of proving ‘that the services at issue are performed (a) free from control or direction of the employing enterprise; (b) outside of the usual course of business, or outside of all the places of business, of the enterprise; and (c) as part of an independently established trade, occupation, profession, or business of the worker.’”70 “[I]f an employer fails to establish any one of the three prongs, the services in question will constitute ‘employment’ . . . .”71

The court in Coverall did not address the first two prongs of the employment test, noting that “the weight of the evidence establishes that Coverall failed to satisfy the third prong . . . .”72 “Under the third prong, the court ‘is to consider whether the service in question could be viewed as an independent trade or business because the worker is capable of performing the service to anyone wishing to avail themselves of the services or, conversely, whether the nature of the business compels the worker to depend on a single employer for the continuation of the services.’”73

On appeal, Coverall claimed that “the division erred by classifying the claimant as a Coverall employee and incorrectly focused on what the claimant actually did with her franchise instead of what she was capable of.”74 Coverall argued that “the franchise agreement that the claimant signed allowed her to be an entrepreneur and to expand her business by hiring employees and directly soliciting new customers,” and “although the claimant did not take advantage of these opportunities, she is still an independent contractor because she was capable of expanding her business.”75 The court rejected this argument, noting that “[a]lthough the court can consider whether a worker is ‘capable of performing the service to anyone wishing to avail themselves of the services,’ the court may also consider whether ‘the nature of the

70 Id. at 1087.
71 Id.
72 Id.
73 Id.
74 Id. at 1088.
75 Id.
business compels the worker to depend on a single employer for the continuation of the services.\textsuperscript{76} "In this regard, we determine 'whether the worker is wearing the hat of an employee of the employing company, or is wearing the hat of his own independent enterprise.'\textsuperscript{77}

In this case, the claimant was “required to allow Coverall to negotiate contracts and pricing directly with clients, bill clients, and provide a daily cleaning plan to which the claimant was required to adhere.”\textsuperscript{78} Further, “[e]ven if the claimant was capable of being an ‘entrepreneur’ and expanding her own business as Coverall suggests, it is undisputed that the growth of her own business inevitably expanded Coverall’s clientele base, as each new ‘client’ became a Coverall client.”\textsuperscript{79} The court concluded that there was substantial evidence supporting the Division’s conclusion that “Coverall failed to satisfy its burden of establishing that the claimant’s business was independent of Coverall under the third prong of the ABC test.”\textsuperscript{80}

Four years later, in \textit{Awuah v. Coverall North America, Inc.}, the plaintiffs, workers who performed cleaning services as franchisees for Coverall, brought an action alleging that Coverall misclassified its franchisees as independent contractors.\textsuperscript{81} The plaintiffs moved for partial summary judgment with regard to their claim that they had been misclassified as independent contractors. The court noted that under Massachusetts law, “an individual performing a service is considered an employee unless: (1) the individual is free from control and direction in connection with the performance of the service, both under his contract for the performance of service and in fact; and (2) the service is performed outside the usual course of the business of the employer; and, (3) the individual is customarily engaged in an independently established trade, occupation, profession or business of the same nature as that involved in the service performed.”\textsuperscript{82}

The court in \textit{Awuah} focused on the second prong which it found to be “dispositive.” “To satisfy the second prong, Coverall must establish that the worker is performing services that are part of an independent, separate, and distinct business from that of the employer.”\textsuperscript{83} The court rejected Coverall’s argument that “it is not in the commercial cleaning business, but rather it is in the franchising business.” The court found that “[d]escribing franchising as a business in itself, as Coverall seeks to do, sounds vaguely like a description for a modified Ponzi scheme-a company that does not earn money from the sale of goods and services, but from taking in more money from unwitting franchisees to make payments to previous franchisees.”\textsuperscript{84} The court held that the “undisputed facts establish that Coverall sells cleaning services, the same services provided by these plaintiffs. Because the franchisees did not perform services outside the usual course of Coverall’s business, Coverall fails to establish that the franchisees are independent contractors.”\textsuperscript{85} Accordingly, the court granted the plaintiffs’ motion for partial summary

\textsuperscript{76} \textit{Id.}
\textsuperscript{77} \textit{Id.}
\textsuperscript{78} \textit{Id.}
\textsuperscript{79} \textit{Id.}
\textsuperscript{80} \textit{Id.}
\textsuperscript{82} \textit{Id.} at *2.
\textsuperscript{83} \textit{Id.} at *3.
\textsuperscript{84} \textit{Id.}
\textsuperscript{85} \textit{Id.} at *4.
judgment, holding that “the Massachusetts franchisees were misclassified as independent contractors.”86

More recently, in *De Giovanni v. Jani-King International, Inc.*, the plaintiffs claimed that the franchisor, Jani-King, “improperly classifies its franchisees as independent contractors when they are in fact employees,” thereby violating “a variety of Massachusetts laws that afford protections to employees, including minimum wage, overtime pay, and timely payments of all wages owed without improper deductions from pay.”87 The plaintiffs sought certification of a proposed class “consisting of all individuals who have performed cleaning work for Jani-King in Massachusetts any time since January 12, 2004.”88

The court noted that “[p]ursuant to Massachusetts General Laws ch. 151A, § 2, an individual is an employee unless the services ‘at issue are performed (a) free from control or direction of the employing enterprise; (b) outside of the usual course of business, or outside of all the places of business, of the enterprise; and (c) as part of an independently established trade, occupation, profession, or business of the worker.’”89 “[I]f an employer fails to establish any one of the three prongs, the services in question will constitute ‘employment,’ as opposed to an independent contractor relationship.”90

The court certified a class on the employment question, finding that “[c]ommon questions will predominate for the plaintiffs’ employment classification class under all three prongs of the Massachusetts test.”91 With regard to the second prong of the test, the court found that “common issues will predominate as to whether the services performed by the class fall outside of Jani-King’s usual course of business.”92 Similarly, for the third prong “common issues will predominate in determining whether the plaintiffs are capable of performing the service to anyone wishing to avail themselves of the services or, conversely whether the nature of the business compels the[m] to depend on a single employer for continuation of the services.”93 The court found that prong one presented a “closer issue” but “[w]hat is critical to the prong one analysis is the balance between the areas in which franchisees have total, uninhibited control over their franchises, and the areas where Jani-King pervasively controls the franchisees’ conduct.”94 “Although the balance may ultimately favor Jani-King . . . the Court is convinced that the question can be answered with reference to common facts.”95

b. **States Seeking to Impose Employment Related Obligations on Franchisors**

Other recent decisions and administrative actions have called into question the long-standing notion that franchisors may insulate themselves from employment issues by entering into franchise agreements which designate their franchisees as independent contractors. In recent years, federal and state agencies have been aggressively targeting businesses, including franchisors, for perceived violations of various employment laws. In particular, state and federal

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86 *Id.* at *5.
88 *Id.*
89 *Id.*
90 *Id.*
91 *Id.* at 84.
92 *Id.* at 85.
93 *Id.*
94 *Id.*
95 *Id.*
agencies have aggressively targeted the perceived misclassification of employees as independent contractors leading to the imposition of employment-related liabilities, including taxes and statutory penalties.

In Employment Dept. v. National Maintenance Contractors of Oregon, Inc., on appeal from a decision by Oregon’s Employment Department, the Oregon Court of Appeal held that the franchisees of National Maintenance Contractors of Oregon, Inc. (“NMC”) were employees within the meaning of Oregon’s unemployment insurance statutes.⁹⁶

In 2005, Oregon’s Employment Department conducted an audit of NMC for the years 2002 through 2004. Following the audit, the department issued a notice of tax assessment to NMC for unemployment insurance taxes that NMC owed for its franchisees during that period. NMC disputed the assessment and requested a hearing before an administrative law judge (“ALJ”).⁹⁷ NMC argued, inter alia, that “its franchisees were not ‘employees’ within the meaning of the unemployment insurance statutes . . . .”⁹⁸ The ALJ agreed with NMC that its franchisees were not employees, finding that “NMC did not pay remuneration to the franchisees.”⁹⁹

On appeal, the court found that the ALJ properly concluded that the franchisees provided a service to NMC, because “NMC essentially subcontracted with its franchisees to provide janitorial services . . . .”¹⁰⁰ However, the court disagreed with the ALJ’s finding that NMC did not pay remuneration to its franchisees. The court noted that “[u]nder the terms of the franchise agreement, NMC collects payment from building owners for janitorial services pursuant to a contractual relationship between NMC and the building owners. Then, pursuant to the terms of a separate contract-the franchise agreement-NMC ‘will pay [its franchisee] the amount [NMC] collects . . . after deducting the fees described below [for royalties, ‘office management,’ and liability insurance].’”¹⁰¹ The court noted that “[t]he payment from NMC to its franchisees, though calculated based on the services provided by franchisees to building owners, is paid, as a matter of contract, by NMC to its franchisees.”¹⁰²

Despite its finding that NMC’s franchisees provided a service to NMC and NMC paid remuneration to its franchisees, the court noted that its analysis was not complete, because Oregon’s employment statute provided for an exception for finding an employment relationship by including the phrase “unless the context requires otherwise.”¹⁰³ “[T]he phrase ‘unless the context requires otherwise’ means that, ‘in some cases, the circumstances of a case may require the application of a modified definition of the pertinent statutory terms to carry out the legislature’s intent regarding the statutory scheme.’”¹⁰⁴

With regard to applying the exception to the statute in the context of a franchise relationship, the court stated “[w]e appreciate that franchises are unique business arrangements that can differ in many important ways from a traditional employment relationship,” however, “we are not persuaded that franchise relationships demand a modified definition of service or

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⁹⁷ Id. at 154.
⁹⁸ Id.
⁹⁹ Id. at 155-156.
¹⁰⁰ Id. at 156.
¹⁰¹ Id. at 157.
¹⁰² Id.
¹⁰³ Id. at 158.
¹⁰⁴ Id.
remuneration for purposes of ORS 657.030.” 105 “Rather, the question whether a particular franchise relationship satisfies that statute must be answered on a case-by-case basis, by determining whether services for remuneration have been provided and, if so, whether some exclusion to the definition of employment nevertheless applies. See, e.g., ORS 657.040(1) (excluding from the definition of ‘employment’ any services performed for remuneration by ‘independent contractors’ within the meaning of ORS 670.600).” 106

The court remanded the matter to the ALJ to address NMC’s argument that its franchisees are independent contractors under Oregon law. 107

Although many people view the Massachusetts decision as an anomaly, several states utilize a similar definition in determining whether someone is an employee or an independent contractor; thus, the Massachusetts decision may have much greater ramifications in the near future.

c.  Tipping

One recent area that has been the subject of litigation in several states involves the issue of employee tipping. Although there have not been very many cases involving tipping within the franchise context, the development of law in this area could have serious ramifications for franchise systems, particularly those with a large proportion of company owned units. Further, although no reported cases have yet addressed a franchisor’s potential liability for violations committed by a franchisee, it is worth noting that franchisors have in fact been sued for purported violations committed by their franchisees. Thus, of particular import of this area is with respect to how franchisors address the issue of tips and tip collection in their manuals, if at all.

In Chau v. Starbucks Corporation, a former Starbucks barista filed a class action against Starbucks, alleging that its policy of allowing shift supervisors to share in tips placed in a collective tip box violated California law. 108 The plaintiff in Chau alleged that Starbucks’ policy violated California’s Unfair Competition Law (“UCL”), because the policy violated California Labor Code section 351. Section 351 provides in relevant part that “[n]o employer or agent shall collect, take, or receive any gratuity or a part thereof that is paid, given to, or left for an employee by a patron . . . .” After certifying a class of current and former baristas and conducting a bench trial, the trial court found that the shift supervisors were “agents” because they had “the authority to ‘supervise’ and ‘direct’ the acts of employees.” 109 Based on this conclusion, the trial court ruled that as a matter of law Starbucks violated section 351 because the statute prohibits ‘agents’ from sharing tips left in communal tip containers if nonagents also receive tips from the tip containers. 110 The court found that plaintiff had proved the UCL claim and awarded the class $86 million in restitution. 111

On appeal, the court reversed the judgment of the trial court, finding that regardless of whether the shift supervisors were “agents,” “section 351 does not say that an employee (who is

105 Id. at 160.
106 Id.
107 Id.
109 Id. at 696.
110 Id.
111 Id. at 691.
also an agent) cannot keep his or her own tip. The code section does not provide that merely because an employee falls within the definition of an ‘agent,’ (e.g., someone who has the authority to ‘supervise, direct or control’ another employee), an employer must bar that employee from retaining a tip that was given to him by a customer for services provided to the customer. Because “section 351 does not prohibit a shift supervisor from keeping gratuities given to him or her for his or her customer services, there is no logical basis for concluding that section 351 prohibits an employer from allowing the shift supervisor to retain his or her portion of a collective tip that was intended for the entire team of service employees, including the shift supervisor.” The Court went on to note that “[because a shift supervisor performs virtually the same service work as a barista and the employees work as a ‘team,’ Starbucks did not violate section 351 by requiring an equitable distribution of tips specifically left in a collective tip box for all of these employees.”

The court in Chau appeared to place special emphasis on the fact that 90% of the work being done by the shift supervisors was also being done by the baristas; thus, as a practical matter there was no real difference between the baristas and the shift supervisors and the shift supervisors only had “limited supervisory duties.” The court also took note of the fact that Starbucks absolutely prohibited store managers and assistant managers from partaking of the tips. The result would likely have been different had the shift supervisors not performed the same basic tasks as the baristas or had Starbucks permitted employees with substantial supervisory powers to partake of the tips left by customers.


The complaint alleged, inter alia, that all of the defendants, including the franchisor, Ruth’s Hospitality Group, had violated the Fair Labor Standards Act (“FLSA”) “primarily by unlawfully taking and keeping plaintiffs’ tips for their own profit. Because Prime paid the plaintiffs as ‘tipped employees,’ it claimed a ‘tip credit’ and paid them an hourly wage below the minimum wage that otherwise would have applied. As a standard practice Prime withheld a percentage of servers’ tips, and a portion of that money was paid to ‘the house.’ The rest was placed into a ‘tip pool,’ which Prime used to pay other employees, including some who were not eligible to participate in the tip pool. When a manager or supervisor believed that a customer had tipped an employee too much, the manager or supervisor persuaded the customer to reduce the amount of the tip to the employee or not to tip at all. Those practices, it is claimed, rendered defendants’ use of the tip credit unlawful under the FLSA, requiring them to pay direct wages for the full minimum wage and to return the tips.”

As a result of these alleged violations, the plaintiffs requested “injunctive and declaratory relief, all unlawfully taken tips, lost minimum and overtime wages, liquidated damages matching the amount of lost tips and wages, and reasonable attorney’s fees.” The district court dismissed these counts with prejudice, “but only to the extent that they request declaratory and injunctive relief. The court concluded that the remedial provisions of the FLSA do not provide for

\[112\] \textit{id.} at 698.  
\[113\] \textit{id.}  
\[114\] \textit{id.} at 698-699.  
\[116\] \textit{id.} at 1285.  
\[117\] \textit{id.}
equitable relief.” The Eleventh Circuit refused to address the plaintiffs’ argument that the
district court had wrongfully dismissed their request for injunctive relief with prejudice, noting
that it was not “a final judgment disposing of an entire claim.” The court noted that “[t]he
district court’s partial dismissal of Counts 2-6 foreclosed injunctive and declaratory relief, but it
left intact the rest of the claim, including the plaintiffs’ request for all unlawfully taken tips, lost
minimum and overtime wages, liquidated damages matching the amount of lost tips and wages,
and reasonable attorney’s fees.”

*Edwards* is notable because the franchisor, Ruth’s Hospitality Group (“Ruth’s”),
remained as a defendant in the action with regard to the majority of the plaintiffs’ claims,
including the claims under the FLSA. A review of the court’s docket and previous rulings reveal
that Ruth’s filed a motion for partial summary judgment asserting that it was not the plaintiffs’
employer as a matter of law, however, the district court reserved any ruling on the summary
judgment motion until discovery was completed. In addition, the district court appears to have
let the FLSA claims proceed against Ruth’s because it accepted “the assertion that Ruth’s is an
employer of the FLSA plaintiffs and similarly situated employees.”

d. **Tipping and the Minimum Wage**

In *Fast v. Applebee’s International, Inc.*, the plaintiffs filed a complaint against
Applebee’s International, Inc. (“Applebee’s”) alleging that Applebee’s violated the FLSA by not
paying at least the hourly minimum wage for non-tipped work or for work the employee
performed that was not incidental to his work as a tipped employee. The class was
conditionally certified as an FLSA collective action.

Applebee’s moved for summary judgment with regard to plaintiff’s claim for time worked
before his shift before he had clocked in, also known as “Appletime.” Applebee’s argued that “it
should not be held liable for any violations that occurred prior to May 23, 2005 - the date when
Applebee’s International, Inc.’s subsidiary, GSI, assumed control of the restaurant. According to
Applebee’s, prior to May 23, 2005, the restaurant was owned and controlled by Ozark, its
franchisee. A franchisor is not ordinarily liable for the actions of its franchisee. *Howell v. Chick-
Fil-A, Inc.*, 1993 WL 603296, *2* (N.D. Fla.1993). But, a franchisor may be held liable for the
actions of its franchisee if the actual relationship between them is that of principal and agent.
Applebee’s motion for summary judgment, finding that “Applebee’s has submitted no evidence
detailing its relationship to Ozark. On the other hand, Fast has submitted an affidavit from Mike
Donnelly, a former Applebee’s Area Director, in which Donnelly swears that Applebee’s
approved the printing of the Ozark employee handbook before Ozark was allowed to have the
manual printed. At this early stage of discovery, Applebee’s relationship with Ozark remains a
disputed issue of fact.”

The court also denied Applebee’s motion for summary judgment with regard to the
plaintiff’s tipping claim under the FLSA. The court’s order was later supplemented by its order in
*Fast v. Applebee’s International, Inc.* wherein it affirmed its decision denying Applebee’s motion

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118 *Id.* at 1287.
119 *Id.* at 1289.
120 *Id.* n. 11.
122 *Id.* at 1004.
123 *Id.*
for summary judgment.\textsuperscript{124} In its subsequent decision, the court found that Applebee’s was not entitled to summary judgment with regard to the plaintiff’s tipping claim.\textsuperscript{125} The court noted that “[t]he FLSA generally requires employers to pay a minimum wage of $7.25,” although employees working in a “tipped occupation” may be paid a direct wage of $2.13 per hour and then take a “tip credit” to meet the $7.25 minimum wage.\textsuperscript{126} With regard to employees who work in dual occupations, the Department of Labor has adopted regulations which mean that “[s]o long as a tipped employee is doing related work in his or her tipped occupation, a tip credit is permitted.”\textsuperscript{127} The Department of Labor’s Handbook indicates that “employees who spend more than twenty percent of their time on general preparation and maintenance work cannot be considered tipped employees at least for the amount of time doing preparation and maintenance.”\textsuperscript{128}

The plaintiffs in \textit{Fast} argued that “they regularly spend more than twenty percent of their time on general preparation and maintenance,” and there was “evidence that Applebee’s required its servers and bartenders to clean and set up the restaurant before it was opened and after it was closed.”\textsuperscript{129} Applebee’s argued that it was entitled to summary judgment on the plaintiffs’ claims, arguing inter alia, that the twenty percent rule in the Department of Labor’s Handbook125 was contrary to the FLSA, which focused not on the duties performed by the employee, but rather on the occupation of the employee.

The court disagreed with Applebee’s, finding that “Congress intended for the tip credit to be taken when employees are primarily engaged in tip producing duties.”\textsuperscript{130} The court found the Department of Labor’s twenty percent cushion to be reasonable, because “[o]therwise, an employer could effectively use servers and bartenders as janitors and cooks both during and outside business hours when no customers were present.”\textsuperscript{131} The court noted that Applebee’s, for example, “has consistently claimed that cleaning bathrooms is related to the occupation of servers and bartenders.”\textsuperscript{132} According to the court, “[t]here is no reasonable argument that cleaning bathrooms is related to occupations where food and beverages are handled even if both the bathroom and the food promote a customer’s enjoyment of the restaurant.”\textsuperscript{133} In addition, “Applebee’s own history with FLSA enforcement . . . indicates that it is capable of enforcing the twenty percent limitation,” because “in 2005, the Department of Labor charged several Applebee’s restaurants with failing to comply with the Handbook’s twenty percent limitation. Applebee’s agreed to audit other locations to assure that this noncompliance was not systemic.”\textsuperscript{134} Although the court denied Applebee’s motion for summary judgment, it concluded that “Plaintiffs must make a prima facie showing which hours were not properly paid ‘as a matter of just a reasonable inference’” before the burden would shift to Applebee’s to demonstrate that it properly paid plaintiffs the tipped wage.\textsuperscript{135}

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\textsuperscript{125} \textit{id.} at *3.
\textsuperscript{126} \textit{id.} at *1.
\textsuperscript{127} \textit{id.} at *2.
\textsuperscript{128} \textit{id.}
\textsuperscript{129} \textit{id.}
\textsuperscript{130} \textit{id.} at *4.
\textsuperscript{131} \textit{id.} at *5.
\textsuperscript{132} \textit{id.} at *6.
\textsuperscript{133} \textit{id.} at n.7.
\textsuperscript{134} \textit{id.}
\textsuperscript{135} \textit{id.} at *9.
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The Applebee’s decision is notable for several reasons. First, with regard to the plaintiffs’ claim for “Appletime,” although it appears that the plaintiffs later abandoned that claim, the Court was initially unwilling to entertain Applebee’s argument that it could not be liable for the purported acts of its franchisee, indicating that because Applebee’s had approved the printing of the franchisee’s employee handbook it could potentially be liable for the franchisee’s alleged acts. In addition, the Court’s decision means that employers dealing with tipped employees need to ensure that they are keeping track of the time these employees spend on non tip producing duties, as any potential violation may lead to litigation. The court in Fast seemed to be particularly bothered by Applebee’s continued assertion that cleaning bathrooms was related to the occupations of servers and bartenders; thus, any attempt by employers to use tipped employees for general cleaning duties is likely to be frowned upon.

3. Alcoholic Beverage Licensing

a. Alcohol Laws: State and Local Rules and Restrictions

The sale and distribution of “intoxicating liquors” is one of the few industries or sectors of commerce that are addressed specifically in the Constitution of the United States, as the 18th Amendment to the Constitution in 1919 ushered in the era of Prohibition.” But Prohibition became unpopular, the government was unable to collect significant revenues from taxes on alcohol, and crime increased. On December 5, 1933, the 21st Amendment of the Constitution was ratified by the states, which repealed the 18th Amendment, and Prohibition was over. The 21st Amendment, and the jurisprudence that interpreted it, provides that states have the right to regulate the importation and sale of alcohol within their borders.

In addition to state regulation, the federal government also has a right to control alcohol sales. The U.S. Treasury Department’s Alcohol and Tobacco Tax and Trade Bureau (also referred to as the “TTB”) regulates certain aspects of alcohol sales. Its principal mission is to collect the revenue on the sale of beer, wine and distilled spirits (which collectively are generally referred to as alcohol), ensure that the products are labeled, advertised and marketed in accordance with law, and administer the laws and regulations to protect consumers. The TTB does not regulate the retail sale of alcohol at the state or local level. That function has been left to the states. And some states delegate the authority to regulate alcohol sales to counties and municipalities.

The retail sale of alcoholic beverages occurs generally in two settings. First, there are sales from a retail store, such as a liquor store, beer and wine store (which are sometimes referred to as a “package store”), convenience store, or grocery store. These are sales for off-premises consumption. Second, there are sales for on-premises consumption, primarily at restaurants, bars, hotels and other entertainment facilities. Many of the retail businesses that sell alcohol for off-premises consumption (e.g., liquor stores or package stores) are not franchised and do not use franchising as a method of growth or expansion, with the notable

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136 U.S. CONST. amend XVIII and XXI.
137 U.S. CONST. amend XVIII, “prohibited the manufacture, sale, transportation and importation of intoxicating liquors.”
138 U.S. CONST. amend XXI.
exception of convenience stores and some grocery store chains. On the other hand, restaurants and hotels utilize franchising to a significant degree.\textsuperscript{140}

All fifty states and the District of Columbia regulate the sale of alcohol.\textsuperscript{141} These regulations include among other things:

- The maximum permitted blood alcohol content (or “BAC”) to determine if someone is drunk or legally impaired by alcohol;\textsuperscript{142}
- Minimum ages for persons to sell, pour/mix, and/or serve alcoholic beverages (and those ages may be different within a state or county, and other circumstances);\textsuperscript{143}
- Sales and/or serving hours restrictions, including restrictions on the days and/or hours that alcoholic beverages may be served;\textsuperscript{144}
- Restrictions regarding to whom alcohol may be served;\textsuperscript{145}
- Restrictions on where alcohol may be served;\textsuperscript{146}
- How much alcohol may be served at a time;\textsuperscript{147}
- Whether discounts on alcohol, happy hours or specials are permitted;\textsuperscript{148}

\textsuperscript{140} According to data compiled from FRANdata (www.Frandata.com), as of July 2010, there were over 32,000 hotels, sit-down restaurants (which excludes fast food restaurants, bakeries and coffee shops) and retail food establishments (which includes convenience stores) that were part of franchised chains or systems in the United States, and these categories of franchised businesses accounted for over 11% of the total franchised units in the United States.

\textsuperscript{141} For a list of states with a summary of many of the regulated activities mentioned in infra notes 142-153, see the National Restaurant Association website, www.restaurant.org/pdfs/legal/state_alc.doc

\textsuperscript{142} Many states set BAC limits at 0.08 grams of alcohol per 100 milliliters of blood or 210 liters of breath for DUI/DWI offenses, see, e.g., VA CODE ANN. § 18.2-266 (2005); FLA. STAT. § 316.193 (2009); COLO. REV. STAT. § 42-4-1301 (2010); OR. REV. STAT. § 813.010 (2009). Other states have set the BAC lower, Arizona, for example, considers a BAC of 0.04 high enough to impair driving. ARIZ. REV. STAT. § 28.1385 (2010).

\textsuperscript{143} Some states will have the same minimum age to sell, to pour/mix, and to serve alcohol, for example 18 in Massachusetts, MASS. GEN. LAWS ch. 138, § 34 (2009), 19 in Idaho, IDAHO CODE ANN. § 23-949 (2010), or 17 in Maine (with a 21 year old supervisor), ME. REV. STAT. tit. 28-A, § 704 (2003), but there are variations. For example, in California a bartender or cocktail server must be 21, but a person who is 18 may serve alcohol in a bonafide eatery establishment, if working in an area primarily designed and used for the sale and services of food, and as an incidental part of a server’s overall duties. CAL. BUS. & PROF. CODE § 25663 (2009). With so many state and county variations, a restaurant and/or hotel franchisor and/or its franchisees needs to understand the local rules before hiring employees.

\textsuperscript{144} For example, in Ohio, alcohol may be sold from 5:30 a.m. to 1:00 a.m., Monday through Saturday. Alcohol is not permitted to be sold on Sundays, unless the licensee first acquires a special Sunday permit, or, if the particular municipality has elected to allow Sunday sales. OHIO ADMIN. CODE 4301:22 (2004).

\textsuperscript{145} All fifty states have a minimum drinking age of 21 years, but some states allow minors to consume alcohol in connection with a religious ceremony or under the supervision of a parent while at home. See, e.g., N.J. STAT. § 9:178-1 (2009).

\textsuperscript{146} Georgia, for example, actually specifies the measurements of distance from the front door of the establishment which intends to sell alcohol to the nearest church, school, government treatment center, etc., required for state alcohol beverage licensees. GA. CODE § 560-2-2-32 (2007).

\textsuperscript{147} In North Carolina, for example, one must have a transportation permit in order to purchase more than eight liters of liquor or 80 liters of malt beverages at one time, unless the alcohol is in a keg (but a keg also requires a special permit). N.C. GEN. STAT. § 18B-303 (2006).
Whether unfinished wine may be removed from the premises (also referred to as “re-corking”);\(^{149}\)

The size of the premises where alcohol is served, including a minimum or maximum number of patrons or seats;\(^{150}\)

Whether the business must serve food in addition to alcohol, and whether the ratio of food sales to alcohol sales must satisfy a minimum threshold;\(^{151}\)

Who may own an interest in the liquor license;\(^{152}\) and

A limit on the number of liquor licenses held by the same person or entity.\(^{153}\)

Before a restaurant or other establishment may serve alcohol, it must apply for, and be granted, an appropriate beer, wine and/or liquor license from the appropriate state or local authority. The type of alcohol beverage license may vary depending on the nature of the business (e.g., a hotel versus a restaurant, or sales at retail for off-premises consumption versus on-premises), or the type of alcohol served (e.g., beer and wine versus “spirits” or liquor). State and local licensing rules vary considerably from state to state, and even within states. By way of example, compare New York and Maryland. In New York, there is one central State Liquor Authority (or “SLA”) which issues licenses and permits for the retail sale of alcoholic beverages (at retail stores, restaurants, bars, hotels and other facilities). While NY SLA is divided into three geographic regions for permitting, the rules, licensing fees, inspections, and approvals are determined by a centralized state agency.\(^{154}\) Maryland, on the other hand, has a decentralized regulatory scheme. Each county in Maryland has its own licensing board, which acts under a delegation of authority under state law.\(^{155}\) Each county’s licensing board sets its own rules for alcoholic beverage licensing. These various licensing authorities, whether operating at the state level, or at a county or local level, have the authority to issue, or deny issuance of, an alcoholic beverage license, charge fees for the license, limit the number or type of licenses granted, enforce the state and/or local laws, approve or disapprove transfers of

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\(^{148}\) See, e.g., Maine (licensees may not give patrons free drinks or serve more than two drinks to one person at one time), ME. REV. STAT. ANN. tit. 28-A, § 709 (2005); and Michigan (licensees may not offer single-priced, unlimited service drink specials, free drinks, or two-for-one specials), Mi. ADMIN. CODE r. 436.1707 (2008).

\(^{149}\) See, e.g., Vermont (partially consumed wine may be removed from the premises if it is re-corked and placed in the trunk of a car), VT. STAT. ANN. tit. 7, § 222 (1999); and West Virginia which does not permit patrons to take home wine purchased with a meal, W. VA. CODE R. § 60-7-3 (2009).

\(^{150}\) In Montgomery County, Maryland, certain of the alcohol licenses require an establishment to have at least 30 seats, such as the Class B beer/wine license, while the Class A beer/wine licenses do not have such requirements. Montgomery County Maryland Board of Liquor Control, License Requirements, http://www.montgomerycountymd.gov/lretmpl.asp?url=/content/dlc/liquor/LRE/lic_classes.asp. In Colorado, in order for a sport and entertainment venue to qualify for a liquor license, the venue must have a minimum of 1,500 seats. COLO. REV. STAT. § 12-47-301 (2010).

\(^{151}\) Compare, e.g., Utah, which requires that at least 70% of the restaurant’s total business must be from the sale of food, UTAH ADMIN. CODE r. R81-4A-7 (2010), and Kansas, which requires that 30% of gross receipts of a restaurant or hotel must be from food sales, KAN. STAT. ANN. § 21-4642 (2009).

\(^{152}\) Interest holders in a liquor license in North Carolina must meet all qualification requirements that the licensees themselves must meet when applying for alcohol beverage licenses. N.C. GEN. STAT. § 18B-900(c) (2004).

\(^{153}\) Wyoming allows a person to hold only one license or permit, but does not restrict that individual from being in a company that owns more than one license. WYO. STAT. ANN. § 12-4-103(b) (2010).

\(^{154}\) But even within this centralized authority, the filing fees vary based on geography within New York. N.Y. ALCO. BEV. CONT. LAW § 17 (2010).

\(^{155}\) MD. ANN. CODE art. 2B, § 6-201 (2009).
licenses, and/or revoke licenses. The varied nature and scope of the alcohol licenses that may be issued throughout the country is beyond the scope of this paper. However, for illustration, attached as Appendix A is a schedule of the types or classes of alcohol beverage licenses, and the applicable fees, that may be granted by New York’s SLA and by the Department of Liquor Control in Montgomery County, Maryland.

The cost for a liquor license can be as little as a few hundred dollars or, the license fee could be several thousand dollars. In addition, the licensing agencies often impose annual renewal fees of several hundred to several thousand dollars. However, the license fee is often only a small part of the total cost. In some jurisdictions, there is a quota on the number of licenses awarded, so the cost to obtain a license can be significantly greater than the fees paid to the government. A new operator or a transferee operator must obtain or receive an assignment of the license from an existing licensee. In those situations the cost of a liquor license could be in the multiples of $10,000. In some jurisdictions, liquor licenses have been reported to have been sold for upwards of several hundreds of thousands of dollars. An operator, or franchisee, will incur legal fees which may be substantial depending on the jurisdiction. (It is advisable to retain experienced, local counsel familiar with the liquor licensing laws, processes and procedures, and in some cases, it is desirable to retain counsel or a consultant who has a personal familiarity with the licensing officials.) In addition, the operator or franchisee will incur the time and expense to go through the local licensing hearing process, which may require addressing concerns raised by local and/or voluntary citizen associations.

Alcohol beverage licensing is not simply one additional license or permit that a restaurant, hotel, bar, or convenience store operator must secure before opening. In many cases the regulatory hurdle is higher, and/or the regulatory labyrinth is more complicated and costly, than with other permits. The franchise relationship creates additional challenges for both franchisors and franchisees.

b. Effects on Franchising

The alcohol beverage licensing laws may impact franchisors and franchisees above and beyond the time and expense to secure a license. Franchisors and franchisees need to be aware of, and proactively address, (a) laws that prohibit the sharing of alcohol sales revenue with non-licensees; (b) laws that require local ownership or impose other ownership criteria for the licensee; (c) laws that limit the number of licenses held by one person or entity; (d) laws prescribing the age for persons serving alcohol and/or hours of operation; (e) development challenges due to obtaining liquor licenses; and (f) FDD disclosures.

i. Royalty Modifications

Some alcohol beverage licensing regulations specify that the licensee is not permitted to share revenues from alcohol sales with non-licensees. This restriction may affect both franchisees and franchisors, as the royalty fee in many franchise agreements is based on gross

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156 In Kansas alone, the license fee can be as high as $3,500 or as low as $250, plus application fee, depending on the type of alcohol beverage license — hotel versus a nonprofit club, for example. KAN. STAT. ANN. § 41-2622 (2001).
158 See, e.g., the California Business and Professions Code, which restricts non-licensees from sharing in the profits from the sale of alcoholic beverages. CAL. BUS. & PROF. CODE §§ 23300 and 23355 (2009).
sales. Therefore, if royalties are paid to a franchisor based on total gross sales – including alcohol sales – those payments could violate the licensing laws.

Several options may be available to address this situation. The franchisor and franchisee may agree to royalty payments that are based on non-alcohol gross sales. While this works to a franchisee’s benefit, if alcohol sales are 10%, 20% or more of total sales, the franchisor will not receive a significant portion of its expected revenue stream, which it would use, in theory, to support the system. An alternative approach is for the franchisor and franchisee to agree upon a royalty rate that is different – and higher – than the standard rate, but it will be based on only non-alcohol gross sales. In such a scenario, the parties need to determine a rate that reflects an economic return that would be equivalent to the standard royalty payment if the royalty were calculated on all gross sales. This adjustment could be made in conjunction with the execution of the franchise agreement or before the restaurant opens. If it is done prospectively, it will be based on the expected food-to-alcohol sales ratio, and one party or the other will find the arrangement unfair after the actual revenues are calculated. The parties could agree that the adjustments be made monthly – which would be cumbersome to both parties – or annually. Whether adjustments are made monthly or annually, the process is burdensome as calculations and post-royalty adjustments are necessary. Of course, during the franchise sales process, many franchisors and franchisees may not know if local revenue-sharing restrictions will be applicable, and they might not learn of them until the permitting process. For this reason, it is desirable to include a provision in the standard form franchise agreement that addresses this issue in a prospective manner. For example, a number of franchise agreements in use today include language in the royalty section that is similar to the following:

**Alternative Royalty Fees and Other Payments.** If a state or local law in which the Restaurant is located prohibits or restricts in any way Franchisee’s ability to pay and Company’s ability to collect Royalty Fees or other amounts based on Gross Sales derived from the sale of alcoholic beverages at the Restaurant, then Company and Franchisee will renegotiate the Royalty Fees and other provisions to provide the same basic economic effect to both Company and Franchisee as otherwise provided in this Agreement, with a corresponding change to the definition of Gross Sales.

The foregoing language may not address all of the issues, including whether a local liquor licensing agency might object to such an adjustment. But at a minimum, both the franchisor and the franchisee are on notice of the issue and the need for a possible change.

### ii. Ownership and Multiple Licenses

Some liquor licensing laws include restrictions on who can hold the liquor license and/or the number of licenses that may be granted to a person or entity.\(^\text{159}\) For example, a jurisdiction may require that the licensee, or a principal of the licensee with a minimum ownership interest, be a resident in the town or county.\(^\text{160}\) If the franchised outlet will be operated in a jurisdiction

\(^{159}\) See *supra* notes 141, 152, 153.

\(^{160}\) In Texas, for example, an applicant must live in the state for a minimum of one year prior to applying for an alcohol beverage license. This requirement applies to companies which wish to own a license as well as individuals. *Tex. Alco. Bev. Code Ann.* § 6.03 (1993).
with this type of restriction, the franchisor and franchisee must address that issue, either before the franchise agreement is signed or before the liquor license is granted. The solution to this challenge may be to permit the franchisee to take on another owner, or to structure a deal between the franchisee/operator and local liquor licensee. The franchisor may need to provide the local licensee with an FDD, and the agreements should address contingencies such as the death or relocation of the local licensee, and possible defaults under the various agreements.

The restrictions on the number of licenses that a person or entity may hold create similar issues for a franchisor or franchisee. Franchisors that grant multiple unit development agreements, and multiple unit franchisees, must be mindful of these types of regulations. Franchise agreement and development agreement obligations should not require more units by the same owner than is permitted in the jurisdiction. Careful planning and structuring of ownership interests will likely enable a franchisor and its franchisees to develop the required outlets and comply with applicable law. This is another situation in which experienced local counsel can play a vital role. Generally, local liquor licensing counsel will understand the limitations and restrictions in the regulations, and the appropriate and accepted methods to structure the arrangement to obtain the required liquor licenses. But, the franchisor and franchisee must be flexible in addressing these issues.

iii. Age and Hour Restrictions

All of the state liquor licensing laws prescribe the minimum age for employees to sell, pour/mix, and serve alcohol. And many of the laws restrict alcohol sales to certain days and times. These rules are critical to all franchisees and operators. Violations of these laws can result in a temporary or permanent revocation of the liquor license, which can be grounds for termination of the franchise. Franchisors must be cognizant of these rules, as franchisors cannot try to impose contractual or operating requirements which would be contrary to these restrictions. Due to the wide variety of rules and regulations, a franchisor should not be expected to know all of the applicable laws and advise the franchisees. A recommended approach is for the franchisor to state in its franchise agreement and/or its manuals that the franchisee must comply with all state and local laws and regulations, and must comply with the applicable alcoholic beverage licensing laws and permits. It is advisable to expand on this requirement by referencing rules regulating the persons serving alcohol, the days and times when the business may serve alcohol, and other operational requirements. This puts the franchisee on notice to undertake its regulatory due diligence. Finally, the default and termination section of the franchise agreement should include a specific provision that the loss or revocation of the liquor license will be grounds for termination of the franchise.

iv. Development and Cost Issues

Franchisors and franchisees that offer alcoholic beverages will face development challenges, costs, and contractual issues that other franchised businesses may be able to avoid. For these franchisees and franchisors, understanding the alcohol beverage licensing process, and efficiently navigating that process, will minimize potential costs and delays. Securing the appropriate liquor license should be a pre-condition to opening the business. Therefore, both the franchisor and franchisee must factor the timing of the licensing process into

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161 See, e.g., Montgomery County Maryland, which limits Class B beer, wine and liquor licenses (for hotels and restaurants) to one “original” license and up to five additional licenses. MD. ANN. CODE art. 2B, § 6-201(q) (2010).
162 See supra notes 141, 143.
163 See supra notes 141, 144.
any development schedule or opening deadline, and prepare for potential delays in obtaining a liquor license. Depending on the jurisdiction, obtaining a liquor license could range from several weeks to several months (or more). With site build-out costs, construction and/or permanent financing, rental payments, and/or other costs, any delay in securing a liquor license can be quite costly. While in most cases the onus is on the franchisee to initiate the process and actively prosecute the application, both the franchisor and franchisee need to incorporate the timing into the development and opening schedule. As noted above, the franchisee should contact local alcohol beverage licensing counsel early in the process. And the franchisor may be able to assist if it has contacts in the state, or in the local area, due to previous company-owned or franchisee operations.

The assignment or transfer of a liquor license, and the potential delay in securing an assignment, can play havoc with respect to a franchise transfer. Because in some jurisdictions the number of licenses is capped by statute or regulation, obtaining an assignment, and obtaining approval for an assignment of the license from the local licensing board, can add weeks or months to a franchise transfer process. Consequently, a prospective transferee franchisee should address an assignment early in the process. Also, as soon as the franchisor becomes aware of the potential transfer, the franchisor should provide assistance and/or guidance to the prospective franchisee. The objective is to secure the assignment of the liquor license as of the day the transfer of the franchise occurs, as neither the franchisor nor the new franchisee wants to have a restaurant, hotel or convenience store operating without a valid liquor license held by the current operator. Advanced planning, and use of local counsel, should help smooth the bumps in the road in this process.

v. FDD Disclosures

If a franchisee is either required to sell, or is permitted to sell, beer, wine and/or alcohol, Item 1 of the FDD should disclose information about the liquor licensing laws. This would apply for retail stores that sell beer, wine or alcohol, as well as restaurants and hotels (and even some other business that sells alcohol, such as a bowling alley). As noted in Part II above, a detailed description, or a state-by-state list of laws is not required. The variations in the requirements under these laws, including the local permutations, would make such a detailed state-by-state disclosure impractical and burdensome to prepare.

Also, Item 7 of the FDD should disclose the estimated costs for obtaining a liquor license. With the wide range in potential costs, the authors suggest that franchisors use a more limited, but “general” or “typical” range of costs for the Item 7 chart, and then explain the variations in greater detail within the notes. These disclosures should utilize information that the franchisor receives from its franchisees, so the franchisor is able to develop a meaningful and accurate cost estimate.

Liquor licensing is fundamentally a state or local issue, and therefore should be a principal operational issue for all franchisees. But, for businesses in which alcohol sales is a significant aspect of the business, a franchisor has a critical stake in a smooth licensing process, and therefore should provide guidance and assistance, and should tailor its franchise agreements and operations manuals appropriately.

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164 If the Item 7 line item for liquor licensing stated “$500 to $250,000,” that disclosure is neither meaningful nor helpful. A much more narrow range is better, with the details appearing in the notes.
4. Dram Shop Laws and Liability

a. Generally

“Dram Shop” laws, or liquor liability laws, impose liability on vendors of alcoholic beverages, including retailers, restaurants, hotels and bars, who sell alcohol to intoxicated adults and/or to intoxicated minors when the adult or minor is subsequently involved in an alcohol related injury. These laws get their names from “dram shops” which in the 1800's were bars, taverns, or other establishments that sold alcoholic beverages by a unit of liquid measure called a “dram.” There are currently forty-one states that have enacted some form of dram shop law. Attached as Appendix B is a chart entitled “Dram Shop Liability by State.”

At common law, there was no cause of action against a party who sold or furnished alcoholic beverages to a person who was subsequently injured by the intoxicated person. And the intoxicated person did not have a cause of action against the seller. The legal theory was that the consumption of alcohol was the proximate cause of the injury, and not the act of selling it. However, over time, and in particular in response to an increase in drunk driving accidents and deaths, and an increase in underage drinking and related drunk driving accidents, public perception changed, and so did public policy. Injured parties, courts, and legislatures started to view the servers of alcohol as at least a contributing factor in drunk driving. Therefore, by imposing liability on the source of the alcohol, the legislatures thought dram shop laws will aid in the reduction of drunk driving accidents. In addition, the businesses that sold the alcohol may be most able to absorb the cost of the liability (or the increased insurance costs).

There are no federal dram shop or liquor liability laws. Dram shop laws exist only at the state level. Dram shop laws vary by state, and may impose different types of liability. The vast majority of dram shop laws impose liability on the seller of alcohol to intoxicated adults, and/or impose liability on the seller of alcohol to minors or intoxicated minors. But each state determines the scope and extent of liability. Some state dram shop laws impose liability on certain vendors and in certain situations, while other laws may specifically exclude a vendor or situation from liability.

As examples of the state variations in these laws, some dram shop laws may:

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166 Some states may not have a specific dram shop law, but may impose criminal liability on dram shop owners for negligent serving of alcohol, or may permit civil claims for such actions. See, http://web.ku.edu/~rlevy/PPC_F03/Drafts/Lloyd.pdf. The chart at Appendix B is based on several sources, including data from “LexisNexis 50 State Survey, Legislation & Regulations - Dram Shop Liability” (August 2008) (available for a fee) at www.lexis.com/research/retrieve; a chart created by, and included with the article authored by, Nina J. Emerson and Sarah B. Struebel, Another Look at Dram Shop Liability, 73 Wis. Lawyer No. 8 (Aug. 2000) (“Emerson & Struebel”); “Alcohol Alert” at http://www.alcoholalert.com/drunk-driving-dram-shop.html (last visited June 12, 2010); and Mothers Against Drunk Driving, at http://www.madd.org/Drunk-Driving/Drunk-driving_laws/ (last visited July 30, 2010)). The reader should be cautioned that various sources identify and list dram shop statutes, regulations and liability differently, and the reader should review a state’s statutes, regulations and applicable case law to determine the scope of any dram shop or liquor liability in a state.
168 See Diane Schmauder Kane, Annotation, Social Host’s Liability for Death or Injuries Incurred by Person to Whom Alcohol was Served, 54 A.L.R. 5th 313 (1999).
169 Emerson & Struebel, supra note 166.
170 Id.
171 Id.
limit, or cap, the potential damages that a vendor may be required to pay.\textsuperscript{172}

limit monetary awards for liquor liability to actual damages.\textsuperscript{173}

impose statutory penalties for improper serving of alcoholic beverages.\textsuperscript{174}

limit or prohibit claims from certain classes of individuals. For example, an intoxicated patron who causes an accident will not have a claim against the vendor.\textsuperscript{175}

allow for claims against the server in addition to the owner of the establishment, or may permit claims only against the vendor/owner.\textsuperscript{176}

impose liability on non-commercial servers, such as associations, clubs, and businesses, and/or other “social hosts” for serving intoxicated adults and/or minors.\textsuperscript{177}

As noted above, some states have no dram shop law.\textsuperscript{178}

A dram shop law may be applicable to a business that sells alcohol for on-premises consumption, or for off-premises consumption, may impact hiring decisions, may affect the nature, scope and frequency of the training provided to staff, and may influence insurance costs. To the extent these businesses are franchised outlets, additional issues arise for the franchisees and the franchisors.

\textbf{b. Franchising}

A franchisor and/or a franchisee that operates a bar, restaurant, tavern, hotel, or entertainment venue (e.g. bowling alley) that offers alcohol, or a franchisor or franchisee that operates a convenience store, retail store, or grocery store that sells alcohol, must be knowledgeable about the local dram shop laws.\textsuperscript{179} Liquor liability and dram shop laws may impact the franchisor-franchisee relationship in several ways. First, the potential liability of the franchisee for serving intoxicated or underage persons may give rise to vicarious liability for the franchisor. Second, to mitigate potential dram shop claims, franchisors may suggest or require that franchisees participate in alcohol awareness and server training programs. Third, liquor liability insurance is often required as a condition of obtaining a liquor license, so the franchisee

\textsuperscript{172} See, e.g., in Colorado, liability is limited to $150,000, \textit{Colo. Code Regs.} § 12-47-801 (1998), in New Mexico, liability is limited to $50,000 for injury or death of one person and $20,000 for damage to property, \textit{N.M. Code R.} § 41-11-1 (1978); and, in Connecticut, liability is capped at $250,000 per accident, \textit{Conn. Gen. Stat.} § 30-102 (2003).


\textsuperscript{174} See, e.g., \textit{Wis. Stat.} § 125.035 (2010).


\textsuperscript{177} We will not address social host liability, or similar private organization liability, as these issues rarely arise in a franchise context.

\textsuperscript{178} See, \textit{Appendix B} and discussion at note 166 \textit{supra}.

\textsuperscript{179} Generally speaking, dram shop laws will not impose liability on retail sales of alcohol for off-premises consumption, except in the case of sales to minors. \textit{Emerson & Struebel, supra} note 166.
network’s insurance requirements should also adequately address liquor liability insurance. We will address several of these franchise-specific issues related to dram shop laws.

i. Vicarious Liability

As discussed in Part II above, franchisors may become vicariously liable for the actions of their franchisees. Several liquor liability cases involving franchisors illustrate how a franchisor may be liable for dram shop law infractions by a franchisee.

A primary argument advanced by plaintiffs that a franchisor should be vicariously liable for the acts of their franchisees is that the franchisor "controlled" the instrumentality that caused the harm. In liquor liability cases, plaintiffs allege that the control is evident in the franchisor’s right to specify the products sold at the franchised business, the franchisor’s control over the franchisee’s method of operation, the franchisor's training of its franchisees and their employees, the franchisor’s right to share in the proceeds of the alcohol sales (through royalty fees), and on-going franchisor oversight and inspection of the franchisee’s business. Plaintiffs will look to the language of the franchise agreement and/or the operating manuals for support for these arguments, as these documents often address operational issues and compliance with brand or system standards. The following two cases highlight the issue of the control that a franchisor may exercise over its franchisees, and whether that control may be sufficient to find the franchisor vicariously liable for dram shop law claims.

In *Pate v. Alian*, 180 a restaurant franchisee served beer to an intoxicated patron, and later, while driving his car, the intoxicated patron hit and injured a motorcycle rider. Under the Oklahoma Dram Shop law, the "commercial vendor" is liable for injuries caused by the intoxicated patron.181 Rahman Alian was the franchisee of Pizza Inn, Inc. The franchise agreement did not require Alian to sell alcohol, but specified that if the franchisee decided to sell alcohol, it must comply with all local laws.182 Alian chose to sell alcohol and obtained the required "commercial vendor" license under Oklahoma law. It was Alian's employee who sold Larry Martinez and his wife two pitchers of beer after they arrived to the restaurant already intoxicated.183 However, the plaintiff alleged that Pizza Inn, the franchisor, maintained or could have maintained control over the franchised business with respect to the sale or service of alcohol, and therefore, Pizza Inn was also liable for the injuries.184

The plaintiff pointed to the franchise agreement as evidence of franchisor control. The franchisor received a four percent royalty on the restaurant's gross sales, which included the sale of alcoholic beverages.185 The franchise agreement permitted Pizza Inn to terminate the franchise agreement for the franchisee’s failure to operate according to Pizza Inn's requirements.186 The contract directed the franchisee to carry insurance and identify the franchisor as an additional insured. Pizza Inn had access to the restaurant.187 The court found that these elements were not sufficient control over the sale of alcoholic beverages to impose liability on Pizza Inn. The court held that Pizza Inn did not own or control the premises, was not

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181 *Id.* at 86-87; OKLA. ADMIN. CODE § 37-537 (2009).
182 *Pate v. Alian* at 87.
183 *Id.* at 86.
184 *Id.* at 89.
185 *Id.*
186 *Id.*
187 *Id.*
the “commercial vendor” who held the liquor license, and did not require that the franchisee sell alcohol.\(^{188}\) In fact, Pizza Inn did not sell alcohol at its company-owned restaurants. Also, under the franchise agreement, the franchisee agreed to abide by all state alcoholic beverage laws. Interestingly, Pizza Inn did not conduct alcohol beverage sales awareness training.\(^{189}\) The court found that due to the franchisee’s voluntary decision to sell alcohol, the franchisee’s duty to abide by the law, and Pizza Inn’s lack of involvement in alcohol sales and training (despite receiving royalties on the sale of alcohol), Pizza Inn did not exercise control over this aspect of the business and did not have a duty to the plaintiff under the dram shop law.\(^{190}\)

*Carrick v. Franchise Associates, Inc.*\(^{191}\) is another case in which the court found that the franchisor did not exercise sufficient control over the operation of the restaurant at the hotel to give rise to liability under the Vermont Dram Shop Act. In *Carrick*, the franchisee failed to stop serving alcohol to an intoxicated customer who subsequently was involved in a fatal car accident.\(^{192}\) The plaintiff alleged that the franchisor failed to take reasonable steps to prevent the franchisee/operator from overserving the customer.\(^{193}\) The Vermont Dram Shop Act provides for liability against any person who “caused in whole or in part” the intoxication or the sale of intoxicating liquor that caused an injury.\(^{194}\) The appellate court upheld the trial court’s ruling that the franchisor was not liable because it did not furnish the alcohol to the patron.\(^{195}\) In analyzing the “control” issues, the court said that the only evidence of the franchisor’s control was the franchise agreement, which granted the franchisor the power to “determine, prescribe and approve standards” for restaurant services, and granted the franchisor the right to inspect the operation of the franchisee’s business.\(^{196}\) And, if the franchisee failed to abide by system standards, the franchisee could be terminated.\(^{197}\) In addition, the court noted that the franchisor had an economic interest in alcohol beverage sales, as it received a royalty on all such sales.\(^{198}\) Despite these arguments, the court refused to find that the franchisor controlled the operations. The court noted, and the plaintiffs admitted, that there was no evidence that the franchisor actually provided bartender training or an alcohol or intoxication awareness program, and the operating manuals were not in evidence.\(^{199}\) Thus, due to the lack of compelling evidence of franchisor control, the franchisor was not vicariously liable.\(^{200}\)

The franchisor in *Pate* clearly exercised less control than the franchisor in *Carrick*. But, the *Carrick* case should not be viewed as a “win” for franchisors, nor as a roadmap to escape liability. The franchisor “urged [the court] to hold that franchisors are immune from liability under the Vermont Dram Shop Act, on the grounds that [franchisors] do not furnish alcohol to consumers.”\(^{201}\) The court only went so far as to say that the plaintiffs did not present sufficient evidence to hold the franchisor liable. Another court, and/or a court construing a slightly different law, and/or evaluating different facts or evidence that suggests a greater degree of

\(^{188}\) *Id.* at 90.

\(^{189}\) *Id.*

\(^{190}\) *Id.*


\(^{192}\) *Id.* at 419.

\(^{193}\) *Id.*

\(^{194}\) *Id.*; *VT. STAT. ANN.* tit. 7 § 501 (2009).

\(^{195}\) *Carrick v. Franchise Assocs., Inc.* at 420-421.

\(^{196}\) *Id.* at 420.

\(^{197}\) *Id.* at 421.

\(^{198}\) *Id.*

\(^{199}\) *Id.* at 421.

\(^{200}\) *Id.*

\(^{201}\) *Id.*
control being exercised by a franchisor, could very well reach a different conclusion and find a franchisor liable.

Even if a "control" argument may not be strong enough to find a franchisor vicariously liable, a franchisor may find itself ensnared in a liquor liability claim. One approach that plaintiffs pursue in cases against franchisors, is that the franchisee was the agent of the franchisor. To demonstrate the agency relationship, the plaintiffs try to show that the franchisor and franchisee were acting in concert. Depending on the requirements of the applicable alcohol beverage licensing regulations, a franchisor that is fairly well removed from the daily operations of the franchised business may nonetheless be perceived to be the alcohol beverage licensee, or permittee, and therefore be at risk for dram shop liability for its franchisees. Two cases illustrate the need for a franchisor to (a) understand the local dram shop and liquor licensing laws, and (b) maintain sufficient independence from that process.

**Wickham v. Southland Corp.** involved the sale of alcoholic beverages at a franchised 7-Eleven store to an intoxicated minor, who then drove a vehicle which injured two people and killed a third. The plaintiffs sued Southland (the 7-Eleven franchisor) under a theory of apparent agency. Part of plaintiff's case included an allegation that Southland was a "co-licensee" on the beer and wine license granted to the store. Southland had signed the application as "applicant," but this was done in conjunction with the transfer of the license to the new franchisee as part of a transfer of the franchise. The ABC license was granted to "Campbell Vallere E; Southland # 13974." The reference to "Southland" was the 7-Eleven store number. The court reviewed the application, as well as the circumstances surrounding the application, and the court rejected the argument that Southland was a co-licensee. But the court did note that Southland was required to disclose its interest in the proceeds from the sale of beer and wine, as it would receive royalties on the sale of beer and wine, and other products, from the store. The fact that the franchisor had a financial interest in the sale of alcohol is one reason why the franchisor's name could appear on an alcoholic beverage license application, which could lead a plaintiff to argue that the franchisor – alone or in concert with the franchisee – was the licensee or permittee responsible for the dram shop law violation.

In **Jackson v. Moreno**, a fatal automobile accident was caused by a customer who drove while intoxicated after purchasing beer from a 7-Eleven store. The trial court dismissed Southland, the franchisor, based on the theory that Southland was not an "owner" or "permitter" within the meaning of the Illinois Dram Shop law. The appellate court overturned that decision and found that Southland could be potentially liable for injuries caused by the franchisee's customers. This case turned on the application of the Illinois Dram Shop law to owners of businesses that sell alcohol, and those that permit others to sell alcohol on the premises. In this case, the owner of the property leased the premises to Southland, with the

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202 See Part III.A.3 above.
204 Id. at 51.
205 Id. at 60.
206 Id. at 53.
207 Id.
208 Id. at 57.
209 Id. at 56.
211 Id. at 505.
212 Id.
knowledge that the 7-Eleven store would sell alcohol.\textsuperscript{213} The 7-Eleven store was operated by Southland’s franchisee, under a franchise agreement. The Illinois Dram Shop law provides that “any person owning, renting, leasing or permitting the occupation of any building or premises with knowledge that alcoholic liquors are to be sold therein... shall be liable, severally and jointly, with the person selling or giving the liquors.” (Emphasis added).\textsuperscript{214} The court found that Southland, as the lessee and franchisor, contemplated the sale of alcoholic beverages, and therefore, Southland “permitted” the occupation of the premises knowing that alcoholic beverages would be sold.\textsuperscript{215} In addition, Southland’s franchise agreement specifically regulated alcohol sales and referred to indemnification for liquor liability.\textsuperscript{216} The court found that Southland “maintained a meaningful degree of control over the premises.”\textsuperscript{217}

The \textit{Jackson} and \textit{Wickham} cases highlight a critical lesson for franchisors. The franchisor must understand the alcohol licensing and permitting rules in the jurisdictions in which its franchisees will operate. A franchisor must ascertain whether a franchisee has obtained its beer and wine or liquor license properly, and whether any aspect of the application may suggest a principal-agent relationship. To the extent that the permitting process and/or the ownership or lease arrangements may give rise to direct liability under the dram shop laws, the franchisor should protect itself through increased insurance coverages, indemnifications, and alcohol server training.

Vicarious liability in the case law is not consistent and franchisors are often at risk for being vicariously liable for franchisee actions, despite their best efforts to insulate themselves. Liquor liability is no exception.

How might a franchisor structure its relationships to reduce its risk or exposure? The following are suggestions that we have gleaned from the case law. While they are not sure-fire defenses, they should be considered as part of a franchise network’s operational rules.

\textbf{ii. Alcohol Sales and Server Training}

Alcohol server training is a form of education typically provided to servers and sellers of alcoholic beverages. The purpose of these courses is to train employees to recognize intoxicated and/or underage drinkers, to carefully and responsibly intervene to limit or prevent additional alcoholic beverage consumption, and to prevent intoxication, drunk driving and underage drinking. Alcohol server training can mitigate liability for an establishment in a liquor liability case by providing a "reasonable efforts defense."\textsuperscript{218} In addition, participation in these training programs can reduce liquor liability premiums paid by restaurants, bars, hotels, etc. Finally, the alcoholic beverage licenses in many states are contingent upon the licensee or permittee obtaining this form of training for its employees.

There are many alcohol server training programs, ranging from local or county programs, to state-wide programs, to national programs. Two such programs are "TIPS" (Training for Intervention ProcedureS)\textsuperscript{219} and ServSafe.\textsuperscript{220} Many programs are private programs

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\textsuperscript{213} \textit{id.} at 507.
\textsuperscript{214} \textit{id.} at 506; 235 ILL. COMP. STAT. 5/6-21 (2006).
\textsuperscript{215} \textit{Jackson v. Moreno} at 509.
\textsuperscript{216} \textit{id.}
\textsuperscript{217} \textit{id.}
\textsuperscript{218} See, e.g., Maine, ME. REV. STAT. ANN. tit. 28-A , § 2515 (2009).
\end{flushleft}
but they are certified by a state agency. Some of these programs are conducted online, and others in a classroom.

Most, if not all, franchisors with businesses that serve alcohol wish to minimize, and if possible prevent, alcohol liability or dram shop claims, at their franchised outlets and company owned operations. Franchisors recognize the costs to franchisees, the potential expense to the franchisors, and the societal benefit of reducing intoxication, drunk driving accidents and underage drinking. However, a franchisor may be concerned that by mandating certain actions or providing certain training, the franchisor may be increasing its potential exposure because it may be viewed as "controlling" the instrumentality that causes harm to a third party. A franchisor may decide to do nothing, other than suggest that the franchisees comply with applicable law. That approach, while minimizing risk to the franchisor, provides little guidance to the franchisee. At the other end of the spectrum, a franchisor could develop its own alcohol server training, and require that all franchisees and their employees attend and successfully complete that training. While this approach may provide comfort that the franchisees are trained and meet the franchisor's standard, this approach will significantly increase a franchisor's potential liability.

The authors suggest a hybrid or middle ground. First, the franchise agreement and manuals should require that the franchisees comply with all laws and regulations. The operating manual should include a reference to state-mandated alcohol server training, as well as state that the franchisees should comply with applicable training requirements. Second, if the franchisee operates in a state that mandates this training as a condition of obtaining a license, the franchisor can reference that requirement and request that each franchisee certify that its employees completed the training program. Third, for franchisees in states that do not require these training programs, the franchisor should suggest – but not mandate – in its manuals that franchisees and their employees attend and satisfactorily complete these training programs. In lieu of developing a training program itself, the franchisor should refer the franchisee to industry approved training programs and/or state approved programs. This approach provides guidance and suggestions for good business practices, and compliance with applicable regulations, but does not mandate a specific franchisor-designated standard. It also removes the franchisor from adopting and conducting a specific training program. If the training program is approved by the state and/or approved by the franchisee's insurance carrier or policy, the training program may be presumed to be sufficient to comply with the law and reduce exposure to claims.

iii. Insurance

As a corollary to alcohol server training, the franchisor should require that the franchisee obtain and maintain appropriate and adequate insurance and the franchise agreement's indemnification clause should cover the franchisor for this sort of liability. For businesses that

(Cont’d)

221 See, e.g., Utah State Division of Substance Abuse website, http://www.dsamh.utah.gov/, which has a link to all of the state approved alcohol server educational programs.
222 See, for example, the Pate case above.
223 See discussion of vicarious liability in the articles cited at footnote 2 supra.
224 See supra note 221.

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serve alcohol, owners must obtain liquor liability insurance. While insurance requirements are often included in franchise agreements, the franchise agreement or the manual should specify the type of insurance, coverage limits, any permitted exclusion, and any required coverages. In addition, the franchisor should be listed as an additional name insured.

As noted above, liquor liability insurance may be mandated by the state as a condition of granting the alcoholic beverage license. But, if the franchisor desires that there be additional coverage, or insurance that covers certain risks not specified in the state minimum coverage, the franchisor should specify its preferences.

Dram shop law liability is something that neither a franchisor nor its franchisees can avoid completely. However, with knowledge of the applicable laws (which vary from state to state), the alcohol beverage licensing and permitting process, and responsible and regular training, the risks – to both franchisees and franchisors – can be mitigated.

iv. FDD Disclosures

Dram shop laws are a type of industry-specific business law or regulation that should be disclosed in Item 1 of FDDs. A franchisor need not provide a state-by-state list of statutory citations, nor a detailed discussion of the variations in state law. Rather, as discussed in Part II above, a general reference to dram shop laws and their potential impact on the business should be sufficient to put a prospective franchisee on notice of these laws.

B. Consumer Focused Laws

There are too many kinds of consumer protection laws to address all of them in this section of the paper. Instead, we have focused on several consumer focused laws that may be of more relevance to many franchise systems.

1. Product Warranty Laws

Product warranties are subject to a number of federal and state laws. Product warranties arise when a franchisor sells goods to its franchisees or extends its warranty to the customer of the franchisee, and when the franchisee resells the franchisor’s goods or the goods of a third party to its customers. A number of product franchisors require their franchisees to pass the franchisor’s warranty to their customers, or to provide their own warranty to their customers. Warranties relating to services provided are subject to general common law principles, although some courts will look to the Uniform Commercial Code (“U.C.C.”) for guidance on warranty obligations. This discussion focuses on product warranties.

a. Uniform Commercial Code

Article 2 of the U.C.C. has several provisions dealing with warranty law and will apply in all domestic sale of goods situations unless properly disclaimed. As a caution, the National

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225 For a discussion of liquor liability insurance policies and coverages, see Susan Vincent and G. Thomas MacIntosh II, Insuring Against Franchisor Vicarious Liability, 34 International Franchise Association Legal Symposium (2001).
Conference of Commissioners on Uniform State Laws (“NCCUSL”) adopted a revised Article 2 in 2003, but as of the date this paper was written, no state had yet adopted the revised Article 2 and it is not likely that any state will. Among other changes, the warranty provisions were substantially revised. When analyzing the U.C.C. warranty obligations, the lawyer should review the U.C.C. as it has been adopted by the states involved in the transaction – not the current version distributed by NCCUSL. 228

We will briefly review the U.C.C. warranty provisions. An important thing to keep in mind when reviewing the U.C.C. provisions is that the doctrine of privity applies, except in the one limited circumstance described below. That means that the U.C.C. warranty obligations extend only to the direct purchaser of the goods from the seller or to other persons that seller expressly extends its warranty. In the franchise situation that means the franchisor’s warranty obligations extend only to the franchisee buying the goods, unless the franchisor expressly extends its warranty to the customers of the franchisee, except as otherwise discussed below.

Section 2-312(1) provides that in a contract for sale, there is a warranty that title is good and that the goods are being delivered free from any liens or encumbrances. Under Section 2-312(2), this warranty can only be excluded or modified by specific language or circumstances which give the buyer reason to know the seller does not claim title or is only selling the right or title he has. Section 2-312(3) is a provision often overlooked by practitioners. It provides that a seller who is a merchant warrants that goods will be delivered free of the rightful claim of any third person by way of infringement of a patent or trademark. This is not true if the buyer orders goods to be assembled, prepared or manufactured to his own specifications. 229

Sections 2-314 to 2-318 deal with warranties relating to the characteristics of the goods themselves. Section 2-313(1) provides that express warranties by the seller are created in one of three ways: (a) by an affirmation of fact or promise which becomes a basis of the bargain; (b) by any description of the goods that becomes a basis of the bargain; or (c) by any sample or model that is made a basis of the bargain.

Section 2-314(a) is an implied warranty of merchantability that, unless excluded or modified, provides that where the seller is a merchant with respect to those kinds of goods, there is a warranty that the goods are merchantable (as that term is defined in Section 2-314(2)). Essentially, the goods must be fit for the ordinary purposes for which they are used. Section 2-315 is an implied warranty of fitness for a particular purpose where the seller, at the time of contracting, has reason to know the particular purpose for which the goods are required and that the buyer is relying on the seller’s skill and judgment to select or furnish suitable goods. A “particular purpose” differs from an ordinary purpose and envisions a specific use by the buyer which is peculiar to the nature of his business. 230 The implied warranty of fitness for a particular purpose is not likely to arise with respect to the sale of off-the-shelf goods.

(Cont’d)

227 In an international sale of goods situation, the United Nations Convention on Contracts for the International Sale of Goods (1980) (“CISG”) will apply if the parties are both in countries that have ratified the treaty, unless it is excluded or modified.


229 For a full discussion of the warranty of title and against patent infringement, see BARKLEY CLARK AND CHRISTOPHER SMITH, THE LAW OF PRODUCT WARRANTIES, Vol. 1, §§3:1 to 3:18 (2d Ed. 2007) (“Clark/Smith”).

230 U.C.C. §2-313, Comment 2.
Section 2-316(2) allows the seller to exclude or modify warranties. To modify the implied warranty of merchantability, the language must mention merchantability and be conspicuous. To exclude or modify any implied warranty of fitness, the exclusion must be by a writing and conspicuous. Under Section 2-316(3), all implied warranties are excluded by expressions like “as is” or “with all faults”. To be conspicuous, the language should be printed in bold faced type or all capitals, and preferably both. For example:

THE FOREGOING WARRANTY IS IN LIEU OF AND EXCLUDES ALL OTHER WARRANTIES NOT EXPRESSLY SET FORTH HEREIN, WHETHER EXPRESS OR IMPLIED BY OPERATION OF LAW OR OTHERWISE, INCLUDING BUT NOT LIMITED TO ANY IMPLIED WARRANTIES OF MERCHANTABILITY OR FITNESS.

Note: the ability to exclude or modify implied warranties is affected by the federal warranty law and some state laws. See discussion below.

The exception to the privity rule is embodied in Section 2-318 of the U.C.C. which gave the states a choice of adopting one of three alternatives. Alternative A: adopted by 29 states, says a seller’s express or implied warranty extends to any natural person who is in the family or household of his buyer or who is a guest if that person is expected to use, consume or be affected by the goods and who is injured by breach of the warranty. Alternative B, adopted by 8 states, extends express or implied warranties to any natural person who may be expected to use, consume or be affected by the goods and who is injured by breach of the warranty. Alternative C, adopted by 6 states, provides that an express or implied warranty, extends to any person who may reasonably be expected to use, consume or be affected by the goods and who is injured by breach of the warranty.231 These provisions cannot be excluded or modified.232

b. Magnuson-Moss Warranty Act

If the franchisor intends to provide a written warranty on a consumer product to the customers of a franchisee, the Magnuson-Moss Warranty Act233 and the Federal Trade Commission (“FTC”) implementing regulations234 will govern the terms and availability of the warranty, and provide remedies for violations. Significantly, the federal warranty law does not preempt the U.C.C., but does affect the U.C.C. provisions discussed above.

The Magnuson-Moss Warranty Act applies to written warranties on a “consumer product”, which is defined in Section 101(1) as:

(1) The term “consumer product” means any tangible personal property which is distributed in commerce and which is normally used for personal, family, or household purposes (including any

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232 For a full discussion of U.C.C. warranty law, including remedies, see Barkley/Smith, chapters 2 through 13.


234 16 C.F.R. Parts 700-703.
such property intended to be attached to or installed in any real property without regard to whether it is so attached or installed).\textsuperscript{235}

A “consumer” is defined in Section 101(3) as

\begin{enumerate}
\item The term “consumer” means a buyer (other than for purposes of resale) of any consumer product, any person to whom such product is transferred during the duration of an implied or written warranty (or service contract) applicable to the product, and any other person who is entitled by the terms of such warranty (or service contract) or under applicable State law to enforce against the warrantor (or service contractor) the obligations of the warranty (or service contract).\textsuperscript{236}
\end{enumerate}

“Written warranty” is defined in Section 103(6) as

\begin{enumerate}
\item The term “written warranty” means
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\item any written affirmation of fact or written promise made in connection with the sale of a consumer product by a supplier to a buyer which relates to the nature of the material or workmanship and affirms or promises that such material or workmanship is defect free or will meet a specified level of performance over a specified period of time; or
\item any undertaking in writing in connection with the sale by a supplier of a consumer product to refund, repair, replace, or take other remedial action with respect to such product in the event that such product fails to meet the specifications set forth in the undertaking,
\end{enumerate}

which written affirmation, promise, or undertaking becomes part of the basis of the bargain between a supplier and a buyer for purposes other than resale of such product.\textsuperscript{237}

Essentially, the Magnuson-Moss Warranty Act and FTC rules require several things: (1) the designation of a warranty as either “Full (Statement of Duration) Warranty” or “Limited Warranty”\textsuperscript{238}, (2) that the warranty contain certain specific warranty terms and statements,\textsuperscript{239} and (3) that the warranty be made available to the buyer prior to sale so the buyer can review the terms.\textsuperscript{240}

A “full” warranty is one that meets the federal minimum standards of Section 104 of the Act\textsuperscript{241} and essentially requires the warrantor to remedy the defective goods without charge and

\begin{footnotes}
\textsuperscript{237} Section 101(6), 15 U.S.C. §2301(6).
\textsuperscript{238} Section 103(a), 15 U.S.C. §2303(a).
\textsuperscript{239} Section 102(a), 15 U.S.C. §2302(a); 16 C.F.R. §701.3.
\textsuperscript{240} Section 102(b), 15 U.S.C. §2302(b); 16 C.F.R. §702.3.
\end{footnotes}
not impose any limitation on implied warranties, exclude or limit consequential damages, or restrict the rights of any subsequent transferee of the product. Because few warrantors are willing to go so far, few consumer warranties are “Full Warranties” and most are “Limited Warranties.”

The Magnuson-Moss Warranty Act and FTC rules and interpretations impose other restrictions on the warrantor. First, no supplier can disclaim or modify any implied warranty to a consumer that arises under state law (U.C.C.), except that the duration of the implied warranty can be limited to the duration of a written warranty of reasonable duration if it is conscionable and set forth in clear and unmistakable language prominently displayed on the face of the warranty.\footnote{242} Second, a warrantor cannot indicate in any written warranty, either directly or indirectly, that the decision of the warrantor or any designated third party is final and binding in any dispute concerning the warranty. Nor can the warrantor state that it alone shall determine what is a defect under the agreement. Those statements are considered deceptive.\footnote{243}

Third, section 102(c) of the Magnuson-Moss Warranty Act prohibits tying arrangements that condition coverage on the consumer’s use of an article or service identified by a brand, trade or corporate name unless it is provided without charge to the consumer.\footnote{244} The FTC rules further provide that under a limited warranty that provides only for replacement of defective parts and no portion of the labor charges, the consumer cannot be required to use service (labor) identified by the warrantor to install the replacement part.\footnote{245} And a not uncommon requirement that only authorized services or parts be used is prohibited.

\(c\) No warrantor may condition the continued validity of a warranty on the use of only authorized repair service and/or authorized replacement parts for non-warranty service and maintenance. For example, provisions such as “This warranty is void if service is performed by anyone other than an authorized ‘ABC’ dealer and all replacements parts must be genuine ‘ABC’ parts,” and the like, are prohibited where the service or parts are not covered by the warranty.\footnote{246}

Fourth, the warrantor can designate representatives to perform duties under its written or implied warranty, but the warrantor must make “reasonable” arrangements for compensation of such designated representatives.\footnote{247} The legislative history of the Magnuson-Moss Warranty Act makes clear that this does not necessitate cash payment, as long as whatever method is used insures that such compensation is equitable.\footnote{248} However, nothing in section 107 is intended to dictate the method of compensation for warranty or service contract work.\footnote{249} A sample Limited Warranty is attached as Appendix C.

\footnote{242} Sections 108(a), (b); 15 U.S.C. §§2308(a), (b).
\footnote{243} 16 C.F.R. § 700.8.
\footnote{244} Section 102(c), 15 U.S.C. §2302(c).
\footnote{245} 16 C.F.R. §700.10(b).
\footnote{246} 16 C.F.R. §700.10(c).
\footnote{247} Section 107, 15 U.S.C. §2307.
In a not uncommon situation, the franchisor or an affiliate may sell products to the franchisees and ask them to pass its limited warranty directly to the franchisee’s customers. In such cases, the warranty must meet the FTC requirements for the content of the warranty, the franchisor must give the franchisee warranty materials to make available to the customer to review prior to sale, and the franchisor must make reasonable arrangements for compensation of the franchisee if the franchisee is going to provide warranty services under the franchisor’s warranty. If the franchisee is providing its own warranty to its customers, it must comply with the written disclosure terms and pre-sale availability rule.

Section 110 of the Magnuson-Moss Warranty Act provides a procedure for informal dispute settlement mechanisms similar to an enhanced mediation process. A warrantor can set up a procedure that complies with the FTC’s implementing rules for what is called a “Mechanism.” If a Mechanism is in place and properly disclosed to the consumer, the consumer cannot commence a civil action (other than a class action) unless he initially resorts to this procedure. In any civil action, while decisions of the Mechanism are not legally binding on any person, any decision in such procedure is admissible in evidence. The automobile industry often uses this procedure. Section 110 also provides a civil remedy for violation of the Magnuson-Moss Warranty Act, including costs and expenses (including attorney’s fees incurred by the plaintiff) and provides that no class action can be brought unless the person obligated under the warranty has a reasonable opportunity to cure a failure to comply with a warranty obligation. Only the warrantor actually making the warranty can have rights enforced against it.

The FTC periodically takes enforcement action to remind various warrantors of their obligations under the Magnuson-Moss Warranty Act. Typically the enforcement actions have involved well-known retailers. One of the first major enforcement actions was taken against Montgomery Ward and Company for failure to make the text of written warranties readily available to prospective buyers prior to sale. Similar action was later taken against Circuit City Stores.

In addition, private parties often sue warrantors claiming a violation of the Magnuson-Moss Warranty Act, particularly when an automobile is involved. Section 110(d) of the Magnuson-Moss Warranty Act gives a consumer who is damaged by the failure of a supplier, warrantor or service contractor to comply with any obligation under the Magnuson-Moss Warranty Act or under any written warranty, implied warranty or service contract, the right to bring suit for damages and other legal and equitable relief in any court of competent jurisdiction in the U.S., or in an appropriate U.S. district court as long as (i) any individual claim is at least $25, (ii) the amount in controversy is $50,000 or more for all claims in the suit, or (iii) the number of plaintiffs in a class action total 100 or more.
c. **State Limitations on Disclaimers of Implied Warranties**

In addition to the FTC restrictions on implied warranties when a written consumer warranty is provided, a number of states have enacted statutes that prohibit disclaimers of implied warranties of merchantability or fitness for a particular purpose in consumer transactions.

For example, the following states have amended Section 2-316(2) of the U.C.C: Alabama, California, Connecticut, District of Columbia, Kansas, Maine, Maryland, Massachusetts, Minnesota, Mississippi, New Hampshire, Oregon, Rhode Island, Vermont, Washington and West Virginia. In Appendix D, we have provided a brief description of various state provisions. The modifying statutes affect both new and used goods.

Recognizing the existence of these state statutes, the FTC requires that the following statement appear in any written consumer warranty:

Some States do not allow limitations on how long an implied warranty lasts, so the above limitation may not apply to you.

d. **State Laws on Dealer Reimbursement for Warranty Work.**

Although the Magnuson-Moss Warranty Act established a flexible standard for how a manufacturer of consumer products can compensate its representatives for repairs made under the manufacturer's warranty, some state statutes stipulate that a manufacturer must pay its dealers retail value for such services. At least the following states have enacted such statutes: California, Connecticut, Minnesota, Oregon, Rhode Island and West Virginia. In Appendix E, we have provided a brief description of various state provisions.

We will provide an example. The California Song-Beverly Warranty Act requires every manufacturer of consumer goods sold in California for which an express warranty has been made either to maintain in the state sufficient service and repair facilities reasonably close to where its goods are sold to carry out the terms of the warranty, or to designate and authorize in the state as service and repair facilities independent repair or service facilities reasonably close to all areas where its goods are sold to carry out the warranty terms. The service contracts with the independent service and repair facilities can provide for a fixed schedule of rates to be charged for the warranty service or warranty repair work in conformity with the requirements of Section 1793.3(c). Sections 1793.5 and 1793.6 provide that except as otherwise provided in (Cont’d)

(Cont’d) in violation of the Magnuson-Moss Warranty Act, when it and its dealer failed to correct defects in the purchaser's new car, entitling the purchaser to bring a federal private cause of action for damages, costs and reasonable attorneys' fees); *Blumer v. Acu-Gen Biolabs, Inc.*, 638 F. Supp. 2d 81 (D. Mass. 2009) (consumer's private right of action survived challenge in claims arising out of allegations that entities and their owner violated the Magnuson-Moss Warranty Act by failing to abide by terms of warranties and guarantees; consumers alleged at least $54,450 in dispute).

**Caution:** The listing may not be exhaustive. Check the law of the applicable jurisdiction. See Stephen E. Friedman, "Text and Circumstances: Warranty Disclaimers in a World of Rolling Contracts", 44 Ariz. L. Rev. 677, 687 n. 78 (Winter, 2004); Donald F. Clifford Jr., *Non-UCC Statutory Provisions Affecting Warranty Disclaimers and Remedies in Sales of Goods*, 71 N.C.L. Rev. 1011 (April, 1993) ("Clifford").

**Caution:** The listing may not be exhaustive. Check the law of the applicable jurisdiction.

257 16 C.F.R. §701.3.

258 Caution: The listing may not be exhaustive. Check the law of the applicable jurisdiction.


260 Cal. Civ. Code §1793.3(c)
a warranty service contract, where a manufacturer does not have repair facilities in the state, the manufacturer will be liable to an independent service and repair facility who performs services or incurs obligations in giving effect to the manufacturer’s express warranties in an amount equal to the actual and reasonable costs of the service and repair, including any costs for parts and any reasonable cost of transporting the goods or parts, plus a reasonable profit.262

e. Service Contracts

Section 106 of the Magnuson-Moss Warranty Act provides that the FTC may prescribe by rule the manner and form in which the terms and conditions of service contracts are fully, clearly and conspicuously disclosed. The Warranty Law does not prohibit a supplier or warrantor from entering into a service contract with the consumer in addition to or in lieu of written warranty.263

However, the FTC has never regulated service contracts. “Service contract” is defined in Section 101(8) of the Magnuson-Moss Warranty Act as:

(8) The term “service contract” means a contract in writing to perform, over a fixed period of time or for a specified duration, services relating to the maintenance or repair (or both) of a consumer product.264

All the FTC has done so far is to adopt a regulation explaining the difference between a written warranty and service contract. The FTC explained:

(b) “Written warranty” and “service contract” are defined in sections 101(6) and 101(8) of the Act, respectively. A written warranty must be “part of the basis of the bargain.” This means that it must be conveyed at the time of sale of the consumer product and the consumer must not give any consideration beyond the purchase price of the consumer product in order to benefit from the agreement. It is not a requirement of the Act that an agreement obligate a supplier of the consumer product to a written warranty, but merely that it be part of the basis of the bargain between a supplier and a consumer. This contemplates written warranties by third-party non-suppliers.

(c) A service contract under the Act must meet the definitions of section 101(8). An agreement which would meet the definition of written warranty in section 101(6)(A) or (B) but for its failure to satisfy the basis of the bargain test is a service contract. For example, an agreement which calls for some consideration in addition to the purchase price of the consumer product, or which is entered into at some date after the purchase of the consumer product to which it applies, is a service contract. An agreement

which relates only to the performance of maintenance and/or inspection services and which is not an undertaking, promise, or affirmation with respect to a specified level of performance, or that the product is free of defects in materials or workmanship, is a service contract. An agreement to perform periodic cleaning and inspection of a product over a specified period of time, even when offered at the time of sale and without charge to the consumer, is an example of such a service contract.\textsuperscript{265}

Most likely, the FTC has not strayed into the service contract area because many states regulate them as contracts of insurance or have other applicable statutes dealing with service contracts in particular industries, particularly automotive repair.\textsuperscript{266} Those types of agreements are subject to the Magnuson-Moss Warranty Act only to the extent that they are not regulated in a particular state as the business of insurance because the McCarran-Ferguson Act, 15 U.S.C. §1011, et seq., precludes jurisdiction over the business of insurance to the extent the agreement is regulated by state law as insurance.\textsuperscript{267}

A number of states regulate service contracts, particularly in the automotive area.\textsuperscript{268} Although a full discussion is beyond the scope of the paper, a few examples may be instructive.

Illinois has a Service Contract Act\textsuperscript{269} that applies to “service contracts”:

“Service contract” means a contract or agreement whereby a service contract provider undertakes for a specified period of time, for separate and identifiable consideration, to perform the repair, replacement, or maintenance, or indemnification for such services, of any automobile, system, or consumer product in connection with the operational or structural failure due to a defect in materials or workmanship, or normal wear and tea, with or without additional provision for incidental payment or indemnity under limited circumstances, for related expenses, including, but not limited to, towing, rental, and emergency road service. Service contracts may provide for the repair, replacement, or maintenance of such property for damage resulting from power surges and accidental damage from handling. Service contracts shall not include contracts of limited duration that provide for scheduled maintenance only.\textsuperscript{270}

\textsuperscript{265} 16 C.F.R. §700.11(b)
\textsuperscript{266} In an advisory opinion, the FTC opined that automobile dealers who entered into service contracts with vehicle purchasers at the time of sale could not limit the duration of implied warranties to the duration of the service contract. FTC Advisory Opinion, 92 F.T.C. 1050, 1978 F.T.C. LEXIS 73 (1978).
\textsuperscript{267} 16 C.F.R. §700.11(c).
\textsuperscript{269} 215 ILCS 152/1 to 152/99.
\textsuperscript{270} 215 ILCS 152/5.
Service contract providers who comply with the Act are not subject to provisions of the Illinois Insurance Code.271

The Act requires that the service contract provider meet certain financial requirements, such as being insured under a service contract reimbursement policy issued by an insurer licensed in the state who will pay all sums that the service contract provider is obligated to pay under the service contract, or maintaining a funded reserve account for its obligations of not less than 40% of the gross consideration received, less claims paid, for all service contracts sold and then in place.272

Service contract providers have to register annually with the state, and, among other things, have to provide copies of all service contracts to be sold in the state.273 All service contracts have to have certain disclosures in clear and understandable language.274 The contract must be cancelable, but the service contract provider can retain a cancellation fee.275

Wisconsin takes a different approach, with its Motor Club Service Contracts law276 that applies to motor club service contracts.

“Motor club service” means the rendering, furnishing or procuring of 3 or more of the following, to any person, in connection with that person’s ownership, operation, use, or maintenance, of a motor vehicle, in consideration of that person’s being or becoming a member of, affiliated with or entitled to membership or other motor club service from any company rendering, procuring or furnishing those services by virtue of any agreement or understanding with any such company: [12 categories omitted].277

Insurance service is defined as:

“Insurance service” means any act by a company, as herein define, consisting of the selling or giving with a service contract, as herein defined, or as a result of membership in or affiliate with a company, as herein defined, a policy of insurance covering liability or loss by the holder of a service contract with any such company as the result of injury to the person of such service contract holder following an accident resulting from the ownership, maintenance, operation or use of a motor vehicle.278

The Wisconsin law requires the company offering the motor club services contract to deposit cash, securities or a bond with the Commissioner of Insurance.279 The Commissioner of

271 215 ILCS 152/10.
272 215 ILCS 152/15(1), (2).
273 215 ILCS 152/25(a).
274 215 ILCS 152/30.
275 215 ILCS 152/35.
276 W.S.A. 616.71 to 616.82.
277 W.S.A. 616.71(12)
278 W.S.A. 616.71(9).
279 W.S.A. 617.72.
Insurance will issue an annual certificate of authority and must approve all service contract forms.\textsuperscript{280}

2. FTC Guides

The FTC has issued a number of industry guides that affect consumer transactions, many of which are directly applicable to franchise programs. While they are not substantive laws, parties who ignore them do so at their peril. The FTC rules explain:

"Industry guides are administrative interpretations of laws administered by the Commission for the guidance of the public in conducting its affairs in conformity with legal requirements. They provide the basis for voluntary and simultaneous abandonment of unlawful practices by members of industry. Failure to comply with the guides may result in corrective action by the Commission under applicable statutory provisions. Guides may relate to a practice common to many industries or to specific practices of a particular industry."\textsuperscript{281}

a. Guides for the Advertising of Warranties and Guarantees

The FTC has adopted Guides for the Advertising of Warranties and Guarantees.\textsuperscript{282} Section 239.2 applies to advertisements for written warranties on consumer products covered by the Magnuson-Moss Warranty Act. If the advertisement mentions a warranty, it must disclose with such clarity and prominence as will be noticed and understood by prospective purchasers, that prior to sale, at the place where the product is sold, prospective purchasers can see the written warranty for complete details of warranty coverage. Examples of acceptable statements are included in the Guides. One example is as follows.

A. "The XYZ washing machine is backed by our limited 1 year warranty. \textit{For complete details, see our warranty at a dealer near you.}"\textsuperscript{283}

But the Guides also address two other subjects of interest. If the term "Satisfaction Guarantee", "Money Back Guarantee," "Free Trial Offer" or similar language is used in an advertisement, the seller must refund the full purchase price of the advertised product at the purchaser’s request. The advertisement must also disclose, with such clarity and prominence as will be noticed and understood by prospective purchasers, any material limitations or conditions that apply. Examples of acceptable statements are included in the Guides. One example is as follows:

Example A: (In an advertisement mentioning a satisfaction guarantee that is conditioned upon return of the unused portion within 30 days) "We guarantee your satisfaction. If not completely

\textsuperscript{280} W.S.A. 616.74, 616.76.
\textsuperscript{281} 16 C.F.R. §1.5.
\textsuperscript{282} 16 C.F.R. Part 239.
\textsuperscript{283} 16 C.F.R. §239.2(a).
satisfied with Acme Spot Remover, return the unused portion within 30 days for a full refund.”  

Finally, the Guides say that if “lifetime” or a similar representation is used in an advertisement in describing the duration of a warranty or guarantee, the advertisement must disclose, with such clarity and prominence as will be noticed and understood by prospective purchasers, the life to which the representation refers. Examples of acceptable statements are included in the Guides. One example is as follows:

Example A: (In an advertisement mentioning a lifetime guarantee on an automobile muffler where the duration of the guarantee is measured by the life of the car in which it is installed) “Our lifetime guarantee on the Whisper Muffler protects you for as long as your car runs – even if you sell it, trade it, or give it away.”  

b. **Guides Concerning the Use of the Word “Free”**.

The FTC has a Guide Concerning Use of the Word “Free and Similar Representations.” The FTC cautions that all such offers must be made with extreme care so as to avoid any possibility that a consumer may be misled or deceived. Except in the case of introductory offers, the FTC says the public understands that an offer of “free” merchandise is based on a regular price for the merchandise that must be purchased in order to avail themselves of that which is represented to be free. For consumer products, the regular price is that which the seller has openly and actively sold the product in the geographic market or trade area in which it is making the free offer in the most recent and regular course of business, for a reasonably substantial period of time, i.e., a 30 day period.

When making a “free” offer, all the terms, conditions and obligations must be set forth clearly and conspicuously at the outset of the offer, in close compensation with the offer. Putting the disclosure of the terms of the offer in a footnote of the advertisement by use of an asterisk is not regarded as disclosure at the outset. However, notice of the existence of a free offer on the main display panel of a label or package is not precluded if four criteria are met, including that no purchase be required in order to discover the terms and conditions of the offer.

If a supplier making a free offer knows that it is not being passed on by a reseller, it is improper for the supplier to continue to offer the product with the promotion and it should take steps to withdraw the free offer.

Before advertising a free promotion, the supplier should offer the product as promoted to all competing resellers as set forth in the Guides for Advertising Allowances and Other Merchandising Payments and Services. The supplier has to identify the areas in which the

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284 16 C.F.R. §239.3(b).
285 16 C.F.R. §239.4
287 16 C.F.R. §251c). The other three criteria are: (1) the notice does not constitute an offer or identify the item brought offered “Free”, (2) the notice informs the customer of the location, elsewhere on the package or label, where the required disclosures can be found, and (3) the notice and offer are not deceptive.
288 16 C.F.R. §251(d).
offer is not available and clearly state that it is available only through participating resellers, indicating the extent of participation (e.g., “some”, “all”, “a majority” or “a few”).

So that a “free” offer is special and meaningful, a single size of product or line of service should not be advertised with a “free” offer in a trade area for more than 6 months in any 12 month period. At least 30 days should elapse before another such offer is promoted in the same trade area. No more than three such offers should be made in the same area in any 12 month period. Moreover, in such period, the sale of the product in the size promoted with a “free” offer should not exceed 50% of the total volume of the sales of the product in the same size in the area.

c. Guides Against Deceptive Pricing.

The FTC Guides Against Deceptive Pricing affect a number of common pricing activities. With respect to former price comparisons, the FTC is concerned with fictitious pricing, such as whether an artificial, inflated price was established for enabling a subsequent offer of a large reduction. If a former price is set forth in an advertisement, the advertiser has to make certain that the former price is not a fictitious one.

With respect to retail price comparisons, goods may be offered at prices lower than the one being charged by others for the same merchandise in the advertiser’s trade area in which it does business. The advertiser has to be reasonably certain that the higher price he advertises does not appreciably exceed the price at which substantial sales of the article are being made in the area.

With respect to advertising retail prices which have been established or suggested by manufacturers, the FTC says if a reduction from the manufacturer’s list price or suggested retail price is advertised, the consumer may be misled into thinking they are getting a genuine bargain if the advertised price does not correspond to prices at which a substantial number of sales are made. An advertised list price will not be deemed fictitious if it is the price at which substantial sales are made in the advertiser’s trade area in which it does business.

With respect to bargain offers based on the purchase of other merchandise (e.g., “Buy one – Get One Free”), the FTC says a consumer may be deceived if the seller increases his regular price, or decreases the quantity or quality of that article, or attaches other strings to the offer. Whenever such an offer is made, the terms and conditions of the offer have to be made clear at the outset.

d. Guides Against Bait Advertising.

The FTC Guides Against Bait Advertising address an offer to sell a product or service which the advertiser in truth does not intend nor want to sell. “No advertisement containing an offer to sell a product should be published when the offer is not a bona fide effort to sell the

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290 16 C.F.R. §251(e).
291 16 C.F.R. §251(h).
293 16 C.F.R. § 233.1.
294 16 C.F.R. §233.2.
295 16 C.F.R. §233.3.
296 16 C.F.R. §233.4.
297 16 C.F.R. Part 238.
advertised product.\textsuperscript{298} The advertiser should not discourage the purchase of the advertised merchandise as part of a bait scheme to sell other merchandise. Exemptions of prohibited practices include disparaging the advertised product or not having a sufficient number of products on hand to meet reasonably anticipated demands (unless the advertisement discloses the supply is limited).\textsuperscript{299} The FTC also prohibits an advertiser from "unselling" with the intent and purpose of selling other merchandise instead of the advertised product. One example is accepting a deposit for the advertised product, then switching the purchasers to a higher-price product.\textsuperscript{300}

e. \textbf{Guides for the Use of Endorsements and Testimonials in Advertising.}

The FTC Guides Concerning The Use of Endorsements and Testimonials in Advertising were revised in 2009.\textsuperscript{301} This Guide represents an administrative interpretation of laws enforced by the FTC. An endorsement means any advertising message that consumers are likely to believe reflects the opinions, beliefs, findings or experiences of a party other than the advertiser.\textsuperscript{302}

Endorsements have to reflect the honest opinions, findings, beliefs or experience of the endorser. The endorsement need not be phrased in the exact words of the endorser, unless the advertisement says that it does. An advertiser can use an endorsement of an expert or celebrity only so long as the endorser continues to subscribe to the views presented. The advertiser must periodically secure the endorser's views by providing current information on the product, service, company or industry. If the advertisement represents that the endorser uses the product, the endorser must have been a bona fide user of it at the time the endorsement was given. The advertiser can run the advertisement only for so long as endorser remains a bona fide user of the product. Endorsers can be liable for statements made in the course of their endorsements.\textsuperscript{303}

Consumer endorsements are not competent and reliable scientific evidence. The advertiser using a consumer endorsement must have adequate substantiation, including competent and reliable scientific evidence, to support claims made through consumer endorsement in the same manner as it would have to do if it had made the representation directly. Advertisements purporting to show actual consumers should utilize actual consumers in both the audio and video, or clearly and conspicuously disclose that those persons are not actual consumers of the advertised product.\textsuperscript{304}

If an advertisement represents that the endorser is an expert with respect to the endorsement message, the endorser's qualifications must in fact give the endorser the expertise that he or she is represented as having. The endorsement must be supported by an actual exercise of that expertise in evaluating product features or characteristics with respect to which

\begin{footnotesize}
\begin{itemize}
\item[298] 16 C.F.R. §238.1.
\item[299] 16 C.F.R. §238.3.
\item[300] 16 C.F.R. §238.4.
\item[301] 16 C.F.R. Part 255.
\item[302] 16 C.F.R. §255.0(b).
\item[303] 16 C.F.R. §255.1.
\item[304] 16 C.F.R. §255.2.
\end{itemize}
\end{footnotesize}
he or she is an expert, and which are relevant to an ordinary consumer’s use or experience with
the product and are available to the ordinary consumer.305

Where an organization is the endorser, that endorsement must be reached by a process
sufficient to ensure that it fairly reflects the collective judgment of the organization. If the
organization claims to be an expert, it must use experts suitable for judging the relevant merits
of the products.306

Finally, when there is a connection between the endorser and the seller that might affect
the weight or credibility of the endorsement, that connection has to be fully disclosed. For
example, if the endorser is not an expert or well known, the advertiser should clearly and
conspicuously disclose either the payment or promise of compensation prior to and in exchange
for the endorsement or that some benefit would be given for the endorsement.307

f. Advising the Client

Lawyers are sometimes asked by their franchise clients to review advertisements, often
at the last minute when the advertisement is about to be printed or used. An understanding of
the various FTC interpretations regarding common business practices is essential to an
effective review of those advertisements.

3. Usury Laws

a. Introduction / General Description of Elements

Usury is the exaction of a greater sum for the use of money than the highest rate of
interest allowed by law. For a franchise system, issues of usury can occur both between the
franchisor and its franchisees and between system outlets and their customers. For example,
interest may be charged on late payments of initial fee installments, royalties or goods or
services acquired from the franchisor or its franchisees, and also on loans to enable a
franchisee to build out its facilities. While almost entirely a function of state law, the following
highlights issues the authors believe to be of particular concern to a franchise system, but is not
an attempt at an examination of the usury laws of all 50 states. Further, since statutes are
amended and repealed from time to time, this section does not purport to be authoritative as to
the existing statutory law of any state, and in cases involving the question of usury in a
particular state, counsel should always make sure to review the current statutes of the
jurisdiction in question.

Determining whether issues of usury need to be considered begins with an analysis of
whether there is (i) a loan or forbearance of money, (ii) an understanding that the principal is
absolutely repayable, (iii) the charging of a greater profit than allowed by law by the party
making the loan or agreeing to the forbearance (the lender), and (iv) an intention to violate the
law.308

305 16 C.F.R. §255.3.
306 16 C.F.R. §255.4.
307 16 C.F.R. §255.5.
(applying Kentucky law); Fogie v. THORN Americas, Inc., 95 F.3d 645 (8th Cir. 1996) (applying Minnesota law); Party
Yards, Inc. v. Templeton, 751 So. 2d 121 (Fla. Dist. Ct. App. 5th Dist. 2000); Mallard v. Forest Heights Water Works,
(1991); Jansen v. Nu-West, Inc., 102 Wash. App. 432, 6 P.3d 98 (Div. 3 2000), as amended on reconsideration,
usurious, franchise counsel are advised to determine the specific elements applicable in the jurisdiction in question, and in particular to determine if the subject transaction can avoid usury based on exceptions available in such jurisdiction. This exploration entails determining whether a choice of law provision will be enforceable or whether some other jurisdiction will be the likely supplier of the limitations on interest.

b. Choice of Law

In most jurisdictions, a provision in a contract for the payment of interest will be found to be valid if the stated rate is permitted by the law of the place of contracting, or of the place of performance, or any other place with which the contract has a substantial relation.309

Parties to a lending transaction may, and often do, however, agree that the law of a particular state will control. So long as the chosen state bears a reasonable relation to the transaction, and so long as the chosen state's usury laws are not contrary to the public policy of the state in which litigation regarding the contract is brought, then the chosen state's laws should govern.310 When the parties have expressly designated in their contract the governing law, the only question for the court is whether they acted in good faith or bad faith for the purpose of evading the law of the place to which their contract is really referable.311 So long as the chosen jurisdiction has a real and vital, and not merely fictitious, connection with the transaction, the court should enforce the choice of law provision.312

The public policy exception, however, can be construed broadly to overrule the parties' contracted choice of law.313 In State ex rel. Meierhenry v. Spiegel314 the South Dakota Supreme Court held that the public policy of protecting South Dakota citizens overruled the choice of law provision agreed to by the parties to a revolving credit facility. Spiegel, Inc., a Delaware corporation with its principal place of business in Oak Brook, Illinois, maintained no office, officers, employees, agents, stores, property or warehouses in South Dakota, and took (Cont'd)

(Sept. 21, 2000). Note that "intention" is often achieved by intending to charge the rate of interest which is in excess of that permitted by law. See Miller v. Colortyme, 518 N.W.2d 544, 550 (Minn. 1994) (stating "To be guilty of violating the usury law, a lender need only intend to charge a rate that is in fact usurious").

309 Blackford v. Commercial Credit Corp., 263 F.2d 97 (5th Cir. 1959) (applying Maryland law); Binghamton Trust Co. v. Auten, 68 Ark. 299, 57 S.W. 1105 (1900).


311 Id. at § 15 (citing Albrighton v. General Finance Corp., 204 F.2d 125 (5th Cir. 1953) (applying Mississippi law); Bella Isla Const. Corp. v. Trust Mortg. Corp., 347 So. 2d 649 (Fla. Dist. Ct. App. 3d Dist. 1977); and Big Four Mills v. Commercial Credit Co., 307 Ky. 612, 211 S.W.2d 831 (1948)). See also, 16 A.L.R. 4th 967 at [*8(b)] (citing Armstrong v. Alliance Trust Co., 88 F.2d 449 (5th Cir., 1937) (applying Mississippi law) (holding that the stipulation of the parties should control unless forbidden by statute or public policy, and so long as not done for the purpose of evading a usury law). But see, Plitt v. Seven Corners Realty, 149 F.2d 832 (App. D.C. 1945); West Side Motor Exp., Inc. v. Finance Discount Corp., 340 Mass. 669, 165 N.E.2d 903 (1960) (holding that the place of making the contract is controlling).

312 16 A.L.R. 4th 967 at [*8(b)] (citing Andrews v. Pond, 38 U.S. 65, 10 L. Ed. 61, 1839 WL 4292 (1839); United States Savings & Loan Co. v. Beckley, 137 Ala. 119, 33 So. 934 (1903); Green v. Northwestern Trust Co., 128 Minn. 30, 150 N.W. 229 (1914); and Shannon v. Georgia State Building & Loan Ass'n, 78 Miss. 955, 30 So. 51 (1901)). See also 16 A.L.R. 4th 967 at [*2] and [*8a] (citing Jones v. Tindall, 216 Ark. 431, 226 S.W.2d 44 (1950), in which the court upheld a choice of law provision which was neither the jurisdiction in which the contract was made nor the jurisdiction in which it was performed where a party claiming usury as a defense and the contracted choice of law was the state in which the borrower and the property pledged as collateral was located).


314 Id. at 301.
no security interests in property sold to residents of South Dakota. It did, however, solicit sales in the state through mail order catalogues. The catalogues contained credit application forms for credit accounts and credit agreement forms for ordering merchandise, which agreements would be signed by South Dakota customers and mailed to Illinois for acceptance, at which point credit would be extended. The terms of the revolving credit arrangement included the payment of interest at the rate of 1.65% per month, which is an annual percentage rate of 19.8%. This amount was permitted under applicable Illinois law, but exceeded the 12% interest rate limitation applicable under South Dakota law. In ruling in favor of the borrower, the South Dakota Supreme Court articulates that the public policy concerns of the state's legislature in passing its usury laws is to "protect the general welfare of South Dakota citizens by preventing the exaction of excessive rates of interest in revolving charge account agreements." This policy is circumvented if foreign businesses can conduct business with residents of the state and extract interest at rates higher than those permitted by the legislature.

Thus, a franchisor's counsel should attempt to establish as much connection with the desired jurisdiction as possible and should insist on all agreements being executed in the jurisdiction being agreed to by the loan parties. As long as the chosen jurisdiction bears some relation to the transaction, the franchisor should avoid most (but not all) of the ambiguity associated with a franchise system's potential usurious arrangements.

With respect to the potential usurious consumer arrangements between a system outlet and its customers, however, the choice of law question may pose a more complicated endeavor. For instance, a franchise system whose franchisor is headquartered in Illinois is likely to provide its franchisees with form customer contracts based on Illinois law, but a franchisee based in South Dakota and performing services in South Dakota to a resident of South Dakota, is likely to have difficulty enforcing a lending arrangement designed to avoid the Illinois usury laws simply by providing for Illinois law to govern. A South Dakota court would, in this case, likely not enforce that provision, instead interpreting the arrangement under South Dakota's usury law.

In summary, the available jurisdictions likely to be enforced are (i) parties' choice, (ii) situs of where agreement is made and (iii) situs of where agreement is performed. Once these possible locations are determined, franchise counsel can determine if one or more of the above choices provides more liberal interest rate limitations (i.e., higher caps or more exceptions to the usury defenses) than the others. If available, counsel may want to review Section 3.17 of the applicable state's Law Digest published by Martindale-Hubbell, which provides a useful summary of the state's usury laws.

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315 Id. at 299.
316 Id.
317 Id.
318 Id. at 301.
319 Id.
320 So that in addition to the parties agreeing on choice of law, the contract can be shown to have been made in the desired jurisdiction.
321 The chosen jurisdiction would still need to pass the public policy standard of a particular competing jurisdiction.
322 See notes 310 and 313-319, supra.
323 See Spiegel, supra at note 66.
324 One issue that does not appear to be addressed by the cases reviewed for this paper is the choice of law bearing any relationship to the ease of administration when the lender (i.e., franchisor) is preparing form agreements for application in multiple jurisdictions and any public policy implications of a franchisor treating system franchisees similarly.
c. **Laws limiting effect of usury defense based on type of loan (i.e., loans to corporations; business loans)**

A few states do not impose maximum interest rates. Many jurisdictions impose interest limitations only on loans related to personal, family or household purposes. Others provide higher interest rate limits on loans not related to such personal, family or household purposes. Still others provide that no corporation or similar business entity can bring a usury defense against the payment of interest on a loan, or that there is no maximum rate of interest applicable to loans to corporations or similar business entities. There are even states that eliminate interest rate caps if the principal amount being loaned exceeds a certain threshold. It should be noted, however, that a number of states also have criminal usury statutes that could apply to a business loan, loan to a corporation or other loan that is exempted from civil usury provisions.

d. **Laws limiting effect of usury defense for time-price differential**

In addition to applying a choice of law with usury limitations, it might be advantageous for certain franchise systems to base financing arrangements on the laws of a jurisdiction offering no interest rate cap when the transaction involves a time-price differential. The "time-

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324 See, e.g., Nevada (any interest rate agreed to by the parties in writing); New Hampshire; New Mexico (any interest rate agreed to by the parties in writing); South Dakota; and Washington (if parties agree in writing).
325 See, e.g., Connecticut (if in excess of $10,000); District of Columbia; Illinois (no limit on loans between merchandise wholesaler and retailer); Indiana; Iowa; Kansas; Louisiana; Maryland (if in excess of $15,000 and not secured by residential real property, or $75,000 if secured by residential real property); Nebraska; North Carolina; Ohio; Pennsylvania (if in excess of $10,000); Rhode Island; South Carolina; Virginia (if in excess of $5,000); and West Virginia (if in excess of $20,000).
326 See, e.g., California (higher of 10% per annum or 5% above prior month's discount rate at the San Francisco Federal Reserve Bank, which is currently at .75%); Mississippi (higher of 15% or 5% above discount rate on 90-day note at Federal Reserve Bank); and Texas (generally, 28%).
327 See, e.g., Delaware; Illinois; Kansas; Maryland; Michigan (corporations cannot bring usury if agreement on higher interest is made in writing; non-bank lender can lend to "business entities" at rate not in excess of 25%); Minnesota; Missouri; Nebraska; New Jersey; New Mexico; New York (civil usury cannot be plead as defense, but criminal usury can be used as defense); North Carolina; North Dakota; Pennsylvania; Texas; Virginia; and West Virginia.
328 See, e.g., Alabama (any interest agreed to in writing if principal is over $2,000); Alaska (any interest agreed to in writing if principal is over $25,000); Arizona (any interest agreed to in writing if principal is over $1,000); Georgia (generally, any interest agreed to in writing if principal is over $250,000, though specific statutes may impose other limits); Kentucky (any interest agreed to in writing if principal is over $15,000; Minnesota (any interest agreed to in writing if principal is over $100,000); Mississippi (if principal is over $5,000); Nebraska (any interest agreed to in writing if principal is over $25,000); New Jersey (no civil rate of maximum interest rate applicable to loans over $50,000 not secured by first lien on real property containing 6 or fewer units, but criminal rate prohibits loans in excess of 30% per annum or, in the case of corporations, 50% per annum); North Carolina (any interest agreed to in writing if principal is over $25,000); North Dakota (any interest agreed to if principal is over $35,000); Ohio (any interest agreed to in writing if principal is over $100,000); Pennsylvania (if secured and principal is over $50,000, if unsecured and principal is over $35,000); Rhode Island (if principal is over $1,000,000 and not secured by principal residence); and Wisconsin (if principal is over $150,000 and not secured by debtor's principal residence).
329 See, e.g., New Jersey (no loan over 30% per annum or 50% in the case of corporations); and Pennsylvania (over 25% is a racketeering activity).
330 See Servpro Industries, Inc. v. Pizzillo, 2001 Tenn. App. LEXIS 87 (Tenn. App., 2001); Munson v. White et al., 217 S.W.2d 641 (Ky. App., 1949); Gilbert Schauman and Another v. Solmica Midwest Inc. and Another, 168 N.W.2d 667 (Minn., 1969). But see St. Paul Bank For Cooperatives v. Ohman, 402 N.W.2d 235 (Minn. App., 1987) (trying to distinguish between situations in which there is a "cash" price and a "time" price, and therefore a time-price differential exists that is not subject to usury, and situations in which there is only a "cash" price and therefore a loan of money in exchange for interest subject to usury limitation). In Ohman, the court reasoned that when there is a
price differential” means the difference between the amount charged on a sale of property or services for cash and the amount charged if payments are deferred or made in installments. In *Servpro Industries*, the franchisor provided financing for a portion of the initial fee due under the franchise agreement. That financing provided for interest on the financed initial fees at 13.5%, an amount which exceeded the Tennessee usury rate of 10%. In ruling in favor of the respondent, Servpro Industries, the court held that the financed portion of the initial fee was not the borrowing of money, as alleged by the appellant, franchisee, but rather his purchase of both tangible and intangible property. These facts, the court reasoned, fit squarely within the time-price differential exception to usury found in the Tennessee Code, which provides that any time-price differential (i.e., any excess charged for the deferred payment of purchase price for goods or services) is not “interest” subject to usury.

However, it should be noted that most courts applying a time-price differential require there to be two prices set forth in the contract, a “cash” price and a “time” price. The authors cannot discern how, given the overwhelming preference for requiring two prices to be given, the court in *Servpro International* concluded the agreement on the part of the franchisor to defer payment of the established “cash” price of the initial fee constituted a time-price differential transaction.

e. **Enforceability of Usury Savings Clauses**

Because an element of usury generally includes an intent to charge a rate of interest above the maximum rate permitted by law, many loan documents incorporate a usury savings clause such as “interest at lower of ___% or highest rate permitted by applicable law” in order to document that the parties to the transaction did not intend to charge a usurious rate. While such provisions appear to be generally enforceable, courts do not universally accept them, especially in cases in which evidence exists on the face of the document to indicate a usurious intent. In North Carolina, the state Supreme Court has ruled it against public policy to give effect to a usury savings clause in that its existence impermissibly shifts the burden of knowing when a rate of interest is usurious from the lender (the party whose business should require it have this knowledge) to the borrower. The Court in *Swindell* stated:

The [North Carolina usury] statute relieves the borrower of the necessity for expertise and vigilance regarding the legality of rates he must pay. That onus is placed instead on the lender, whose business it is to lend money for profit and who is thus in a

(Cont’d)
contract binding the seller to sell the goods or services at the "cash" price, then there cannot be a "cash" price and a "time" price, but only a "cash" price. *Id.* at 238.

332 *Id.* at *2.
333 *Id.* at *14 (citing TENN. CODE ANN. §47-14-120).
334 *See* Ohman, 402 N.W.2d 235, discussed at note 330, *supra*; and 14 A.L.R. 3d 1065 at [*4].
335 *See* note 308, *supra*.
336 *See* Kennon v. McGraw, 281 S.W.3d 648, 652 (Tex. App. – Eastland, 2009) (*stating* “Savings clauses are favored by the law and will be given effect if reasonably possible”) (internal citation omitted).
337 *Id.* (citing Nevels v. Harris, 102 S.W.2d 1046, 1050 (Tex. 1937) for the proposition that “[a] party may not, however, escape penalty by disclaiming the intention to do what was clearly done”). *And see*, Countrywide Funding v. Kapinos, 1993 Conn. Super. LEXIS 844, *5 - 7* (finding that under Connecticut law, a savings clause cannot be said to avoid a usurious intent when the lender’s actions in demanding payment of a usurious interest rate shows the requisite intent).
better position than the borrower to know the law. A usury savings clause, if valid, would shift the onus back onto the borrower, contravening statutory policy and depriving the borrower of the benefit of the statute's protection and penalties...A lender cannot charge usurious rates with impunity by making that rate conditional upon its legality and relying upon the illegal rate's automatic rescission when discovered and challenged by the borrower.339

This rationale may play a role in rulings in Texas, where courts have upheld savings clauses most often when the usurious interest arises from a contingency (e.g., upon a default), rather than the standard rate of interest called for under the terms of the loan.340 Thus, a savings clause is a useful provision to prevent a default rate of interest or other contingent financing charge from causing the total cost of borrowing the loaned principal to be usurious, but such a provision will not always save a loan’s standard rate of interest from being usurious.

f. Effect on franchisee/consumer relationship

While a franchisor is likely to always be able to rely on the relationship between it and its franchisee-borrowers being a loan for non-personal purposes and thus excluded from maximum interest rates in many jurisdictions, an operating outlet that provides financing to the general public may not, depending on the franchise concept, be so fortunate. In addition to state usury laws, an outlet will also need to be aware of and, if applicable, compliant with certain federal laws affecting the consumer credit relationship, such as the Truth in Lending Act341 and Consumer Leasing Act.342 Both of these federal laws involve the disclosure to the consumer of the cost of financing being offered to them.343 It is important to recognize that these Acts apply to the extension of consumer credit and do not apply to commercial lending arrangements.344

Details of the requirements of the Truth in Lending Act and the Consumer Leasing Act are beyond the scope of this paper, but in summary, both Acts are disclosure laws as opposed to regulatory laws that impose disclosure requirements over four general areas of a lending relationship: credit transactions, credit advertising, credit billing, and consumer leases.345 But

339 Id. at 896 (internal quotations and citations omitted).
340 See Parhms v. B & B Ventures, 938 S.W.2d 199, 204 (Tex. App. – Houston, 1997) ("However, a savings clause may cure an open-ended contingency provision, the operation of which may or may not result in a charge of usurious interest") (citing First State Bank v. Dorst, 843 S.W.2d 790, 793 (Tex. App. – Austin, 1992).
341 15 USC § 1601 et seq.
342 15 USC § 1667 et seq.
343 See 15 U.S.C. § 1605(a) (requiring the disclosure of all finance charges) and 15 U.S.C. § 1667(a)(9) (requiring the disclosure of the number, amount and due dates or periods of payments under covered consumer leases).
345 See generally, 15 USC §§1631 – 1667f; Turner v. GMAC, 180 F.3d 451, 454 (2nd Cir. 1999) (citing Johnson v. McCrackin-Sturman Ford, Inc., 527 F.2d 257, 262 (3rd Cir. 1975) when describing how the Consumer Leasing Act extended the Truth in Lending Act’s credit disclosure requirements and noting that “TILA provides for full disclosure of credit terms rather than regulation of the terms or conditions under which credit may be extended”) (internal quotations omitted).
these disclosure rules only apply to the extension of consumer credit\textsuperscript{346} by a creditor who regularly extends consumer credit payable in more than four installments.\textsuperscript{347}

When applicable, the main disclosures required include a statement of the “finance charges” and the “annual percentage rate” applicable to the extension of credit. If disclosure is not conspicuously made, the debtor can rescind the contract. However, it may be important to note that the Truth in Lending Act does not provide a cause of action when the lender engages in “bait and switch” techniques but only requires that the lender make certain disclosures with respect to the offered terms.\textsuperscript{348} Furthermore, the practice of “spot delivery” does not violate the Act.\textsuperscript{349}

g. Effect of finding usury applicable

Usury is used as a defense by a debtor to the payments owed under the loan. The successful use of usury as a defense usually results, at a minimum, in the loss of the usurious portion of interest charged.\textsuperscript{350} In other jurisdictions, the result will be a total loss of ability to collect any unpaid interest due on the loan and the treatment of the already paid amounts as principal payments.\textsuperscript{351} However, in a handful of other jurisdictions, a finding of usury can, depending on the severity of abuse, result in the loss of the principal amounts loaned in addition to interest.\textsuperscript{352} The justification for this severe result is punitive — if a lender’s only risk for charging a usurious rate of interest is merely the loss of that portion of the interest that was usurious, a lender has little incentive to attempt to get away with making the usurious loan. Of course, a competing argument (as should be evident in the wide variety of state laws one must consider in drafting to avoid claims of usury) would be that a lender may have made a usurious loan simply because of where that loan ended up being enforced and in such an event, the lender should not be punished by a loss of its entire principal.

4. Membership Agreements

As a result of high levels of consumer complaints related to membership agreements within certain industries, many states have enacted legislation that requires specific disclosures, specific cancellation and refund rights, and have other prohibitions related to how such

\textsuperscript{346} See note 344 \textit{supra}.

\textsuperscript{347} 15 U.S.C. §1602(f); and see 12 C.F.R. §226.2(a)(17)(v) (“A person regularly extends consumer credit only if it extended credit (other than credit subject to the requirements of § 226.32) more than 25 times (or more than 5 times for transactions secured by a dwelling) in the preceding calendar year.”).

\textsuperscript{348} See 17 Am. Jur. 2d \textit{Consumer and Borrower Protection} §15 fn 5 (\textit{citing} Clark v. Troy and Nichols, Inc., 864 F.2d 1261 (5th Cir. 1989)).

\textsuperscript{349} See \textit{id.} at fn. 6. “Spot Delivery involves: (1) an automobile dealer entering into a sales contract with a consumer at a low interest rate when the dealer knows the consumer will not qualify for that rate; (2) the dealer giving the consumer possession of the car and accepting the consumer’s trade-in; and (3) the dealer notifying the consumer that his financing has been denied and that he must enter into a new contract at a higher rate, which the consumer will do because he no longer has his trade-in and because he has become attached to his new car.” \textit{Id. (citing Janikowski v. Lynch Ford, Inc., 210 F.3d 765 (7th Cir. 2000)).}

\textsuperscript{350} See, e.g., Missouri

\textsuperscript{351} See, e.g., Alabama, Arizona, Ohio, Pennsylvania.

\textsuperscript{352} See, e.g., District of Columbia (25% of principal paid is forfeited if usurious interest charged on “small” loans); Mississippi (if more than 100% in excess of maximum rate, then any amount paid, principal or interest, may be recovered by debtor); New York (neither principal nor interest can be recovered in a usurious loan); North Dakota (can recover interest and 25% of principal paid, or double interest and 25% of principal paid if action brought within 4 years of date of transaction); and Texas (on consumer loans: treble amount of excessive interest or $2,000 or 20% of principal, whichever is greater; on commercial loans: treble excessive interest; if more than double maximum rate, then lender forfeits all interest and principal).
agreements can be entered into or enforced.\textsuperscript{353} For instance, in Illinois under the Physical Fitness Services Act, contracts for physical fitness services are cancelable by the customer within three (3) business days after the business day on which it is signed with a full refund; are cancelable if the customer moves more than twenty-five (25) miles from the fitness center and no comparable center is made available by the original center with a partial refund (equal to the portion of the membership fee allocable to the time prior to the move less a reasonable cancellation fee not in excess of 10% of the unused balance or $50, which ever is less); and are cancelable upon the death or disability of the customer, with a partial refund (equal to the portion of the membership fee allocable to the time prior to death or disability).\textsuperscript{354} Illinois also prohibits physical fitness service contracts with individuals to exceed a payment of more than $2,500 a year; to require payments in excess of three (3) years from the date the contract is entered into; to have a term in excess of two (2) years (which may be renewable at the option of the customer each year); or to require the customer to sign any negotiable instrument which, when negotiated by the fitness center, would eliminate rights or defenses to payment the customer would otherwise have against the fitness center.\textsuperscript{355}

In New York, a contract for health club services is cancelable by the consumer within three (3) days with a full refund; is cancelable by the consumer's estate if the consumer dies; and is cancelable by the consumer if he or she moves more than twenty-five (25) miles from the health club or becomes physically disabled for more than six (6) months.\textsuperscript{356} New York requires that refunds be given in the event of a cancellation for death, disability or relocation in amounts equal to the price paid by the consumer, less an amount retained by the health club for its incurred expenses and the portion of the total price representing the services used by the consumer (up to the total contract price).\textsuperscript{357}

Of apparent particular concern to these states are contracts for memberships to fitness centers that are not yet open for business.\textsuperscript{358} New York,\textsuperscript{359} Missouri\textsuperscript{360} and Illinois\textsuperscript{361} each require membership fees paid prior to a fitness center's opening be placed in escrow, and Illinois gives consumers seven (7) days after signing to cancel a contract for a fitness center not yet opened.\textsuperscript{362} New Jersey protects consumers by granting them the right to cancel the contract


\textsuperscript{354} 815 ILCS 645/6.

\textsuperscript{355} 815 ILCS 645/8. Illinois also has a Physical Fitness Facility Medical Emergency Preparedness Act. See 210 ILCS 74/1 et seq.

\textsuperscript{356} NY CLS GEN BUS § 624.

\textsuperscript{357} Id.

\textsuperscript{358} See C. Koster, note 353, supra. – Caution: This listing may not be exhaustive. Check the law of the applicable jurisdiction.

\textsuperscript{359} NY CLS GEN BUS § 622.

\textsuperscript{360} R.S.Mo. § 407.329.

\textsuperscript{361} 815 ILCS 645/13.

\textsuperscript{362} 815 ILCS 645/6; and see 815 ILCS 645/7 (providing that if a fitness center is under construction, the contract shall provide that in the event the facility or services contracted for are not available within the earlier of one year from the date of the contract or three (3) months from the date specified in the contract, then the contract can be cancelled by the consumer with a full refund).
and receive a full refund if the fitness center is not yet open when the contract is signed, but the fitness center can set the cut off date for this right in the body of the contract.  

Notice of the applicable cancellation and other rights are typically required to be conspicuously stated in the contract. Consumers are typically given a private right of action to recover damages, and State Attorneys General are empowered to seek civil penalties.

5. **Consumer Protection Statutes**

Many states have unfair business practices laws to protect consumers. For example, in Washington, the Unfair Business Practices--Consumer Protection Act prohibits unfair or deceptive acts or practices in conduct of any trade or commerce. Violations can result in civil penalties, injunctive orders and treble damage actions including liability for costs and attorney fees. In addition to this general prohibition, Washington supplements the Unfair Business Practices--Consumer Protection Act with statutes specifying particular acts or practices that are unfair or deceptive and thus subject to remedies provided by the general Act. Interestingly, Washington's law requires an analysis of whether the alleged deceptive practice is injurious to the public interest, and without this public interest, no violation occurs.

Likewise, Illinois' Consumer Fraud and Deceptive Business Practices Act establishes a general prohibition on deceptive business practices and then references violations of that act as penalties for violations of other specific consumer focused laws. Generally, unfair or deceptive acts include deception, fraud, misrepresentation, concealment, suppression or omission of material fact in the conduct of a trade or business with the intent that another relies on that act. Specific areas of regulation include pyramid schemes, the sale of insurance or securities, installment sales, and the advertising related to "going out of business" sales, bankruptcy sales, claims of the availability of purchasing over time, coupon sales, advertising factory authorized services, gasoline prices, sale of franchises, eye exams and glasses, free prizes, gifts and gratuities, insurance, and advertising sales and use.

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363 N.J. STAT. § 56:8-42(j).
364 Id.; and see 815 ILCS 645/4; R.S.Mo. § 407.330; and N.J. STAT. § 56:8-42.
365 815 ILCS 645/11 (treble damages and attorneys’ fees); and NY CLS Gen Bus § 628 (treble damages and attorneys’ fees).
366 815 ILCS 645/12 (referencing enforcement authority and penalties of up to $50,000 per violation, as set forth in 815 ILCS 505/7); and NY GEN BUS § 629 ($2,500 per violation).
367 REV. CODE WASH. § 19.86.020.
368 REV. CODE WASH. § 19.86.090 (treble damages cannot exceed $10,000).
369 For example, pyramid schemes are specifically prohibited (REV. CODE WASH. § 19.275.030), as are violations of the rules established for charitable solicitations (REV. CODE WASH. § 19.09.340), collection agencies (REV. CODE WASH. § 19.16.440) and auto repair work (REV. CODE WASH. § 46.71.070).
370 REV. CODE WASH. § 19.86.920.
371 815 ILCS 505/2.
372 815 ILCS 505/2A.
373 815 ILCS 505/2B(f).
374 815 ILCS 505/2G.
375 815 ILCS 350/3.
376 815 ILCS 350/7.
377 815 ILCS 505/2J.
378 815 ILCS 505/2J.1.
379 815 ILCS 505/2M.
380 720 ILCS 305/1 – 305/2.
381 815 ILCS 705/30.
382 815 ILCS 355/1.
tax discounts. 385 In addition, any violation of Section 2 of the Uniform Deceptive Trade Practices Act 386 or a laundry list of other acts 387 is a violation of the Consumer Fraud and Deceptive Business Practices Act. Violations can result in civil penalties of up to $50,000 per violation. 388 In addition, the consumer has a civil action for violation of the Consumer Fraud and Deceptive Business Practices Act. 389

Many jurisdictions have similar laws and the lawyer should check the law of the applicable jurisdiction. A full discussion of this topic is beyond the scope of this paper. 390

6. Consumer Product Safety Act

The Consumer Product Safety Commission ("CPSC") regulates consumer product safety under the Consumer Product Safety Act ("CPSA") 391 and four transferred acts: the Federal Hazardous Substances Act, the Poison Prevention Packaging Act of 1970, the Flammable Fabric Act and the Refrigerator Safety Act. 392 The CPSC can promulgate regulations establishing consumer product safety standards and banned hazardous products 393 or requirements or standards under one of the transferred acts. 394 The Consumer Product Safety Improvement Act of 2008 expanded the CPSC's enforcement authority and mandated new testing and certification requirements for many consumer products. 395

The CPSA defines “consumer product” as follows:

The term “consumer product” means any article, or component part thereof, produced or distributed (i) for sale to a consumer for use in or around a permanent or temporary household or residence, a school, in recreation, or otherwise, or (ii) for the personal use, consumption or enjoyment of a consumer in or around a permanent or temporary household or residence, a school, in recreation, or otherwise, but such term does not include —

(A) any article which is not customarily produced or distributed for sale to, or use or consumption by, or enjoyment of, a consumer.

(Cont’d)

383 815 ILCS 505/2P.
385 35 ILCS 105/7.
386 815 ILCS 505/2. The UDTP Act is found at 815 ILCS 10/1 et seq.
387 815 ILCS 505/2Z.
388 815 ILCS 505/7.
389 815 ILCS 505/10a. See Gaebler v. New Mexico Potash Corp., 676 N.E.2d 228, 1995 WL 17164658 at *12 (Ill. App. 1995) (the act broadly proscribes a broad range of “unfair” or “deceptive” practices which threaten harm to consumers).
390 Workshop W6 addresses “Claims Under the ‘Little FTC Acts’.”
393 See 16 C.F.R. § 1101-1420.
394 See 16 C.F.R. § 1500-1750.
A number of items are excluded from the definition, such as motor vehicles, boats, aircraft, drugs, cosmetics and good.

While the CPSC has promulgated a number of consumer product safety standards over the years, its primary enforcement tool has been the so-called Section 15(b) substantial product hazard reporting requirements. Sections 15(a) and (b) of the CPSA provide:

(a) For purposes of this section, the term “substantial product hazard” means —

(1) a failure to comply with an applicable consumer product safety rule under this Act or a similar rule, regulation, standard, or ban under any other Act enforced by the Commission which creates a substantial risk of injury to the public, or

(2) a product defect which (because of the pattern of defect, the number of defective products distributed in commerce, the severity of the risk, or otherwise) creates a substantial risk of injury to the public.

(b) Every manufacturer of a consumer product, or other product or substance over which the Commission has jurisdiction under any other Act enforced by the Commission (other than motor vehicle equipment as defined in section 30102(a)(7) of title 49, United States Code), distributed in commerce, and every distributor and retailer of such product, who obtains information which reasonably supports the conclusion that such product—

(1) fails to comply with an applicable consumer product safety rule or with a voluntary consumer product safety standard upon which the Commission has relied under section 9 [15 U.S.C. § 2058];

(2) fails to comply with any other rule, regulation, standard, or ban under this Act or any other Act enforced by the Commission;

(3) contains a defect which could create a substantial product hazard described in subsection (a)(2); or

(4) creates an unreasonable risk of serious injury or death,

[Other exclusions omitted]396

shall immediately inform the commission of such failure to comply, of such defect, or of such risk, unless such manufacturer, distributor, or retailer has actual knowledge that the Commission has been adequately informed of such defect, failure to comply, or such risk. A report provided under paragraph (2) may not be used as the basis for criminal prosecution of the reporting person under section 5 of the Federal Hazardous Substances Act (15 U.S.C. 1264), except for offenses which require a showing of intent to defraud or mislead.  

Section 37 of the CPSA also requires manufacturers and importers to report certain information on civil actions involving consumer products.  

Companies that manufacture, import, distribute or sell consumer products have an obligation under Section 15(b) to report substantial product hazards to the CPSC under strict time constraints. The Sections 15(b) and 37 reporting obligations apply to products regulated under the CPSC and under the four transferred acts. The failure to report in a timely fashion can result in substantial civil and criminal penalties. A knowing violation can result in civil penalties not to exceed $100,000 for each violation, including a failure to furnish information required by Section 15(b) or information required by Section 37, which is a separate offense with respect to each consumer product involved, except that the maximum civil penalty cannot exceed $15 million for any related series of violations. 

The CPSA requirements can affect both franchisors and franchisees involved in the sale or distribution of consumer products or one of the products covered by one of the four transferred acts. The CPSC reporting requirements are spelled out in great detail in the Substantial Product Hazard Reports rule. We will provide a brief overview of those reporting requirements.

Rule 1115.2(b) emphasizes that every manufacturer (including an importer), distributor and retailer of a consumer product who obtains information which reasonably supports the conclusion that product fails to comply with a consumer product safety rule, a voluntary consumer product safety standard, or contains a defect which could create a substantial product hazard or creates an unreasonable risk of serious injury or death, to “immediately” inform the CPSC, unless the party has actual knowledge that the CPSC has been informed of the failure to comply, defect or risk.

The obligation to report arises upon receipt of information from which one could reasonably conclude the existence of a reportable event. However, a “subject firm” (i.e., the manufacturer, importer, distributor or retailer) can conduct a reasonably expeditions investigation in order to evaluate the reportability of a death or grievous bodily injury or other

\[397\] 15 U.S.C. § 2064(a), (b).
\[399\] 15 C.F.R. Part 1115.
\[400\] 15 C.F.R. § 1115.2(d).
\[402\] 16 C.F.R. Part 1115.
\[403\] 16 C.F.R. §1115.2(b). For Section 37, see 16 C.F.R. § 1115.7. A failure to comply with a standard or regulation issued under one of the transferred acts need not be reported unless the failure to comply could create a substantial product hazard. 16 C.F.R. § 1115.10(b).
\[404\] 16 C.F.R. § 1115.12(a).
information. The investigation and evaluation should not exceed 10 days unless a firm can demonstrate that a longer period is reasonable.\textsuperscript{405} Immediately, within 24 hours after a firm has information that has to be reported, the firm should report.\textsuperscript{406}

The CPSC regulations spell out the reporting obligations. Initial reports can be made orally or by telephone or electronically, but must be confirmed in writing within 48 hours.\textsuperscript{407} A full written report has to be filed if the CPSC staff determines that there may be a substantial product hazard.\textsuperscript{408} Usually the manufacturer or importer will be making the initial report, but the regulations specify reporting obligations on the part of distributors and retailers. A distributor or retailer can satisfy the initial reporting obligations either by telephoning or writing the CPSC’s Office of Compliance and Enforcement, Division of Corrective Actions (“Division”), or by sending a letter describing the noncompliance, defect or risk of injury to the manufacturer (or importer) with a copy to the Division or by forwarding to the Division reportable information received from another firm. A distributor or retailer who receives reportable information from a manufacturer (or importer) must report to the CPSC unless the manufacturer (or importer) informs the distributor or retailer that a report has been made. Unless further information is requested by the staff, this will constitute a sufficient report for the distributor or retailer, both for the initial and full reports.\textsuperscript{409}

When the report is made to the CPSC, the CPSC will determine whether a product recall will be required. In most situations, product recalls are voluntary and negotiated between the CPSC and the manufacturer (or importer). When a report is made, the CPSC staff will make a preliminary determination of the reported hazard and a determination whether there should be a voluntary or involuntary recall. To short cut the process, the CPSC has adopted a “Fast Track Product Recall Program.”\textsuperscript{410} The CPSC Recall Handbook spells out the fast track reporting obligations. When a company reports a potential product defect, it must implement a voluntary recall that is satisfactory to the staff within 20 working days. The recall information will be included in a joint news release from the CPSC and the company, information will have to be posted on the company’s website and sent to consumers, distributors, dealers, sales representatives, retailers and others, there will need to be a toll-free call-in number and point-of-purchase posters, and a variety of other disclosure obligations. The distributors or retailers will have to post the point-of-purchase posters.\textsuperscript{411} The CPSC will continue to monitor the recall until it is satisfied that as many consumers as possible have received the recall notice and had an opportunity to take advantage of the offered remedy. However, the recall notice will stay on the CPSC website for an indeterminate amount of time even after the CPSC closes its investigation.\textsuperscript{410}

In the franchise context, while the franchisor will have the primary reporting and recall obligations, the franchisee’s cooperation will be critical to the success of the recall. To the extent that the franchisor or franchisee maintains detailed customer records and can communicate directly with the affected consumer, the recall is more likely to be a success and can be closed more quickly. Where those kinds of records do not exist, more public notice will be required with the attendant bad publicity for the franchisor and the system. Very few

\begin{itemize}
\item \textsuperscript{405} 16 C.F.R. § 1115.14(d). Weekends and holidays are excluded from the time computations, so 10 days is essentially 10 working days. 16 C.F.R. §1115.14(a).
\item \textsuperscript{406} 16 C.F.R. § 1115.14(e).
\item \textsuperscript{407} 16 C.F.R. § 1115.13(c).
\item \textsuperscript{408} 16 C.F.R. § 1115.13(d).
\item \textsuperscript{409} 16 C.F.R. §§ 1115.13(b), (d).
\item \textsuperscript{410} 62 Fed. Reg. 39827 – 28 (July 24, 1997).
\item \textsuperscript{411} Recall Handbook: www.cpsc.gov/businfo/8002.html.
\end{itemize}
franchise agreements contain provisions requiring franchisees to cooperate in recalls, which can create some difficulty for a franchisor trying to obtain the cooperation of its franchisees in the recall program.

C. General Operational Laws

1. Telemarketing and “Do Not Call” Laws

a. Generally – the Legislative and Regulatory Framework

Telemarketing is a direct sales or direct marketing technique in which a salesperson solicits a prospective purchaser of a product or service via a telephone call. Telemarketing has been utilized by direct marketing companies in the U.S. since the 1960's. As of 2009, approximately $334.3 billion of goods and services were sold through telemarketing efforts. But telemarketing has earned a reputation among consumers, Congress, and government officials as a means to perpetrate fraud and scams on unsuspecting consumers. In addition, telemarketing calls annoy the public, as telemarketers could (and still do) call potential customers at all hours of the day or evening, hang up on calls, and tie-up valuable telephone lines. Telemarketing, and the now well-known “do-not-call” rules (also referred to as “DNC”) are regulated at the federal level by the Federal Communications Commission (“FCC”) and the Federal Trade Commission (“FTC”). The federal rules do not preempt state laws, so many states have laws or regulations governing telemarketing practices and do-not-call lists.

In response to consumer complaints about telemarketing, Congress enacted the Telephone Consumer Protection Act of 1991 ("TCPA"), which prohibited certain telephone solicitations, automated or automatic telephone dialing practices and unsolicited fax advertisements. The TCPA instructed the FCC to adopt and implement rules to protect consumers from these unwanted telephone solicitations, and authorized the FCC to "require the establishment and operation of a single national database to compile a list of telephone numbers of residential subscribers who object to receiving telephone solicitations." In 1992 the FCC adopted rules implementing the TCPA, including do-not-call lists, record keeping regarding consumers’ requests to not receive further solicitations, prohibitions on making telemarketing calls before 8 a.m. or after 9 p.m., and other rules.

Recognizing that the FCC’s TCPA rules were not sufficient to protect consumers, in 1994, Congress passed the 1994 Telemarketing Consumer's Fraud and Abuse Prevention Act ("Telemarketing Act"). The Telemarketing Act directed the FTC to adopt rules prohibiting deceptive and abusive telemarketing acts and practices, and in 1995 the FTC adopted its

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412 Under the FTC’s Telemarketing Sales Rule, 16 C.F.R. § 310 (“TSR”), the definition of “telemarketing” is “a plan, program or campaign which is conducted to induce the purchase of goods or services or a charitable contribution, by use of one or more telephones…” 16 C.F.R. § 310.2 (cc).
417 47 U.S.C. § 227(b)(2) & (c).
original Telemarketing Sales Rule. The original Telemarketing Sales Rule included the DNC rules, and restrictions on telemarketing activities to prevent fraud and abuse, and to minimize the aggravating and annoying calls received by consumers.

The TCPA and the Telemarketing Act did not preempt state law. States' attorneys general may bring civil actions under either law, and states are not precluded from enforcing their own state statutes or laws related to the same conduct as that governed by TCPA or the Telemarketing Act.

The marketplace and telemarketing technology changed in the decade after the implementation of the FCC's TCPA rules and the FTC's original Telemarketing Sales Rule, with significant increases in telemarketing activities and the sale of goods and services via telemarketing. By 2003, telemarketers made over 100 million calls to consumers and businesses each day. In March 2003, Congress enacted the Do-Not-Call Implementation Act, which authorized the FTC to promulgate rules to enable it to establish the Do-Not-Call Registry and required the FCC to coordinate with the FTC in promulgating its DNC rules. In early 2003, the FTC promulgated a new Telemarketing Sales Rule ("TSR") which established the National Do-Not-Call Registry (the "National Registry") that would be maintained by the FTC, and imposed other restrictions on telemarketers. And in 2003, the FCC amended its TCPA rules to better coordinate with the FTC and the National Registry. At the state level, as of 2003, 36 states had passed "do-not-call" statutes. As of July 2010, almost every state had enacted some form of telemarketing, telemarketing sales or anti-fraud, and/or do-not-call legislation.

b. Telemarketing Restrictions, Prohibitions and Protections

The TSR, and the complementary FCC TCPA rules, apply to "telemarketers" (a person who initiates a telemarketing call) as well as to "sellers (persons or entities that arrange to provide goods or services to consumers in exchange for payment)." A business, person or entity – which could be a franchisor, a franchisee, or possibly a franchise system marketing fund – that engages in telemarketing, or hires a third party to conduct telemarketing, could be subject to the telemarketing and DNC rules. Certain businesses are exempt from aspects of the TSR, and some types of calls need not comply with certain of the requirements of the TSR, even if the entity is covered. For example, non-profit organizations and companies soliciting charitable contributions are exempt from certain obligations under the TSR and the DNC rules. Examples of other calls that may be exempt from certain TSR rules include political solicitations and telephone surveys, calls placed in response to a catalog, the sale of franchise and

429 FCC 2003 Order, supra para. 12, n.44.
430 16 C.F.R. § 310.2(bb); 47 C.F.R. § 64.1200(f)(9).
431 16 C.F.R. § 310.2(z); 47 C.F.R. § 64.1200(f)(7).
432 16 C.F.R. § 310.6(a); 47 C.F.R. § 64.1200(a)(2).
433 FCC 2003 Order, supra, para. 37.
business opportunities, general media advertising or direct mail advertising;\textsuperscript{434} calls made to persons with whom the business has an “established business relationship;”\textsuperscript{435} calls involving the sale of a franchise governed by the FTC Franchise Rule,\textsuperscript{436} and calls that are part of a transaction in which the payment or transaction is not completed until after a face-to-face sales presentation.\textsuperscript{437} But even if certain calls are exempt from certain TSR rules, abusive telemarketing practices, threats, failing to transmit caller information, interfering with a person’s right to be placed on the National Registry, or calling during prohibited hours are not exempt.

The TSR and related FCC and state rules include several principal (and sometimes overlapping) rules or restrictions. Telemarketers and sellers: (1) must provide material information in calls to consumers; (2) may not make false or misleading statements; (3) may not engage in abusive telemarketing practices; and (4) may not call people whose phone numbers are listed on the National Registry or state do-not-call registries. The detailed prohibitions and restrictions on telemarketers and sellers are described in the TSR,\textsuperscript{438} the FCC’s TCPA rules,\textsuperscript{439} in guidance provided on the FTC’s and FCC’s websites,\textsuperscript{440} and in state laws and regulations. Some of the more significant rules and restrictions include:

- Sellers and telemarketers – whether placing an outbound call or receiving an inbound call – must provide certain material information, including:\textsuperscript{441}
  - The cost and quantity of the good or services
  - The existence of a “negative option plan”\textsuperscript{442}
  - Material restrictions, limitations or conditions on the purchase
  - No-refund policies
  - Prize promotion information, such as the odds of winning the prize, and any material cost to receive or redeem the prize
  - Credit card loss protection and any limitations on that protection

- The outbound telemarketing call must include prompt disclosures – before any “pitch” – including the identity of the seller, the purpose of the call, the nature of the goods and services offered, and in the case of a prize promotion, that no purchase is necessary. Charitable contribution solicitations also must include certain prompt (pre-pitch) disclosures.\textsuperscript{443}

\textsuperscript{434} 16 C.F.R. § 310.6(b)(5) & (6).
\textsuperscript{435} 16 C.F.R. § 310.4(b)(iii)(B)(ii); 47 C.F.R. § 64.1200(a)(2)(iv).
\textsuperscript{436} 16 C.F.R. § 310.6(b)(2).
\textsuperscript{437} 16 C.F.R. § 310.6(b)(3). This exemption can be particularly useful to franchise companies that offer products or services to consumers at their homes, as many sales of products and services to consumers are not concluded until after the franchisee’s representative meets with the consumer.
\textsuperscript{438} 16 C.F.R. Part 310.
\textsuperscript{439} 47 C.F.R. § 64.1200.
\textsuperscript{441} 16 C.F.R. § 310.3(a)(1).
\textsuperscript{442} 16 C.F.R. § 310.3(a)(1)(vii). This is a plan where a consumer’s silence or failure to take an affirmative action to reject goods or services or cancel an agreement will be deemed an acceptance of an offer. 16 C.F.R. § 310.2(l).
\textsuperscript{443} 16 C.F.R. § 310.4(d).
\textsuperscript{444} 16 C.F.R. § 310.4(e).
Telemarketers and sellers are prohibited from making false or misleading statements to induce a person to pay for goods or services, including, for example, statements related to the performance and efficacy characteristics of the products, refund or repurchase policies, and endorsements or sponsorships.

Telemarketers may not cause billing information to be submitted for payment without complying with payment authorization rules, and must comply with rules and restrictions on credit card purchases and other billing procedures.

Telemarketers and sellers must not engage in “abusive telemarketing acts” or practices, including:

- using threats, intimidation or obscene language;
- requesting a fee or payment in advance for a loan; or
- disclosing or receiving, for consideration, unencrypted consumer account number for use in telemarketing.

Telemarketers and sellers may not:

- deliver an artificial or prerecorded voice message (subject to certain exceptions, such as the existence of an established relationship with the caller);
- send an unsolicited advertisement to a fax number;
- abandon more than 3% of telemarketing calls that are answered live by a person;
- make calls to a residential telephone between 9 p.m. and 8 a.m. local time.

For a more comprehensive list of restrictions, prohibitions and obligations under the TSR, see the FTC’s “Facts for Business – Complying with the Telemarketing Sales Rules”, available on the FTC’s website. The summary of this FTC report (“Amended TSR at a Glance”) is reproduced at Appendix F of this paper.

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445 16 C.F.R. § 310.3(a)(2).
446 16 C.F.R. § 310.3(a)(2)(iii)-(v).
447 16 C.F.R. § 310.3(a)(3).
448 16 C.F.R. § 310.4(a).
449 47 C.F.R. § 64.1200 (a)(2).
450 47 C.F.R. § 64.1200 (a)(3).
451 47 C.F.R. § 64.1200 (a)(6). Telemarketers use “predictive dialers” which automatically dial one number while the telemarketing agent is talking to a person on another line. The predictive dialer will hang up on a caller if the telemarketer is not available to speak. These "hang ups" infuriate consumers and prompted this rule.
452 47 C.F.R. § 64.1200 (c)(1).
c. Do-Not-Call Registry

All consumers who do not wish to receive telemarketing calls may place their names and phone numbers in the National Registry, maintained by the FTC. Consumers may register via the FTC website at www.donotcall.gov, or by phone (1-888-382-1222). The National Registry accepts landline numbers and wireless phone numbers. Sellers and telemarketers may not make calls to telephone numbers on the FTC’s National Registry (with some exceptions). Violators are subject to civil penalties of up to $10,000 per violation, as well as injunctive remedies.

Telemarketers, sellers and other service providers may access the National Registry to obtain the phone numbers of consumers who have requested that they not be contacted by telemarketers. Telemarketers must pay a fee to access the National Registry database so that they may "scrub" their calling lists. The current annual fee (for fiscal year 2010, beginning October 1, 2009) to access the National Registry is $55 per area code, or $15,058 for every area code, whichever is less. Telemarketers and sellers must update their do-no-call list at least once every 31 days. That is, they must delete all numbers in the National Registry from their call lists.

The TSR and DNC rules contain a “safe harbor” so that a telemarketer or seller will not be subject to civil penalties or sanctions for erroneously calling a consumer on the National Registry. To qualify for the safe harbor, the telemarketers or seller must:

- Establish and implement written procedures to honor customer’s requests
- Train its personnel to comply with the do-not-call rules
- Maintain and record a do-not-call list of prohibited telephone numbers
- Maintain records documenting the process utilized to prevent calls to numbers on the National Registry
- Monitor and enforce compliance with the do-not-call rules

454 The Do-Not-Call provisions do not cover certain calls from political organizations, charities, telephone surveyors, or companies with which a consumer has an existing business relationship. 16 C.F.R. § 310.6. And see the FTC’s website, www.fcc.gov/edocs_public/attachmatch/fcc-03-U3A1.pdf. See also text at footnotes 431-436 supra.
456 FCC 2003 Order, supra, para. 9. “Scrubbing” refers to comparing a do-not-call list to a company's call list and eliminating from the call list the telephone numbers of consumers who have registered a desire to not be called. Id. para. 9, n.37
458 16 C.F.R. § 310.4(b)(3).
• Establish that any call made to someone on the National Registry was in error

d. State Laws

The FTC’s TSR and the FCC’s rules do not preempt state law. As of July 2010, approximately 43 states have enacted some type of telemarketing fraud and/or do-not-call law.459 Some states maintain their own do-not-call lists,460 and some specify that telemarketers operating in their state utilize the FTC’s National Registry to satisfy the state’s law.461 In addition, state laws also prohibit fraudulent, misleading, deceptive and/or abusive telemarketing practices.462 Violations of a state’s laws may range from $500 per infraction (e.g., Vermont)463 to up to $25,000 per infraction for multiple infractions (e.g., Indiana).464

e. Scrubbing and Teleblock®

As discussed above, a seller or telemarketer must not engage in deceptive, fraudulent or abusive telemarketing practices. And, it must not call persons on the National Registry and state do-not-call lists. Companies often compile and/or purchase databases of potential customers and phone numbers prior to commencing a telemarketing campaign. To avoid penalties or sanctions, the company (or its telemarketing vendor) must access the National Registry (and state lists) and remove from their call lists any prohibited numbers. The basic method is to “scrub” lists on a monthly basis. This is a timely and costly process. But, if done properly it will minimize the risk of calling a number on a do-not-call list. An alternative method is a product called Teleblock®. Teleblock® is a patented program that automatically screens and blocks outbound calls against available federal, state, wireless, third party and in-house do-not-call lists.465 According to Call Compliance, Inc.,466 the owner and marketer of Teleblock®, no company that uses Teleblock has been fined for do-not-call violations.467

f. Franchising

Telemarketing may be utilized by any business in any industry, and may be employed by national chains, franchised networks, and small offices or businesses. But, certain businesses

459 Several companies and organizations maintain databases and/or regulatory compliance guides with summaries of state laws. See Call Compliance, Inc. (www.callcompliance.com) and the American Teleservices Association (ATA) (www.ataconnect.org), which jointly publish (for sale) a Do Not Call Regulatory Guide. Attached as Appendix G is a Summary of State Do Not Call Regulations, published by, and used with permission from, Call Compliance, Inc. The Do Not Call Regulatory Guide contains summaries of federal and state laws regarding telemarketing rules and do-not-call rules. Attached as Appendix H is an excerpt from the Do Not Call Regulatory Guide, with a summary of the telemarketing and DNC rules and laws from one state (Indiana), used with permission of Call Compliance, Inc. (“Regulatory Guide”). In addition, the National Association of Regulatory Utility Commissioners (“NARUC”) maintains a website, http://www.naruc.org/commissions.cfm, which lists all state regulatory commissions which have, or may have, jurisdiction over telemarketing practices and do-not-call lists. These commissions may be a source for additional state-specific information.

460 See, e.g., FLA. STAT. § 501.059(3)-(4) (Florida); WISC. STAT. § 100.52(2) (Wisconsin).

461 See, e.g., KY REV.STAT. ANN. § 367.46955(15) (Kentucky).


464 Ind. Code § 24-4.7-5-2 (Indiana).


466 Id.

467 Author’s note: The discussion regarding Teleblock® above should not be construed or deemed to be the authors’ or the ABA Forum on Franchising’s endorsement of any particular methodology, product, or provider for complying with the federal and state telemarketing and DNC rules.
tend to use telemarketing more than others. For example, businesses that sell resort
timeshares and similar properties (including affiliates of franchised hospitality companies), have
utilized telemarketing quite extensively. Businesses that sell products and services to
consumers (particularly for at-home sales) through mobile sales teams or distributors may utilize
telemarketing, and some of these industries are franchised. But telemarketing may be utilized
by any franchisor or franchisee, and the telemarketing and DNC rules will apply to a company
that sells the goods or services that are marketed by telemarketers. A franchisor that expects or
encourages its franchisees to undertake telemarketing, or learns of a franchisee’s intent to
telemarket, should advise its franchisees to seek appropriate counsel, investigate the
prospective telemarketing company to assess whether and how it complies with the TSR, and
obtain assurances of compliance. Even if telemarketing may not be an integral part of a
franchise system’s marketing campaigns, the potential for adverse consequences is significant
enough for franchisors to warn franchisees of the compliance obligations. The negative public
relations generated by a do-not-call violation – even if it pertains to only one franchisee or
market – will harm the franchisor, other franchisees, and the goodwill of the system. Consequently, if telemarketing may be utilized by franchisees, references to compliance with
these laws can be added to the franchisor’s manuals. Unless the franchisee’s business is in a
telemarketing-intensive business, disclosure of these rules in the FDD is generally not
necessary.

2. Drug Testing

a. Generally

Drug-testing is the practice by which employers screen prospective and/or current
employees to determine if the prospect or employee has used, or has in his/her system, certain
drugs and/or alcohol. Most employers in the United States are not required to test employees
or applicants for illegal drugs, alcohol, or other substances, even though they have the right to
test for a variety of substances. However, drug-testing in the U.S. workplace is standard
practice, as it is an “integral part of [the] hiring process and the employment process” in the U.S.
today. If a business chooses to test employees for illegal substances, its drug-testing policies
and programs will likely be subject to state laws and possibly federal law.

For any employer, promoting a drug-free workplace has many benefits: it develops
customer confidence and goodwill; it helps maintain a safe workplace for employees and its
customers, and establishes a positive work environment for all employees. Drug-testing and a
“drug-free workplace” policy may also provide tangible economic benefits to a company.
Businesses that adopt a drug-testing policy may pay lower workers’ compensation and/or
unemployment compensation insurance premiums because of the policy. To achieve a drug-
free workplace, employers must be able to not hire employees that use illegal drugs, and/or to
provide counseling to, and/or to fire, those who use illegal substances. And to determine if
employees are using drugs and/or alcohol, an employer must be able to test for such
substances. But, a drug-free workplace and the procedures to implement a drug-free workplace
policy run up against privacy concerns. In addition, any person who has had to provide a urine,
saliva or hair sample in conjunction with a pre-employment evaluation, or a random test at work,

468 The authors wish to thank Matthew F. Nieman, Esq., of Jackson Lewis LLP, Reston, Virginia, for his assistance
and contributions to this section of this paper.
469 Mark A. de Bernardo & Matthew F. Nieman, GUIDE TO STATE AND FEDERAL DRUG-TESTING LAWS (Institute for a Drug
may be concerned about the accuracy of the test. Due to these concerns for privacy and accuracy, as well as claims of unfair or unjust termination of employees, the states and federal government have enacted a wide range of laws pertaining to drug and alcohol testing of employees. The laws are designed to regulate employment policies and practices so that actions taken against employees due to drug use are fair.

i. Federal Laws

While there is no one law or incident that launched employee drug-testing, the concept of a “drug-free workplace” began to gain traction in the 1980’s. In 1986, President Ronald Reagan issued Executive Order 12564, which instituted mandatory drug-testing for certain safety-sensitive federal jobs. In 1988, Congress passed an omnibus drug bill called the “Drug-Free Workplace Act” which required private sector federal contractors and recipients of federal funds to implement steps towards assuring that they have a drug-free work force. The Drug-Free Workplace Act does not require workplace drug-testing, but a company may include various forms of drug and alcohol testing to achieve the goals of its drug-free workplace policies. While the Drug-Free Workplace Act is relatively narrow in terms of the employers that it covered, it accelerated the trend among employers to have and maintain a drug-free work force.

Since the adoption of the Drug Free Workplace Act of 1988, a number of federal laws and regulations have been adopted or implemented that require drug and alcohol testing for certain regulated industries. These industries include transportation, aviation, carriers and holders of commercial driver's licenses (“CDL”), the railroad industry, the mass transit industry, the pipeline industry, and commercial vessels. These federal regulations prescribe who must be tested, the frequency of drug and alcohol tests for employees, the types or methods of permissible testing, and required procedures in administrating tests, handling samples, and reporting results. The Department of Transportation’s (“DoT”) Office of Drug and Alcohol Policy Compliance (“ODAPC”) regulates how drug and alcohol tests are conducted, and what procedures are used. The regulations of the DoT agencies (i.e., FRA, FMCSA, FTA, FAA, PHMSA, and USCG) determine who is tested and when. And the U.S. Department of Health and Human Services adopted guidelines that certify labs and establish threshold detection levels and scientific testing procedures. Most of these drug and alcohol testing rules apply to safety-sensitive and/or security-related positions. But these rules and regulations have applications that are broader than their narrow target range of employers and industries. In particular, the criteria for testing, and the methodologies used for testing, transporting and safeguarding samples, and reporting results, are often used by private sector

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479 See supra note 472.
481 There are approximately 12.1 million people performing safety-sensitive transportation jobs that are covered by DoT drug and alcohol regulations. DOT Office of Drug and Alcohol Policy and Compliance webpage, www.dot.gov/ost/dapc.
employers and/or third party testing companies hired by private sector employers. If a private sector company, including a franchisor or franchisee, decides to implement a drug and alcohol policy, it will most likely retain a third party testing company. And if an adverse action is taken against an employee for failing a drug test, the legality and enforceability of that action is enhanced if the policy complies with law and the testing is done by a company and lab that follow DoT standards.

ii. State Laws and Regulations

If a company adopts a drug-free workplace policy, which may include drug-testing, it will be part of the employer’s employment policy. In response to the competing interests of maintaining drug (and alcohol) free workplaces, privacy concerns, and fairness to employees and prospective employees, many states have statutes and/or case law that regulate drug-testing and/or provide guidelines for an acceptable drug-testing policy. The principal purpose of drug-testing, or a drug-testing policy, is not to catch employees that have used or are using a banned, controlled or illegal substance. Rather, the purpose of the policies is to put employees and applicants on notice that: (a) the employer desires to have a drug-free workplace, (b) the employer desires to have its employees be drug (and alcohol) free so that they can perform their job duties properly, (c) the employee may be tested for drug or alcohol use, and (d) the employer can fire the employee or take other actions if the employee does not comply with the policy. Employers want productive employees; employers do not want to fire employees.

“Drug-testing” is shorthand for a broad array of testing and policies. There are various types of drug-testing. While some definitions vary, the following are four broad categories:

- **Pre-employment Testing**: This is testing that is part of the application process before an offer of employment is made. It may be part of the hiring process, and the testing may be conducted after the offer of employment is made, but the offer is contingent upon passing the test.

- **For-Cause Testing**: Also referred to as “probable cause” or “reasonable suspicion” testing, this testing is performed when an employee’s behavior or physical appearance suggests drug use or possession. Many states have very specific definitions of “cause.”

- **Post-Accident Testing**: This involves testing an employee after his/her involvement with an on-the-job accident that may have involved human error and which causes serious injury or fatality, or significant property damage. This is sometimes referred to as “post-incident” testing.

- **Random Testing**: These are tests of employees who are chosen on a “neutral-selection” basis, without individual suspicions and without advance notice. Random

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482 See the Guide, supra note 469, at 3-4.
483 Id. at 3.
484 Id. at 4. See, e.g., Rhode Island, R.I. GEN. LAWS §§ 28-6.5-1 to 28-6.5-2 (2003) (the employer must be able to point to specific aspects of an employee’s performance based on observations of the employee’s appearance, behavior or speech).
485 See the Guide, supra note 469, at 4.
testing may also involve testing all employees, but the date and time is not announced in advance.486

As noted above, except for certain safety-sensitive and/or security related industries where drug-testing is required, for most employers, adopting a drug-testing, substance abuse, or zero tolerance policy is voluntary. And the elements of a policy -- who is tested, when the tests are conducted, and the consequences of a positive test -- are also left to the discretion of the employer.487 For example, a company may decide to conduct only pre-employment testing, and test only certain employees who work in safety-sensitive areas. Or an employer may determine it is necessary to test employees only under a post-accident or post-incident scenario. Regardless of the elements of the policy, it is likely to be subject to state laws.

Attached as Appendix I is a “Summary of State Drug-Testing Laws and Relevant Workers’ and Unemployment Compensation Laws” (“Summary Chart”).488 As described in the Summary Chart, and as discussed in detail in the Guide,489 there are a myriad of statutes, regulations and case law that may impact a company’s decision to adopt and/or implement a drug-testing policy. Some states may permit certain types of drug-tests, such as pre-employment tests, but prohibit other drug-tests, such as random testing. Some states regulate certain testing procedures.490 Or, there may be no specific state law regulating the type of tests that an employer may conduct, but there may be other laws affecting drug testing.491 Employers must be mindful of these state laws because if a drug-testing policy, and/or the implementation of that policy or the tests that are conducted, do not satisfy the laws and regulations, the employer’s hiring, firing and/or counseling decisions may be subject to challenge, and the employer may be liable for improper or wrongful termination based on illegal or improper drug-testing policies or practices. While a detailed state-by-state analysis of these laws is beyond the scope of this paper, the Summary Chart provides a useful categorization of state drug-testing laws and can be a valuable resource for attorneys counseling their clients. The Summary Chart identifies eight types or categories of statutes, regulations or case law that regulate or impact drug-testing policies, and identify the states that fall under each group. These groupings are:

(1) states that do not have any statutory or case law affecting an employer’s right to drug test employees;

(2) states that have case law on drug testing;

(3) states that do not restrict the types of testing an employer may conduct, but statutorily set forth specific procedures an employer must follow when choosing to implement a drug-testing program;

486 Id. at 3.
487 Note that certain employers may structure their policies in conjunction with a union that represents the company’s workforce.
488 See the Guide, supra note 469. The chart in Appendix I is graciously provided with the permission of the Institute for a Drug Free Workplace, Jackson Lewis LLP, and the editors, Mark de Bernado & Matthew Nieman.
489 The Guide is exceptionally comprehensive, and is an excellent resource for laws, regulations and case summaries. The details in the Guide are beyond the scope of this paper. The Guide, supra note 469.
490 See, e.g., Connecticut, CONN. GEN. STAT. §§ 31-51t to 51aa, §§ 31-128a to 128h (2003), § 14-261b (2006).
491 See, e.g., Florida, which has no drug-testing law, but its Drug-Free Workplace Act requires that certain contractors performing work related to public schools or on public property must implement a drug-free workplace program or policy. Such a policy may or may not have a drug-testing component. FLA. STAT. ANN. § 440.102(15) (2003).
(4) states that statutorily restrict both the type of drug test administered (who and when) and the procedures used (how) to perform such drug testing;

(5) states which have voluntary laws affecting drug testing;

(6) states with voluntary workers’ compensation premium reduction laws that grant employers in compliance a discount on their workers’ compensation insurance;

(7) states with related workers’ compensation statutes and/or cases; and

(8) states with related unemployment statutes and/or cases.

In addition, there are at least two municipalities in the United States – San Francisco, California and Boulder, Colorado – that have enacted drug-testing laws.492

The impact of these laws is that all employers must be careful when adopting a drug-testing policy. A drug-testing policy should clearly describe who can be tested, what tests can be administered, the frequency of the testing and the consequences of a positive test. Applicants and/or employees must be on notice that the consequences may include not hiring the applicant, or firing the employee. Or the consequences could subject an employee to a probationary period coupled with mandatory counseling. The policy can and should be tailored to the needs and objectives of the company, but it must also comply with the applicable state laws. Moreover, companies with operations in more than one state must be mindful of the variations in state laws, and the variations with respect to permitted and prohibited activities. A drug-testing policy that complies with the laws of one state may run afoul of the laws of another state. So a company’s employees may be subject to different rules depending upon the state in which they work. These state variations are particularly critical to franchisors and multiple-unit franchisees with multiple-state operations.

b. Impact on Franchising

i. Required Drug-Testing in a Regulated Industry

Most franchised businesses do not operate in industries which are subject to one of the federally-mandated drug testing regulations.493 However, if the business is subject to these laws,494 the franchisee (and any franchisor-operated businesses) must implement a policy that complies with the applicable regulation.

A franchisor with franchised businesses that are subject to one of these industry-mandated laws, should disclose information about drug-testing in the FDD, and should include references to the requirements in the franchise agreement and manuals. As noted in Part II above, the disclosure of these regulations would appear in Item 1 of the FDD. To the extent drug-testing costs will be incurred in the franchisee’s initial start-up phase, the tests should be disclosed in Item 7. Also, if the franchisor designates a particular vendor for drug-testing, or if

492 See Guide, supra note 469, at 77-78 and 87-88; S.F., CAL., POLICE CODE art. 33A (1993); BOULDER, COLO., HUMAN RIGHTS CODE, §§ 12-3-1 to -6 (1994).

493 See supra notes 470 to 478.

494 For example, a franchised moving and storage company, and/or a franchised cement distribution and delivery business, may hire drivers that need a CDL, and/or other businesses which require a CDL, are likely to be subject to the drug-testing rules enacted by FMCSA. See supra note 473.
drug-testing is part of the training program, this information may need to be disclosed in Item 8 or Item 11. Generally speaking, if a franchisor operates in any industry that is subject to these mandatory federal laws, the franchisor will most likely have extensive knowledge of the requirements and should have the relevant information to include in the FDD.

Also, there may be franchised businesses that are in industries that are not subject to mandatory drug-testing, but the nature of the work, or the location that the work is performed, or the nature of the customer, may require that the franchised business comply with a state drug-testing rule or law. See, for example, the Florida law cited in supra note 490. Franchised businesses that provide tutoring or testing at schools, or provide construction, repair or maintenance work on public property, may be subject to the Florida Drug-Free Workplace Act.

ii. Voluntary or Discretionary Drug-Testing Policies

For many franchise networks, adopting or recommending a drug-testing policy is a voluntary decision, and will not be mandated by federal or state law. Drug-testing will, therefore, generally arise in the franchise context in one of the following scenarios:

1. A franchisor considers a drug-testing policy for its employees for its headquarters and/or company-owned locations.

2. Franchisees, on their own, or based on a recommendation, suggestion or mandate from the franchisor, consider a drug-testing policy for their employees.

3. A franchisor considers recommending or mandating that its franchisees adopt a drug-testing policy for the franchisee’s employees.

4. A franchisor considers implementing a drug-testing policy applicable to prospective franchisee candidates, or existing franchisees.

The first two scenarios involve an employer-employee relationship, but do not have specific franchise implications as they involve a company or business adopting a policy (or not adopting one) for its workforce. The considerations for these franchisors and franchisees will be similar to any other business in their industry that adopts or may implement a drug-testing policy. The third scenario, however, does raise additional issues for a franchisor, as the franchisor is either suggesting or requiring employment-related rules for its franchisees. As noted in the discussion of vicarious liability in Part II above (and the sources described in note 2 above), and in Parts III.A.2 and III.A.4 above, franchisors often refrain from requiring that franchisees adopt certain employment policies to reduce their exposure to claims from the franchisee’s employees. The fourth scenario is outside of the employment context, and treats passing a drug test as a pre-condition to granting a franchise.

A franchisor or franchisee that is considering a drug-testing policy should evaluate the costs and benefits. For example:

- Will workers at the outlets be engaged in safety-sensitive jobs, and will a drug-free workplace policy help assure safe working conditions?

- Will the safety of customers be improved with a drug-free workplace?
What is the likelihood that an accident or other incident may occur due to an employee who is using drugs or alcohol, that the incident might generate negative publicity, and the existence of a drug-free workplace policy and/or drug-testing might blunt some of the negative public relations and/or shield the employer (franchisor or franchisee) from liability?495

Is the franchise in an industry in which the premiums for the workers’ compensation and/or unemployment insurance policies will be reduced if an employer has adopted a drug-testing policy?

Are the franchised outlets operating in an industry in which drug and alcohol use by employees is well-known or suspected, and a drug-testing policy may eliminate a significant portion of the prospective labor pool?

In the event a franchisor or franchisee believes that there are benefits for its company by adopting a drug-testing policy, it may do so. But such a policy should be well-conceived and well-constructed with the advice of employment lawyers and other professionals, and it should be well-documented and consistently applied.

As discussed earlier in other contexts regarding vicarious liability, franchisors often tread lightly, if at all, in areas which may impact a franchisee’s employer-employee relationships.496 Drug-testing is no exception. A franchisor may determine that a drug-free workplace policy and drug-testing are desirable goals for all outlets within its franchised network. Even if the franchisor has adopted a policy that it believes is right for its outlets and employees, the varied prohibitions under state laws demonstrate that these policies cannot be one-size-fits-all. Moreover, to protect against or reduce the risk of a claim from a franchisee’s employee, a franchisor should not dictate a drug-testing policy. Drug-testing and drug-free workplace policies would be incorporated as part of an employment policy. Because the ultimate consequence of the policy may be the termination of a franchisee’s employee, a franchisor would be wise to avoid requiring any particular drug-testing policy or practice, and leave it to the discretion of the franchisee. By not mandating the implementation of a policy, the franchisor has a stronger argument that it is not controlling the franchisee’s employment policies. To minimize potential franchisee employee claims against the franchisor, the franchisor should only suggest or recommend that a franchisee adopt a drug-free workplace policy. The suggestions or recommendations -- which should be included in the manual or other communications -- should be clear that: (a) the franchisor is not mandating any specific policy, (b) the franchisee is free to adopt its own policy, (c) any policy must comply with applicable law, and (d) the franchisee should obtain qualified counsel and other professionals in developing the policy.

495 As an example, a pizza restaurant or chain may determine that conducting pre-employment, for cause, random and/or post-accident drug-testing for its delivery drivers will reduce accidents, and if an accident does occur, the pizza chain can point to the drug-testing policy as an effort to prevent driving accidents, and reduce potential liability.

496 As discussed in Cynthia M. Klaus, et al., Vicarious Liability, ABA 31st Annual Forum on Franchising, 2008, franchisors may face claims from employees of franchisees for sexual harassment or similar claims under a “single employer” test, if the employee can demonstrate that the franchisor controlled the day-to-day employment decisions of the franchisee. In several cases cited therein, e.g., Lockard v. Pizza Hut, 162 F.3d 1062 (10th Cir. 1998); and Alberter v. McDonald's Corp., 70 F. Supp 2d 1138 (D. Nev. 1999), the facts concerning the franchisor's control over the franchisee's employment policies and employment decisions was critical. In both cases, the franchisor did not dictate or mandate employment policies, and the lack of control over the employees was a principal reason why the franchisor was not liable to the franchisee's employee for sexual harassment or a hostile work environment at the franchised outlet.
iii. Franchisor Testing of Franchisees

A franchisor may wish to conduct drug-testing on prospective franchisees as part of the pre-sale screening or evaluation process. Even if the franchised business is not in an industry with federal drug-testing requirements, there may be valid reasons to conduct drug-testing as a condition of granting the franchise. For example, if the franchisee is likely to operate as a sole proprietorship or single person operator (such as a distributor of hand tools that drives a truck (even if a CDL is not required), or a franchisee that sells and installs alarms and security systems), the franchisor may determine that pre-sale testing will be beneficial. Clearly the franchisor does not wish to have a substance-abusing franchisee drive a truck with the franchisor’s logo on it. In the event of an accident in which drug or alcohol use is a contributing factor, a franchisor may be able to blunt some of the expected criticism and negative publicity if it had conducted, and the franchisee passed, a drug test prior to granting a franchise. And the drug-testing policy may be useful in defending against claims from third parties.

In addition to pre-sale testing, a franchisor may decide to adopt a drug-testing policy for all operating franchisees. If a concern exists that warrants pre-sale drug-testing (e.g., truck drivers), that concern is likely to be present during the term of the franchise. If the franchisor plans to drug-test franchisees, the franchisor should have a clear, unambiguous, and well-communicated policy. Evidence of drug, alcohol or other illegal substances may be a default under the franchise agreement and grounds for termination. But before adopting such a policy, it should be reviewed and approved by counsel, and should be compliant with the laws of all applicable states. Moreover, it should be clearly disclosed in the FDD, and included with specificity in the franchise agreement.

If a franchisor adopts a drug-testing policy to test prospective or existing franchisees, the franchisor is unlikely to find clear guidance under the laws regarding implementing such a plan or policy. Many of the state drug-testing laws are written in terms of individuals, companies, employers and employees, and may not apply specifically to the franchisor sale-of-a-franchise scenario or a franchise termination situation, because these are not employment-related situations or relationships. Even though a franchise or independent contractor relationship is not an employment relationship, the drug testing laws may provide a framework for policies that might be adopted by franchisors in the franchise application process. For example, in Connecticut, like many other states, pre-employment drug-testing is permitted, but applicants must be provided with written notice of the testing. Applying this notice principal to the franchise context, a franchisor selling franchises in Connecticut (or another state with a similar law) may decide to implement pre-sale testing, but it should look to the state laws for guidance regarding pre-testing written notice. The written notice requirements of many state laws easily can be applied to the franchise application process. By providing advance notice of the franchisor’s drug-testing plans, a prospective franchisee will have a choice as to whether to apply for the franchise and undergo a drug test. Even if the drug-testing laws do not apply to the franchisor-franchisee relationship, a franchisor that models its policy in compliance with laws applicable to employers can argue – if its actions are challenged – that it followed the closest analogous laws and regulations.

Drug-testing is part of the employment landscape. It is something every franchisor and franchisee should consider in the context of their business operations, employee safety and morale, and potential impact to the goodwill of the brand. But, because of the state-specific

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497 See supra note 490.
variations of permitted and prohibited drug-testing activities, drug-testing policies should be carefully created, tailored, and implemented with advice from experts.

3. Service Animal Laws

The American with Disabilities Act ("ADA") prohibits discrimination against any individual based on their use of a service animal. Federal law (the Code of Federal Regulations ("CFR")) provides that "[n]o individual shall be discriminated against on the basis of disability in the full and equal enjoyment of . . . any place of public accommodation by any private entity who owns, leases (or leases to), or operates a place of public accommodation."498 The CFR provides that "[g]enerally, a public accommodation shall modify policies, practices, or procedures to permit the use of a service animal by an individual with a disability."499 A service animal is defined as "any guide dog, signal dog, or other animal individually trained to do work or perform tasks for the benefit of an individual with a disability, including, but not limited to, guiding individuals with impaired vision, alerting individuals with impaired hearing to intruders or sounds, providing minimal protection or rescue work, pulling a wheelchair, or fetching dropped items."500

With the exception of Alabama,501 all fifty states have enacted regulations regarding service animals that are similar to the ADA, although many state laws offer greater protection than the ADA. For example, the ADA states that liability will be imposed on "any private entity who owns, leases (or leases to), or operates a place of public accommodation."502 As a practical matter, this provision on its face would eliminate liability for many franchisors, as they ordinarily do not "own, lease, or operate" their franchisees' locations. On the other hand, California Civil Code section 51 imposes liability on "whoever denies, aids or incites a denial" of the rights of a disabled person with a service animal. Accordingly, if a plaintiff argues that a franchisor's policies, e.g. a no pets policy that results in a disabled person being turned away, "aids or incites" a denial of the rights of disabled persons with service animals, then the franchisor could arguably be liable under California's law.

The majority of states also provide that trainers of service animals are entitled to the same protections as persons with disabilities, however, some states require that trainers of service animals comply with additional requirements in order to be protected under the statutes.

a. What is a Service Animal?

The issue of whether service animals are limited to dogs, as opposed to other animals such as monkeys or miniature horses is currently the subject of much debate. The ADA does not explicitly limit service animals to dogs, but provides that a service animal is "any . . . animal individually trained to do work . . . for the benefit of an individual with a disability . . . ."503 Like the ADA, the majority of states define a service animal as "any animal" that is individually trained to help an individual with a disability, leaving open the question of whether animals other than dogs may qualify as service animals. Some states, like Rhode Island explicitly allow for animals other than dogs to be used assistance animals. Rhode Island law provides that "[t]he

498 28 C.F.R. § 36.201
499 28 C.F.R. § 36.202
500 28 C.F.R. § 36.202
501 Both Alabama and the District of Columbia have enacted anti-discrimination statutes for individuals with guide dogs or hearing dogs, however, service animals are not mentioned in their statutes.
502 28 C.F.R. § 36.201
503 28 C.F.R. § 36.104
privileges of access . . . provided to personal assistance animals . . . shall be extended to family therapy pets which are further defined as primary companions which include, but are not limited to, dogs, cats, rabbits, and guinea pigs, that are working in the provision of pet assisted therapy treatment and education."504

More recently, in May of 2010, the Vermont Fish and Wildlife Department granted approval to a disabled woman with multiple sclerosis to use a service monkey trained by Helping Hands, a non-profit organization in Boston that breeds and trains small monkeys to work as service animals. The Department had originally denied the woman's request. After the disabled woman turned to the State Legislature for help, the State Senate passed a bill to allow the importation of a monkey in limited circumstances. Before the bill moved to the House for consideration, the Department reversed its stance, setting a series of conditions, including yearly visits by Department officials to check the monkey’s living arrangements and an annual health exam. The issue of what type of animal qualifies as a service animal will likely remain in flux for a few years. While franchisees are likely aware of the requirement to accept service “dogs,” they may not be aware that in some states they may be required to accept an animal other than a dog as a service animal. As discussed below, because franchisors may potentially be liable for their franchisees’ violations, the issue is one that franchisors should pay attention to.

b. Potential Liability of Franchisors

There are only a handful of cases addressing the potential liability of a franchisor where a franchisee fails to accommodate a guest with a service animal. The Eighth Circuit has concluded that a franchisor could not be held liable for an alleged violation of the ADA by a franchisee because it did not “own,” “operate” or “lease” the premises where the incident occurred.505 The California courts that have addressed the issue have similarly concluded that a franchisor could not be held liable for a franchisee’s alleged act of turning away a disabled guest with a service animal. However, the California decisions leave open the possibility that a franchisor may be found to be vicariously liable for a franchisee’s violation of laws related to service animals.

In Pona v. Cecil Whittaker’s, Inc., 506 the Eighth Circuit held that a franchisor could not be held liable for a franchisee’s failure to accommodate a guest with a service animal. In Pona, the employees at a Cecil Whittaker’s Pizzeria asked the plaintiff to leave their premises because she had a service dog with her. The franchisor, Cecil Whittaker’s, Inc. (“CW”) argued that “as the franchisor of the pizzeria, it did not own, lease, or operate the pizzeria, and therefore cannot be liable under the ADA.”507 The court found that “[i]t is undisputed that CW was only a franchisor, and that under its franchise agreement it reserved no right to control entry to the pizzeria.”508 The court disregarded evidence that CW’s president had told the franchisee’s manager “that he ‘wouldn’t have any animals in [his] restaurant’ because it ‘doesn’t look good for the franchise.”509 The court disregarded this evidence because “it does not establish that CW owned, leased, or operated the pizzeria within the meaning of the ADA.”510 The court found

504 RHODE ISLAND GENERAL LAWS, Title 40, Chapter 9.1, Section 40-9.1-5.
505 Pona v. Cecil Whittaker’s, Inc., 155 F.3d 1034 (8th Cir. 1998).
506 Id.
507 Id. at 1036.
508 Id.
509 Id.
510 Id.
that CW’s president “had no right to control the manager’s actions in any relevant respect, and, absent any such right, no violation of the ADA appears.”511

The court in Pona also rejected the Plaintiff’s argument that the franchisee had “apparent authority” to act on behalf of the franchisor. The court noted that the question of CW’s liability under the ADA depends on its actual connection to the premises, not the Plaintiff’s belief about that relationship. “Besides, the mere fact that a franchisor’s sign appears on a building and the employees within that building wear uniforms bearing the franchisor’s logo and insignia does not clothe a franchisee with the apparent power to act on the franchisor’s behalf in anything approaching a general way. Nothing in the record, moreover, would indicate that CW did anything to give customers the impression that it controlled access to the building. Nor can Ms. Pona show that she relied on any such impression.”512

The court in Pona focused on the fact that the ADA only imposes liability on one who “owns,” “leases” or “operates” the premises. The result might have been different had the incident occurred in a state like California where liability is imposed on “whoever denies, aids or incites a denial” of the rights of a disabled person with a service animal.

In Stites v. Hilton Hotels Corporation et al., the plaintiff claimed that he was turned away from a Hampton Inn in San Clemente, California while traveling with his brother who allegedly used a service animal.513 The plaintiff claimed that the desk clerk on duty told them that they must produce proof that the dog was medically necessary and turned them away. The plaintiff’s lawsuit named a dozen corporate defendants, including Hilton Hotels Corporation, Promus Hotel Corporation and the franchisor, Promus Hotels, Inc. The corporate defendants moved for summary judgment, arguing that they did not have any connection to the plaintiff’s claim.

The court noted that “[u]nder the terms of the franchise agreement, [the franchisee] QSSC is ‘an independent contractor,’ not an agent of the franchisor, which has no power to direct or supervise the daily affairs of QSSC. As part of its obligations as a franchisee, QSSC is required to comply with all local, state and federal laws. Hilton and Promus have corporate policies permitting disabled guests with service animals to stay at their hotels. The franchisor sets policies and standards for the Hampton Inn brand. These policies require franchisees to follow the Americans With Disabilities Act, and training materials emphasize compliance with this law.”514

On appeal, the plaintiff argued that Hilton and Promus were “vicariously liable for his injury because the Inn is respondents’ agent.”515 The plaintiff argued that Hilton had “strong centralized management and it exercises the same extensive control over all of the operations at its franchised hotels as it does at its owned/managed hotels.’ He points to Hilton’s ‘brand standard’ manual—which is used at all Hilton hotels—as ‘evidence of sufficient control.’ As a result of Hilton’s extensive control, appellant declares, ‘it is effectively an operator of the hotels,

511 Id.
512 Id.
514 Id. at *2.
515 Id.
whether franchised or company owned/operated.”516 Plaintiff made the same argument with respect to Promus.

The court noted that agency is either “‘actual or ostensible.”517 “Under the common law doctrine of respondeat superior, a principal or employer is vicariously liable for the acts of an agent or employee committed in the course of employment.”518 “A franchisor may be vicariously liable if it has ‘complete or substantial control over the franchisee.”519 “However, the ‘mere licensing of trade names does not create agency relationships either ostensible or actual.”520 “Summary judgment is appropriate in favor of a franchisor when a franchised restaurant denies service to a disabled person with a service dog, if there is no evidence that the franchisor exercises control over the restaurant and its employees.”521 The court ultimately held that the plaintiff had abandoned his claim of actual agency on appeal.

With regard to the plaintiff’s claim for ostensible agency, the court noted that “[o]stensible agency rests on the doctrine of estoppel: ‘The essential elements are representations by the principal, justifiable reliance thereon by a third party, and change of position or injury resulting from such reliance. Before recovery can be had against the principal for the acts of an ostensible agent, the person dealing with an agent must do so with belief in the agent’s authority and this belief must be a reasonable one. Such belief must be generated by some act or neglect by the principal sought to be charged and the person relying on the agent’s apparent authority must not be guilty of neglect.”522 “The burden of proving ostensible agency is on the party asserting its existence.”523

The plaintiff’s claim of ostensible agency rested on the desk clerk’s “unawareness of whether or not he worked for Hilton,” which the plaintiff cited “as proof that ‘Plaintiff, and the public, logically believed the San Clemente hotel personnel were from Hilton.”524 When asked during his deposition whether he ever worked for Hilton Hotels Corporation the desk clerk answered “I worked for the Hampton Inn.... I don’t believe they were corporately owned. So I don’t know if I worked directly for them or not, to be honest with you.”525

Despite the desk clerk’s testimony, the plaintiff himself had “expressly denied that he selected the Inn in reliance upon respondents’ apparent ownership or management. Appellant entered the Inn without any prior planning; therefore, he did not telephone Hilton or Promus to make a reservation. Asked, ‘Why did you pick that particular hotel?’ appellant replied that ‘It was nice’ and ‘It was in San Clemente.’ Appellant was specifically asked, ‘So did you or did you not pick the hotel because it was associated with Hilton and Promus?’ Appellant answered ‘No.’ Similarly, in his declaration, appellant indicated that the only reason he went to the Inn was that it was down the street from the gas station where he purchased fuel: ‘After filling the vehicle up with gas we drove down the street toward the hotels. The Hampton Inn came up before the Travelodge, and it looked nicer than the Travelodge, so I pulled into the Hampton Inn parking

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516 Id. at *3.
517 Id.
518 Id.
519 Id. at *4.
520 Id.
521 Id.
522 Id. (Citations omitted).
523 Id.
524 Id.
525 Id. fn. 3.
Finally, the court disregarded a copy of a web page “showing that the Inn is ‘A proud member of the Hilton Family’” because “the date on the web page is 2008, two years after the incident in question,” thus, plaintiff “could not have relied on this web page when he selected the Inn.”

“Apart from a lack of reliance on [Hilton and Promus’] association with the Inn, appellant also fails to show what representations [they] made. ‘Ostensible agency cannot be established by the representations or conduct of the purported agent; the statements or acts of the principal must be such as to cause the third party to believe the agency exists.’” Plaintiff “does not list any representations or acts by the principal, in this case, Hilton. Instead, in his declaration in opposition to the motion for summary judgment, [plaintiff] pointed to his own beliefs, but not to any representations made by Hilton. He wrote, ‘I believed there was no way [Hilton] would discriminate against my brother and his service dog’ and ‘I thought Hilton had implemented new anti-discrimination policies at its hotels…. I reasonably believed Hilton had already taken steps to retrain its employees and put an end to the discrimination.’ The court found that “[w]e cannot extract from [plaintiff’s] personal expectations or hopes any misleading representations or acts by the principal that would cause [plaintiff] to believe that the Inn was its agent.”

The court concluded that “[a]bsent evidence that [the franchisee] and its employees were actual or ostensible agents of respondents, there is no vicarious liability.”

Similarly, in *Exposito et al. v. Hilton Hotels Corporation et al.*, the plaintiff sued a series of corporations and their executive officers, alleging, *inter alia*, that the defendants had conspired to discriminate against people traveling with service animals. The defendants moved for summary judgment and the trial court granted it.

With regard to the plaintiffs’ claim for violation of California’s Unruh Civil Rights Act, the Court found that Hilton’s corporate executives and in-house attorneys did not violate the Act in connection with the plaintiffs’ use of a service animal. The individual defendants presented evidence that they did not act in any way to prevent one of the individual’s guide dogs from acting as a guide dog for the individual, nor did they do anything to incite a denial of civil rights. The court rejected the plaintiffs’ argument that there was circumstantial evidence of company-wide discrimination to authorize the practice of turning away disabled persons with service dogs from the franchisor’s franchised hotels. Further, speculation presented by the two plaintiffs, based on “informal discovery” that the franchisor’s executives knew of the discrimination and concealed and destroyed complaints was insufficient to raise a triable issue of fact.

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526 Id. at *5.
527 Id.
528 Id.
529 Id.
530 Id.
531 Id.
533 Id.
534 Id.
535 Id.
536 Id.
The plaintiff had also asserted a claim against the defendants for an alleged incident at a franchised property in Rancho Cucamonga. The court noted that defendants submitted evidence that “the franchisor for this property was Promus Hotels, Inc., which is a subsidiary of Hilton Hotels Corporation” and evidence that “there was no agency relationship between Promus Hotels, Inc. and the Rancho Cucamonga hotel, because it did not own or operate the Rancho Cucamonga Homewood Suites; or have day-to-day control over the Rancho Cucamonga location.” The court rejected the declaration of plaintiffs’ counsel, who attested that “as a franchisor, Promus Hotels, Inc. exercised substantial control over its franchisee, thereby converting an independent contractor relationship into an agency relationship; and that despite the language in the Franchise License Agreements, Promus Hotels, Inc. could and did control its franchisees.” The court noted that plaintiffs’ attorney “does not have personal knowledge of the relationship and practices of Promus Hotels, Inc. and the Rancho Cucamonga franchisee, and thus, cannot attest to such facts.”

In Masters v. Tony Lin et al., the plaintiff alleged that while staying at the Moreno Valley Travelodge the owner and an employee of the Travelodge repeatedly tried to increase the room rate and told her to leave because of her signal dog. The plaintiff also filed suit against the owner and the franchisor, Forte Hotels, Inc., alleging that a representative of her employer had telephoned a Travelodge customer service line and was told that plaintiff could continue staying at the Travelodge for the rate originally quoted. The plaintiff asserted claims under the Americans with Disabilities Act and California Civil Code sections 54.1 and 54.2.

Forte moved to dismiss the plaintiff’s complaint on the ground that none of the plaintiff’s allegations supported a claim against it as a matter of law. The court noted that “[t]he specific issue before this court is whether in light of Forte’s alleged status as the franchisor/licensor of the Travelodge, plaintiff has alleged sufficient facts to show that Forte was ‘operating’ the Travelodge, a required element for defendant liability under the ADA, or that Forte retained to itself the right to control the Travelodge exceeding its legitimate interests, the necessary element for Forte to be liable under California law.”

The court noted that “[i]n order for a defendant to be liable under the ADA . . . the defendant must own, lease or operate a place of public accommodation.” The court noted that “[t]here are no allegations or even a suggestion that Forte owns or leases the Travelodge in question.” The plaintiff claimed that she had stated this element of her ADA claim because she had alleged that “Forte had ‘actual and/or apparent and ostensible authority’ to control the Travelodge and has ‘taken responsibility for insuring that the U.S. Travelodge franchisees comply with the [ADA],” pointing to two memoranda sent by Forte to its franchisees. The court noted that “[u]nless additional information would clarify their purpose, all these memoranda appear to do is provide basic information about the ADA to Forte franchisees and other persons. There is nothing in them to indicate that Forte was exerting such control over its franchisees with respect to the ADA that it could be said to be operating the Travelodge in question . . . .” The court also rejected the plaintiff’s claim that the customer service agent’s
statements supported her claim that Forte maintained authority of the Travelodge’s compliance with the ADA, noting that there was nothing in the agent’s statement which indicates that Forte was operating the Travelodge in question. 545

With regard to plaintiff’s state law claims, the court noted that plaintiff “does not allege facts indicating that Forte directly participated in any of the acts which form the bases for these claims.” 546 Further, “California courts have consistently held that a franchisor has no vicarious liability for the acts of its franchisee unless the franchisor ‘has the right to control the means and manner in which the result is achieved’ in the operation of the franchise.” 547 The court found that “[i]n the case at hand, plaintiff has not alleged facts indicating that Forte retained the right to assert complete or substantial control over the day-to-day operations of the subject Travelodge. Absent allegations that Forte retained such power, plaintiff cannot state a claim against Forte based on its liability for the alleged acts of [the franchisee and its employee].” 548

The court granted Forte’s motion to dismiss with leave to amend, noting that “[w]hether Forte was in fact ‘operating’ the Travelodge (with respect to the first claim for violation of the ADA) or whether Forte in fact retained to itself the right to control Travelodge’s daily operations) with respect to plaintiff’s state-law claims) are issues which ultimately cannot be determined except by summary judgment.” 549 The Court’s docket indicates that the Court later denied a motion by Forte to dismiss the plaintiff’s amended complaint, however, Forte later prevailed on summary judgment.

The lessons to be learned from cases where a franchisor has been sued as a result of an alleged violation that occurred at a franchised property appear to be that: (1) under the ADA a franchisor likely will not be found to be liable as it ordinarily does not own, lease or operate the location; and (2) depending on the language of the particular state statute, a franchisor may be found to be vicariously liable for the acts of a franchisee. Although franchisors generally require that their franchisees comply with all laws, including laws related to service animals, exerting too much control may leave the franchisors open to lawsuits from persons who are denied access. For example, implementing a training program that is utilized by all franchisees may leave the franchisor open to a claim that it was ultimately responsible for the negligent training of a franchisee’s employee who turned away a guest with a service animal. In addition, although no court has yet accepted this argument, a plaintiff may attempt to impose liability on a franchisor by claiming ostensible agency, i.e., that he/she chose a particular establishment because he/she believed it was being run by the franchisor and believed that the franchisor would not discriminate against him/her. One potential way for franchisors to alleviate this problem may be to ensure that their franchisees post conspicuous signs stating that the location is independently owned and operated by the franchisee. Although no court has yet accepted these arguments, they also have not foreclosed the possibility that a franchisor may be vicariously liable for the acts of its franchisees.

c. Penalties for Non-Compliance

The penalties for non-compliance with laws related to service animals vary greatly depending on the state. More than half of the states with service animal laws have made it a

545 id.
546 id.
547 id.
548 id.
549 id.
misdemeanor to deny access to a disabled person traveling with a service animal.\textsuperscript{550} Maine has actually declared that any violation of its statute is a “strict liability” crime. In addition to jail time, statutory fines may be imposed on those found to have violated a particular state’s statute. The cost of a violation could rise astronomically because several states provide that, in addition to statutory fees, attorneys’ fees expended in pursuing a civil action are recoverable by the plaintiff. The attorneys’ fees provision in state statutes has dramatically increased litigation relating to service animal laws, as the plaintiff’s attorney is assured of recovering his/her fees even if the statutory penalty is not very large.

IV. CONCLUSION

Franchising operates in approximately 75 industries, and the business laws and regulations that may affect franchised businesses, including franchisors and franchisees, are numerous and diverse. The discussion above touches on but a small number of these laws. In some cases, the overlapping federal and state laws are too numerous to catalog in this paper. But, a franchise lawyer -- for a franchisor or franchisee, in-house or outside counsel – should become aware of the types of laws that may affect his/her clients’ business and how they may impact those businesses, from potential liability to third parties, franchisor vicarious liability, risks to the brand goodwill, the impact on training and ongoing operations, and FDD disclosures. The discussion above and the appendices are intended as a launching point for additional research and/or in state-specific analysis of these laws and regulations.

\textsuperscript{550} These states include but are not limited to Alabama, California, Connecticut, Delaware, Florida, Georgia, Idaho, Illinois, Indiana, Louisiana, Maryland, Michigan, Minnesota, Missouri, Montana, New Hampshire, New Mexico, North Carolina, North Dakota, Oklahoma, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Virginia, West Virginia and Wyoming.
Appendix A

Examples of Alcohol Beverage Licenses

Sample: List of Various Liquor Licenses and Fees from Two Jurisdictions
(New York State Liquor Authority and Montgomery County Maryland)

New York, State Liquor Authority

Effective May 3, 2002 the retail and seasonal license fee schedules provided in the retail application on pages VIII and IX of the instructions will reflect changes in fee categories for four New York State cities. Many of the retail license fees are based on population figures, with a graduated four or two tiered scale. The year 2000 census was recently certified, and population declines in the upstate cities of Albany, Troy and Binghamton have dropped license fees for those cities into the next lower category.

**SCHEDULE OF RETAIL LICENSE FEES**

<table>
<thead>
<tr>
<th>Code</th>
<th>License Class</th>
<th>Length (years)</th>
<th>Location</th>
<th>Filing Fee</th>
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**Note:** Filing fees are in addition to the retail license fees.
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<th>Code</th>
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<td>Wine Winter Club</td>
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<td>Wine Winter Tavern</td>
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<td><strong>Wine (includes Beer)</strong></td>
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<td><strong>Liquor - Private Golf Club (includes Wine &amp; Beer)</strong></td>
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</table>

1221633v-6
Montgomery County Maryland, Department of Liquor Control
Class of Licenses

CLASS A Wine License

Light Wine, Class A, Off-Sale Only, from 6:00 a.m. to 1:00 a.m. including Sundays.

ANNUAL LICENSE FEE: $100 - OFF-SALE ONLY - DOES NOT REQUIRE BATHROOMS OR SEATING - NO ON-PREMISES CONSUMPTION ALLOWED

CLASS A Beer/Wine License

Beer & Light Wine, Class A, Off Sale, from 6:00 a.m. to 1:00 a.m. including Sundays.

ANNUAL LICENSE FEE: $250 - OFF SALE ONLY - DOES NOT REQUIRE BATHROOMS OR SEATING - NO ON-PREMISES CONSUMPTION ALLOWED

CLASS B Beer/Wine

Beer & Light Wine, Class B, On-Sale, Hotels and Restaurants, from 9:00 a.m. to 1:00 a.m., Sunday from 10:00 a.m. to 1:00 a.m. for On Sale. Off-Sale, every day from 6:00 a.m. to 1:00 a.m.

ANNUAL LICENSE FEE: $400 - ON AND OFF SALE PRIVILEGES - REQUIRES BATHROOMS FOR BOTH SEXES AND MINIMUM SEATING FOR 30 PATRONS.

CLASS B Beer/Wine/Liquor

Beer, Wine and Liquor, Class B, On-Sale, Hotels and Restaurants, from 9:00 a.m. to 1:00 a.m. Friday and Saturday sales to 2:00 a.m., Sunday from 10:00 a.m. to 1:00 a.m. No Off-Sale.

ANNUAL LICENSE FEE: $2500 - ON-SALE ONLY - NO ALCOHOL MAY LEAVE THE LICENSED PREMISES (except if a catering privilege is secured) - REQUIRES BATHROOMS FOR BOTH SEXES AND MINIMUM SEATING FOR 30 PATRONS. MUST MEET MINIMUM RATIO REQUIREMENT OF 50% FOOD TO 50% ALCOHOL. REQUIRED TO FILE RATIO REPORTS FOR THE FIRST 12 MONTHS OF OPERATION.

Beer, Wine and Liquor, Class B (H-M), On-Sale, Hotels and Motels, from 9:00 a.m. to 1:00 a.m., Friday and Saturday sales to 2:00 a.m., Sunday from 10:00 a.m. to 1:00 a.m. No Off-Sale.
Beer, Wine, and Liquor, Class B, On-Sale, Hotel-Conference Center, from 9:00 a.m. to 1:00 a.m., Friday and Saturday sales to 2:00 a.m., Sunday from 10:00 a.m. to 1:00 a.m. No Off-Sale

ANNUAL LICENSE FEE: $2,500 - IN ADDITION TO THE ABOVE, A CLASS B, BWL, HOTEL/MOTEL LICENSE REQUIRES 3 FLOORS, AN ELEVATOR, 100 ROOMS, DINING ROOM WITH SEATING FOR 125, AND KITCHEN FACILITIES.

SPECIAL CLASS B

Beer/Wine/Liquor Performing Arts Facility
Beer, Wine and Liquor, Class B, Performing Arts, from 10:00 a.m. to 2:00 a.m. Monday through Sunday.

ANNUAL LICENSE FEE: $1,000 - ON-SALE ONLY - FOR USE BY A NOT-FOR-PROFIT PARTNERSHIP, LIMITED LIABILITY COMPANY, CORPORATION, OR OTHER ENTITY THAT LEASES THE PERFORMING ARTS FACILITY TO HOST ARTISTIC, CORPORATE, AND COMMUNITY-RELATED ACTIVITIES. THE PERFORMING ARTS FACILITY MUST HAVE: (1) A MINIMUM CAPITAL INVESTMENT, NOT INCLUDING REAL PROPERTY, OF $1,000,000; (2) A MINIMUM CAPACITY OF 2,000 PERSONS; AND (3) A FOOD SERVICE FACILITY PERMIT AND 30 SEATS IN A FOOD SERVICE AREA.

SPECIAL B-K Beer/Wine Kensington

Beer and Light Wine, Class B-K, On-Sale, Restaurants, from 9:00 a.m. to 1:00 a.m.; Sunday from 10:00 a.m. to 1:00 a.m. No Off Sale. NOTE: May not serve alcoholic beverages after 11:00 p.m. if located in certain commercial areas.

ANNUAL LICENSE FEE: $400 – ON-SALE ONLY - REQUIRES BATHROOMS FOR BOTH SEXES AND MINIMUM SEATING FOR 40 PATRONS. MUST MEET MINIMUM RATIO REQUIREMENT OF 50% FOOD TO 50% ALCOHOL. THE FOOD RATIO PERCENTAGE CANNOT INCLUDE CARRYOUT FOOD. REQUIRED TO FILE RATIO REPORTS FOR THE FIRST 12 MONTHS OF OPERATION.

SPECIAL B-K Beer/Wine/Liquor Kensington

Beer, Wine and Liquor, Class B-K, On-Sale, Restaurants, from 9:00 a.m. to 1:00 a.m. Friday and Saturday sales to 2:00 a.m., Sunday from 10:00 a.m. to 1:00 a.m. No Off-Sale. NOTE: May not serve alcoholic beverages after 11:00 p.m. if located in certain commercial areas.

ANNUAL LICENSE FEE: $2,500 - MUST BE LOCATED WITHIN CERTAIN SPECIFIC AREAS OF THE TOWN OF KENSINGTON, MARYLAND. NO ALCOHOL MAY LEAVE THE LICENSED PREMISES - REQUIRES BATHROOMS FOR BOTH SEXES AND MINIMUM SEATING FOR 30 PATRONS. MUST MEET MINIMUM RATIO REQUIREMENT OF 50% FOOD TO 50% ALCOHOL. THE FOOD RATIO PERCENTAGE CANNOT INCLUDE CARRYOUT FOOD. REQUIRED TO FILE RATIO REPORTS FOR THE FIRST 12 MONTHS OF OPERATION.

CLASS C Beer/Wine/Liquor Fraternal/Veteran

Beer, Wine and Liquor, Class C, Clubs, from 6:00 a.m. to 2:00 a.m., Sunday from 10:00 a.m. to 2:00 a.m. No Off-Sale.

ANNUAL LICENSE FEE: $1000 - ON-SALE ONLY - NO ALCOHOL MAY LEAVE THE LICENSED PREMISES - ISSUED TO ELEEMOSYNARY GROUPS HAVING A NATIONAL MEMBERSHIP AND AT LEAST 200 LOCAL MEMBERS.
WHO PAY ANNUAL DUES - FOR USE BY MEMBERS AND BONA FIDE GUESTS - NOT OPEN TO THE GENERAL PUBLIC - BATHROOMS FOR BOTH SEXES REQUIRED - NO MINIMUM SEATING REQUIRED.

CLASS C Beer/Wine/Liquor Country Clubs

Beer, Wine and Liquor, Class C. Country Clubs, from 6:00 a.m. to 2:00 a.m., Sunday from 10:00 a.m. to 2:00 a.m. No Off-Sale.

ANNUAL LICENSE FEE: $2000 - ON-SALE ONLY - NO ALCOHOL MAY LEAVE THE LICENSED PREMISES - ISSUED TO COUNTRY CLUB HAVING A 9 OR 18-HOLE GOLF COURSE (OR SWIMMING/TELENISS IN LIEU THEREOF); 100 OR MORE MEMBERS PAYING ANNUAL MINIMUM DUES OF $50.

CLASS C Beer/Wine/Liquor Consumption

Beer & Light Wine, Class C, Clubs, On-Sale Only, from 11:00 a.m. to 12 midnight. Sunday from 10:00 a.m. to 12 midnight. No Off-Sale.

ANNUAL LICENSE FEE: $300 - THERE ARE ONLY 2 CONSUMPTION LICENSES IN MONTGOMERY COUNTY (DAMASCUS/ Cabin John) - THESE ARE BOTH FRATERNAL/VETERAN ORGANIZATIONS. SALES OF ALCOHOLIC BEVERAGES ARE PROHIBITED. LIMITED TO CONSUMPTION ON THE LICENSED PREMISES ONLY.

CLASS C Beer/Wine/Liquor Continuing Care Retirement Community

Beer, Wine, & Liquor, Class C, Continuing Care Retirement Community, from 6:00 a.m. to 2:00 a.m., Sunday 10:00 a.m. to 2:00 a.m. - No Off Sale.

ANNUAL LICENSE FEE: $500 - IS ISSUED TO A CLUB THAT: (1) IS COMPOSED OF RESIDENTS OF A CONTINUING CARE RETIREMENT COMMUNITY THAT HAS OBTAINED A CERTIFICATE OF REGISTRATION FROM THE STATE DEPARTMENT OF AGING UNDER ARTICLE 70B, SECTION 11 OF THE MARYLAND CODE; (2) HAS AT LEAST 50 BONA FIDE MEMBERS; AND (3) HAS ANNUAL DUES THAT AVERAGE AT LEAST $5 PER MEMBER.

CLASS D Beer/Wine On Sale Generally On/Off Sale

Beer & Light Wine, Class D, On-Sale Generally, from 9:00 a.m. to 1:00 a.m., Sunday from 10:00 a.m. to 1:00 a.m. for On-Sale. Off-sale, every day from 6:00 a.m. to 1:00 a.m.

ANNUAL LICENSE FEE: $400 - ON AND OFF-SALE PRIVILEGES - REQUIRES BATHROOMS FOR BOTH SEXES, NO MINIMUM SEATING REQUIREMENTS.

CLASS H Beer

Beer, Class H, Hotels and Restaurants, On-Sale Only, from 9:00 a.m. to 1:00 a.m., Sunday from 10:00 a.m. to 1:00 a.m. No Off Sale.

ANNUAL LICENSE FEE: $400 - ON-SALE ONLY - REQUIRES BATHROOMS FOR BOTH SEXES AND MINIMUM SEATING FOR 30 PATRONS.

CLASS H Beer/Wine

Beer & Light Wine, Class H, Hotels and Restaurants, On-Sale Only, from 9:00 a.m. to 1:00 a.m., Sunday from 10:00 a.m. to 1:00 a.m. No Off-Sale.

ANNUAL LICENSE FEE: $400 - ON-SALE ONLY - REQUIRES BATHROOMS FOR BOTH SEXES AND MINIMUM SEATING FOR 30 PATRONS.
CLASS CAT Beer/Wine/Liquor Caterer’s

ANNUAL LICENSE FEE: $1250 - LICENSE ISSUED TO CATERING COMPANIES LOCATED IN MONTGOMERY COUNTY - PERMITS THE CATERING OF ALCOHOL FOR EVENTS HELD IN MONTGOMERY COUNTY. THE CATERER MUST HAVE A SIGNED CONTRACT FOR THE SALE OF FOOD AND ALCOHOL, AND MUST BE PRESENT AT THE CATERED EVENT TO SERVE THE FOOD AND ALCOHOL.

SPECIAL THEATER Beer/Wine

Beer & Light Wine, Special Theater, On-Sale Only, Alcoholic beverage sales permitted when snacks are served, one hour before and after a performance, and receptions before and after a performance.

ANNUAL LICENSE FEE: $100 - ON-SALE ONLY - ISSUED TO A PERFORMING ARTS THEATER, OR A MOVIE THEATER OPERATED BY A BONA-FIDE NON-PROFIT ORGANIZATION.

Source: Montgomery County Maryland, Department of Liquor Control Class of Licenses, http://www.montgomerycountymd.gov/retmpl.asp?url=/content/DLC/liquor/LRE/lic_classes.asp/
## Appendix B *

Dram Shop Liability by State

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<tr>
<th>STATE</th>
<th>SECTION CITE</th>
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<tbody>
<tr>
<td>Alabama</td>
<td>ALA. CODE §§ 6-5-70 through 6-5-72</td>
</tr>
<tr>
<td>Alaska</td>
<td>ALASKA STAT. § 04.21.020</td>
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<td>Arizona</td>
<td>ARIZ. REV. STAT. §§ 4-301 through 4-312</td>
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<td>Arkansas</td>
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<td>California</td>
<td>CAL. BUS. &amp; PROF. CODE §§ 25602 through 25602.</td>
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<td>Colorado</td>
<td>COLO. REV. STAT. §§ 12-47-801, 13-21-103</td>
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<td>Connecticut</td>
<td>CONN. GEN. STAT. § 30-102</td>
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<td>Florida</td>
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<td>Georgia</td>
<td>GA. CODE ANN. § 51-1-40</td>
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<td>Hawaii</td>
<td>HAW. REV. STAT. §§ 663-41 through 663-42</td>
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<tr>
<td>Idaho</td>
<td>IDAHO CODE § 23-808</td>
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<td>Illinois</td>
<td>235 ILL. COMP. STAT. 5/6-21</td>
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<td>Indiana</td>
<td>IND. CODE ANN. §§ 7.1-5-7-8, 7.1-5-10-15.5</td>
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<td>IOWA CODE § 123.92</td>
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<td>Kentucky</td>
<td>KY. REV. STAT. § 413.241</td>
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<td>ME. REV. STAT. tit. 28-A §§ 2501 through 2516</td>
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<td>MASS. GEN. LAWS ch. 231, § 85T</td>
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<td>N.C. GEN. STAT. §§ 18B-120 through 18B-12B</td>
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<td>N.D. CENT. CODE § 5-01-06.1</td>
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<td>47 PA. STAT. § 4-497</td>
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<td>S.D. CODIFIED LAWS §§ 35-4-78, 35-11-1</td>
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<td>Tennessee</td>
<td>TENN. CODE ANN. §§ 57-10-101 through 57-10-102</td>
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<td>Texas</td>
<td>TEX. ALCO. BEV. CODE §§ 2.01 through 2.03</td>
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<td>Utah</td>
<td>UTAH CODE ANN. §§ 32A-14a-101 through -105</td>
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<td>Vermont</td>
<td>VT. STAT. ANN. tit. 7, §§ 501 - 504</td>
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<td>Wyoming</td>
<td>WYO. STAT. § 12-8-301</td>
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States without Dram Shop Laws

- Delaware
- District of Columbia
- Kansas
- Louisiana
- Maryland
- Oklahoma
- South Carolina
- Virginia
- Washington
- West Virginia

Notes:

a. Most of the state laws address liability to third parties for furnishing alcohol to (a) intoxicated adults or (b) intoxicated minors. See, for example, Pennsylvania. Some states limit the liability to injured third parties to sales to intoxicated minors, but do not impose liability with respect to alcohol sales to adults. See, e.g., California. Some states impose liability if the alcohol is furnished to an intoxicated adult or furnished to a minor (even if the minor was not intoxicated before receiving the alcohol). See, for example, Tennessee. The reader should review the statutes, regulations and case law to determine the applicability and scope of each state’s law.

b. Some states may not have a dram shop law that expressly imposes liability on sellers or furnishers of alcoholic beverages. Some states may have statutes or regulations that may be considered “anti-dram shop” legislation that provides immunity to sellers and/or social hosts for selling or furnishing alcoholic beverages. See, e.g., Louisiana, LA. REV. STAT. ANN § 9:2800.1 (2010). Also, an anti-dram shop law may provide immunity, or a limitation on damages, for furnishing alcohol to individuals “of age,” but the law is silent as to alcohol sales to minors (see LA. REV. STAT. ANN § 9:2800.1). In those cases, a seller may be liable for injuries caused by the underage drinker.

* See note 165 supra for discussion of the sources for, and limitations of, the data in this Appendix. Lexis Nexis prepares, and makes available for a fee, a 50 State Comparative Chart entitled, Dram Shop Liability, see www.lexis.com.
Appendix C

Sample Limited Warranty

LIMITED WARRANTY

ABC Company warrants that its widgets will be free from defects in materials and workmanship for 1 year from the date of purchase. This warranty does not extend to anyone except the first purchaser at retail.

ANY IMPLIED WARRANTIES WHICH THE BUYER MAY HAVE ARE LIMITED IN DURATION TO 1 YEAR FROM THE DATE OF PURCHASE. Some states do not allow limitations on how long an implied warranty lasts, so the above limitation may not apply to you.

At its option, ABC Company will repair or replace, or refund the purchase price of, any widget which is defective or fails to conform with this warranty under normal use and service within 1 year from the date of purchase. Contact ABC Company at the address listed below to obtain service under this warranty.

Repair or replacement of a defective widget, or refund of the purchase price, shall be the sole remedy of the purchaser under this warranty, and in no event shall ABC Company be liable for incidental or consequential damages. Some States do not allow the exclusion or limitation of incidental or consequential damages, so the above limitation or exclusion may not apply to you.

No agent, representative, dealer or unauthorized employee of ABC Company has the authority to increase or alter the obligations of this warranty.

This warranty gives you specific legal rights, and you may also have other rights which vary from State to State.

ABC Company
[Address]
[Phone]
[E-mail address]
Appendix D

State Limitations On Disclaimers
Of Implied Warranties

1. **Ala. Code §7-2-316(5):**

   Alabama adopted U.C.C. §2-316, but adds a provision (subsection (5)) which provides that nothing in the section will “limit or exclude the seller's liability for damages for injury to the person in the case of consumer goods”. Consumer goods are goods which are "used or bought for use primarily for personal, family or household purpose.” (Ala. Code §7-9A-102(23).

2. **Cal. Commercial Code §2316:**

   California adopted U.C.C. § 2-316.

   **Cal. Civ. Code § 1793.**

   In Section 1793 of its Civil Code, California prohibits manufacturers, distributors or retailers of consumer goods from limiting, modifying, or disclaiming implied warranties in cases where express warranties are given. "Consumer goods" are defined in Section 1791 as "any new product or part thereof that is used, bought, or leased for use primarily for personal, family, or household purpose, except for clothes and consumables." "Consumer goods" includes new and used assistive devices sold at retail.


   Connecticut adopted U.C.C. §2-316 but adds a provision (subsection (5)) providing that subsections (2), (3) and (4) do not apply to sales of new or unused consumer goods, except those marked “irregular”, “factory seconds” or “damaged”. Any language, oral or written, used by a seller or manufacturer of consumer goods to exclude or modify the implied warranties of merchantability or fitness or the remedies for breach of those warranties is unenforceable.

4. **D.C. Stat. §28: 2-316:**

   The District of Columbia adopted U.C.C. §2-316.

   **D.C. Stat. §28: 2-316.01:**

   The District of Columbia added a section which declares §2-316 not applicable to the sale of consumer goods, and makes unenforceable any attempt by a seller of consumer goods to exclude or modify any implied warranties of merchantability or fitness by a manufacturer of consumer goods to limit or modify a consumers remedies for breach of the manufacturer's express warranty. However, this provision does not apply to particular defects and limitations noted conspicuously in writing at the time of sale. "Consumer goods" is defined in §28: 9-109(1) as goods which are "used or bought for use primarily for personal, family, or household purposes."


   Kansas adopted U.C.C. 2-316.

In the Kansas Consumer Protection Act regarding consumer transactions, Kansas prohibits suppliers from excluding, modifying, or attempting to limit the implied warranties of merchantability and fitness for a particular purpose, and no action for breach of warranty can fail because of a lack of privity. The act, however, allows for this limiting implied warranties if the consumer had knowledge of the defect, and that knowledge became the basis for the bargain. A disclaimer or limitation in violation of the section is void. If the consumer prevails in a breach of action case, and the supplier violated this provision, the court can award attorney's fees and a civil penalty.

"Consumer transaction" is defined in K.S.A. 50-624(c) as "a sale, lease, assignment or other disposition for value of property or services within this state (except insurance contracts regulated under state law) to a consumer; or a solicitation by a supplier with respect to any of these dispositions."


Maine adopted U.C.C. §2-316. However, Maine adds a provision (subsection (5)) which declares subsection (2) not applicable to the sale of consumer goods or services. Any language used by a seller or manufacturer of consumer goods which attempts to exclude or modify any implied warranties of merchantability or fitness or the remedies for breach of those warranties is unenforceable. Consumer goods and services are new or used goods and services used or bought primarily for personal, family or household purposes. A violation of this provision arising from the retail sale of consumer goods and services is a violation of the Uniform Trade Practices Act.


Maryland adopted U.C.C. §2-316.

Md. Ann. Code §2-316.1:

Maryland adds §2-316.1 which declares §2-316 not applicable to the sale of consumer goods, services or both. Any oral or written language by the seller of consumer goods and services which attempts to exclude or modify any implied warranties of merchantability and fitness for a particular purpose or the remedies for breach of those warranties is unenforceable. Any oral or written language by a manufacturer of consumer goods which attempts to limit or modify a consumer's remedies for breach of the manufacturer's express warranties is also unenforceable, unless the manufacturer provides reasonable and expeditious means of performing the warranty obligation. "Consumer goods" are defined in Section 9-109(23) as "goods that are used or bought for use primarily for personal, family, or household purposes."


Massachusetts adopted U.C.C. §2-316.


Massachusetts added §2-316A which declares §2-316 not applicable to the sale of consumer goods, services or both. Any language by a seller or manufacturer of consumer
goods which attempts to exclude or limit the implied warranties of merchantability and fitness for a particular purpose, or to exclude or modify remedies for the breach of those warranties, is unenforceable. Any language used by a manufacturer of consumer goods which attempts to limit or modify a consumer’s remedies for breach of the manufacturer’s express warranties is unenforceable unless the manufacturer has facilities in the state to provide reasonable and expeditious performance of the warranty obligations.


All consumer sales of goods are accompanied in Minnesota by implied warranties of merchantability or fitness for a particular purpose, unless disclaimed conspicuously with "as is" language. A seller may limit damages or remedies for breach of implied warranties, however.


Minnesota also prohibits any express warranties arising out of a consumer sale of new goods from disclaiming implied warranties of merchantability or, where applicable, fitness.


Mississippi did not adopt U.C.C. §2-316. However, 75-2-315.1(1) provides that any language used by a seller of consumer goods and services which attempts to exclude or modify any implied warranties or merchantability and fitness for a particular purpose, or to exclude or modify the consumer's remedies for breach of those warranties, is unenforceable. However, the seller can recover from the manufacturer any damages resulting from breach of the implied warranties. In addition, §75-2-719(4) prohibits any limitations of remedies for breaches of an implied warranty of merchantability or fitness for a particular purpose.


New Hampshire adopted U.C.C. §2-316. However, New Hampshire adds a new subsection (4) which disallows disclaimers of the warranties of merchantability or fitness in cases in which goods are purchased primarily for personal, family or household use and not for commercial or business use, unless the merchant seller provides the buyer with a conspicuous writing which clearly informs the buyer, prior to or at the time of sale, that the sale is on an "as is" basis and other disclosures, and the writing is signed by the buyer prior to or at the time of sale.

12. Or. Rev. Stat. §§72.8020, 72.8030 and 72.8050:

Sections 72.8020 and 72.8030 provide that a manufacturer of consumer goods to be sold at retail gives an implied warranty of merchantability or fitness unless the warranty is disclaimed by making an "as is" sale with a conspicuous writing attached to the consumer good as provided in Section 72.8050.

Section 72.8010(1) defines "consumer good" as a new consumer good defined in 79.1090(1) and includes products “used or bought for use primarily for personal, family or household purposes.” Section 79.0102(w) defines “consumer goods” as “goods that are used or bought for use primarily for personal, family or household purposes.”
13. **R.I. Gen. Laws §6A-2-316:**

Rhode Island adopted UCC §2-316.

**R.I. Gen. Laws §6A-2-329.**

Rhode Island added a new section which stipulates that no express warranty arising out of a consumer sale of new goods can disclaim implied warranties of merchantability or, where applicable, fitness. In addition, unless disclaimed by an "as is" sale, every consumer sale is accompanied by an implied warranty of merchantability and, where applicable, fitness. "Consumer sale" means a sale of new goods or, as regards an express warranty, any goods purchased primarily for personal, family or household purposes.


Vermont adopted U.C.C. §2-316. However, Vermont added subsection (5) which declares that subsection (2) does not apply to the sale of new or unused consumer goods or services. Any language used by a seller or manufacturer of consumer goods or services to exclude or modify the implied warranties of merchantability or fitness, or the consumer's remedies for breach of those warranties, is unenforceable.


Washington adopts U.C.C. §2-316. However, Washington amended subsection (4) to provide that, notwithstanding subsections (2) and (3), disclaimers of the warranties of merchantability or fitness in cases where goods are purchased primarily for personal, family or household use and not for commercial or business use are not effective to limit the liability of merchant sellers, unless the disclaimer sets forth with particularity the qualities and characteristics not being warranted. Remedies for breach of warranty can still be limited.

16. **W.Va. Code §46A-6-107:**

The West Virginia General Consumer Protection statute stipulates that in a consumer transaction no merchant can exclude, modify, or limit any warranty, express or implied, or any remedy for the breach of those warranties. Any such exclusion, modification or attempted limitation is void. "Consumer transaction" is defined in §46A-6-102(2) as "a sale or lease to a natural person or persons for personal, family, household or agricultural purpose."
Appendix E

State Laws on Dealer Reimbursement
For Warranty Work

1. **Cal. Civil Code §§ 1793.5, 1793.6**

   California Civil Code § 1793.5 stipulates that if a manufacturer which sells goods with express warranties within the state and not provide authorized service and repair facilities within the state will be liable to the retailer who incurs obligations in giving effect to the manufacturer’s warranties "in an amount equal to that which would be received by the retail seller for like service rendered to retail consumers who are not entitled to warranty protection."

   California Civil Code § 1793.6 provides that every manufacturer who sells consumer goods in California under express warranty shall be liable to every independent serviceman performing services in giving effect to the express warranty, whether the independent serviceman is acting as an authorized service or repair facility designated by the manufacturer, or as an independent serviceman. The amount of the liability is an amount equal to the actual and reasonable costs of the service and repair, including costs for parts, transportation and a reasonable profit. "It shall be a rebuttable presumption affecting the burden of producing evidence that the reasonable cost of service or repair is an amount equal to that which is charged by the independent serviceman for like services or repairs rendered to service or repair customers who are not entitled to warranty protection."


   Connecticut General Statute § 42-110w provides that any manufacturer making an express warranty with respect to receiving equipment for personal, family or household purposes who designates a service representative to honor the terms of the warranty must reimburse its representative for work done under the warranty for "the amount charged by such service representative for services and repairs, including parts and labor, to customers who are not covered by any warranty protection." Section 20-342(7) defines “receiving equipment” as “television or radio receiving apparatus and associated components, including, but not limited to, antenna receiving systems, phonographs, tape recorders and audiovisual equipment”.


   Minnesota Stats. Ann. § 325G.19(3) provides that "Every manufacturer who makes an express warranty pursuant to a consumer sale, who authorizes a retail seller within this state to perform services or repairs under the terms of the express warranty shall be liable to the retail seller in an amount equal to that which is charged by the retailer seller for like service of repairs rendered to retail consumers who are not entitled to warranty protection."

4. **Or. Rev. Stat. §72.8130**

   Oregon Statute § 72.8130 provides that each manufacturer who, with respect to a consumer good sold within this state, makes an express warranty but does not provide a service or repair facility within this state is liable to the retail seller (i) when there is a replacement, for the cost of the replaced goods, transportation and reasonable handling charge, and (2) when there are services or repairs in accordance with the warranty, an amount equal to that which would be received by the retail seller for like service rendered to a retail consumer who is not
entitled to warranty protection, including actual and reasonable costs of the service and repair, transportation and a reasonable profit.

5. **RI. Gen. Laws §6A-2-329**

Rhode Island's Uniform Commercial Code § 6A-2-329(3)(d) provides that "every manufacturer who makes an express warranty pursuant to a consumer sale and who designates a representative within this state to provide sale and service under the terms of the express warranty, shall be liable to the representative in the amount equal to that which is charged by the representative for like service and repairs rendered to retail consumers who are not entitled to warranty protection. This equality of charges shall apply to both labor and parts used."


West Virginia Code § 46A-6-108 provides that if the manufacturer is bound to honor a warranty, "if the goods have been replaced or repaired by the merchant or a repairperson, as the case may be, such merchant, repairperson or consumer, in addition to any other remedy provided by law, shall have a cause of action against the manufacturer for the reasonable costs of such replacement or repair."
Appendix F

Summary of the FTC's Telemarketing Sales Rule

as reprinted from
the FTC's “Facts for Business – Complying with the Telemarketing Sales Rule”

“Briefly stated, the amended TSR:

– supplements the company-specific Do Not Call provision of the original Rule with new provisions based on a National Do Not Call Registry.
– creates an "established business relationship" exception to the National Do Not Call provisions so that a company may call a consumer with whom it has such a relationship, even if the consumer's number is on the Registry.
– allows a company to call a consumer who has given the company express written permission to call, even if the consumer's number is on the Registry.
– prohibits denying or interfering with a consumer's Do Not Call request.
– prohibits misuse of Do Not Call lists.
– covers charitable solicitations placed by for-profit telefunders. (The National Do Not Call Registry provisions do not apply to for-profit telefunders; rather, for-profit telefunders must keep their own Do Not Call lists and honor call recipients' requests not to be called.)
– requires sellers and telemarketers to obtain express verifiable authorization when payment is made by methods other than credit card or debit card, and limits the use of the written confirmation method.
– requires sellers and telemarketers offering credit card loss protection plans to disclose specific information.
– prohibits misrepresentations in the sale of credit card loss protection plans.
– requires sellers and telemarketers making an offer that involves a negative option feature to disclose specific information.
– prohibits misrepresentations about negative options.
– specifies that all required disclosures be made truthfully.
– requires additional disclosures for prize promotions.
– prohibits disclosing or receiving, for consideration, unencrypted consumer account numbers.
– requires sellers and telemarketers to get a consumer's express informed consent before submitting the consumer's billing information for payment.
– sets out guidelines for what constitutes evidence of express informed consent in transactions involving "pre-acquired account information" and "free-to-pay conversion" offers.
– requires telemarketers, for purposes of Caller ID, to transmit the telephone number, and, when made available by the telemarketer's telephone company, the telemarketer's name.
– prohibits telemarketers from abandoning any outbound telephone call, subject to a safe harbor.
– prohibits telemarketing calls placed on and after September 1, 2009, that deliver prerecorded messages, whether answered in person by a consumer or by an answering machine or voicemail service, unless the seller has previously obtained the call recipient's
written and signed agreement (which may be obtained electronically under the E-Sign Act) to receive such calls.

– requires any permitted prerecorded message telemarketing call that could be answered in person by a consumer to include an automated interactive opt-out mechanism available at all times during the message.

– requires any permitted prerecorded message telemarketing call that could be answered by an answering machine or voice mail service to include a toll-free telephone number that enables the call recipient to call back and connect directly to an automated opt-out mechanism.

– exempts from the written agreement requirement of the amendment charitable solicitation calls placed by for-profit telemarketers (“telefunders”) that deliver prerecorded messages on behalf of non-profits to members of, or previous donors to the non-profit, but requires that such calls include a prompt keypress or voice-activated opt-out mechanism.

– exempts healthcare-related prerecorded message calls that are subject to the Health Insurance Portability and Accountability Act of 1996 from the prohibition on telemarketing calls that deliver prerecorded messages.

– extends the applicability of most provisions of the Rule to “upselling.”

– requires telemarketers and sellers to maintain records of express informed consent and express agreement.

– narrows certain of the original TSR’s exemptions.

– clarifies that facsimile transmissions, electronic mail, and similar methods of delivery are direct mail for purposes of the direct mail exemption.”

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## Summary of State Do Not Call Regulations

### Alabama
- **State**: Alabama
- **Type**: Federal
- **Posted**: As per FTC Rules
- **Updated**: As per FTC List
- **Enrollment**: No
- **DMA List**: No
- **Webpage**: [http://www.psc.state.al.us/notcall/](http://www.psc.state.al.us/notcall/)
- **Calling Hour Restrictions**: 8:00AM - 9:00PM on no Sundays or holidays
- **Penalties**: $2,000 per infringement

DNC List effective as of 7/1/2000. AL has adopted FTC list as official state list. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to [www.co.regulatoryguide.com](http://www.co.regulatoryguide.com).

### Alaska
- **State**: Alaska
- **Type**: Federal
- **Posted**: As per FTC Rules
- **Updated**: As per FTC List
- **Enrollment**: No
- **DMA List**: No
- **Webpage**: [http://www.law.state.ak.us/dispat](http://www.law.state.ak.us/dispat)
- **Calling Hour Restrictions**: 8:00AM - 9:00PM
- **Penalties**: Up to $5,000 per infringement

Alaska made it a violation of state law to call numbers on the national DNC registry (H.B. 15, enacted 05/21/2004, effective July 1, 2004). This law called for the repeal of Alaska’s state-mandated Do Not Call registry (commonly referred to as AK’s “black dot” law). In recent legislative news, by press release dated October 13, 2006, the Alaska Department of Commerce Community and Economic Development has announced that Alaska’s “Black Dot” Do Not Call law has been officially repealed. Furthermore, HB 15 also reduces the time-frame for the DDR exemption from 24-months to 18 months, and requires all entities that have to register as telephone sellers under Alaska rules to pay a registration fee. The Attorney General shall establish the amount of this fee by regulation. For detailed information on all telemarketing related rules in this state, please go to [www.co.regulatoryguide.com](http://www.co.regulatoryguide.com).

### Arizona
- **State**: Arizona
- **Type**: Federal
- **Posted**: As per FTC Rules
- **Updated**: As per FTC List
- **Enrollment**: No
- **DMA List**: No
- **Webpage**: [http://www.azag.gov/consumer](http://www.azag.gov/consumer)
- **Calling Hour Restrictions**: 8:00AM - 9:00PM
- **Penalties**: Up to $1,000 per infringement

AZ has adopted the FTC registry as the AZ “intestate” DNC program. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to [www.co.regulatoryguide.com](http://www.co.regulatoryguide.com).

### Arkansas
- **State**: Arkansas
- **Type**: Federal
- **Posted**: As per FTC Rules
- **Updated**: As per FTC List
- **Enrollment**: No
- **DMA List**: No
- **Webpage**: [http://www.ag.arkansas.gov/com](http://www.ag.arkansas.gov/com)
- **Calling Hour Restrictions**: 8:00AM - 9:00PM
- **Penalties**: $10,000 per infringement

DNC List active as of 1/1/2000. AR has adopted the FTC registry as its official state list. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to [www.co.regulatoryguide.com](http://www.co.regulatoryguide.com).

### California
- **State**: California
- **Type**: Federal
- **Posted**: As per FTC Rules
- **Updated**: As per FTC List
- **Enrollment**: No
- **DMA List**: No
- **Webpage**: [http://cagov.state.ca.us/donotcall](http://cagov.state.ca.us/donotcall)
- **Calling Hour Restrictions**: 8:00AM - 9:00PM
- **Penalties**: $500 for initial infringement with $1,000 per infringement thereafter

Do-Not-Call Law passed in 2001. CA has adopted the FTC registry as its official state list. Legislative News: CA recently enacted a bill (AB 2059) that requires certain disclosures be made where persons NOT on the CA DNC list (CA area codes in the national registry) are asked via the mail for permission to conduct telephone solicitation. The summary of the bill provided by the CA Assembly reads as follows: This bill would require a person that sends a solicitation by mail that solicits a recipient whose telephone number is not on the national “do not call” registry to consent to receive information via telephone to include a clear and conspicuous identification of the sender and of the entity that is requesting permission to call, the telephone number to which the calls are to be placed, and notice that the recipient may be contacted by a telephone solicitor. A violation of this provision would not be a crime, but would be subject to enforcement by any available civil remedies. The bill would require a mailer that seeks express written permission to call a recipient who is on the do-not-call list to contain certain information, including identification of the sender of the mailing and of the entity that is requesting permission to call, the telephone number to which the calls may be placed, the signature of the recipient authorizing the calls, and specified notice, unless there is an established business relationship between the subscriber and the solicitor, in which case express written permission would not be required. A violation of this provision would be a crime, punishable by specified penalties and would be subject to specified civil liabilities. For detailed information on all telemarketing related rules in this state, please go to [www.co.regulatoryguide.com](http://www.co.regulatoryguide.com).

### Colorado
- **State**: Colorado
- **Type**: State and Federal
- **Posted**: Quarterly
- **Updated**: 3,404,363
- **Enrollment**: No
- **DMA List**: No
- **Webpage**: [http://www.coloradonocall.com](http://www.coloradonocall.com)
- **Calling Hour Restrictions**: 8:00AM - 9:00PM
- **Penalties**: $2,000 per infringement

DNC List effective as of 7/1/2002. CO has forwarded state DNC list information to the FTC. List maintained by third party vendor InsightAmericas. Legislative News: Telemarketer Solicitor Fees associated with the Colorado No-Call List have changed for 2008 according to the designated agent, Data Protection Group LLC. The Public Utilities Commission is allowed by state law to change the annual fee as necessary. Fee is based on the total number of employees who work for the company that employs telemarketers. This includes, but is not limited to delivery staff, receptionists, maintenance workers, accounting clerks, as well as telemarketers. For detailed information on all telemarketing related rules in this state, please go to [www.co.regulatoryguide.com](http://www.co.regulatoryguide.com).

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<tr>
<th>State</th>
<th>Action</th>
<th>As Per FTC Rules</th>
<th>As Per FTC List</th>
<th>DMA List</th>
<th>Webpage</th>
<th>Calling Hour Restrictions</th>
<th>Penalties</th>
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<td>8:00AM - 9:00PM</td>
<td>Proposed fines of $500 plus</td>
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<td>As Per FTC List</td>
<td>No</td>
<td><a href="http://consumer.georgia.gov/">http://consumer.georgia.gov/</a></td>
<td>8:00AM - 9:00PM</td>
<td>$2,000 per infraction</td>
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<td>Hawaii</td>
<td>Federal</td>
<td>As Per FTC Rules</td>
<td>As Per FTC List</td>
<td>No</td>
<td><a href="http://hawaii.gov/">http://hawaii.gov/</a></td>
<td>8:00AM - 9:00PM</td>
<td>DNC Violation is Unfair/Unlawful Act</td>
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<td>As Per FTC List</td>
<td>No</td>
<td><a href="http://www.2.state.id.us/agency/consumer">http://www.2.state.id.us/agency/consumer</a></td>
<td>8:00AM - 9:00PM</td>
<td>$500 for initial infraction; $2,500 for second infraction; $5,000 per infraction thereafter</td>
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<td>As Per FTC Rules</td>
<td>As Per FTC List</td>
<td>No</td>
<td><a href="http://www.ag.state.il.us/donotcall">http://www.ag.state.il.us/donotcall</a></td>
<td>8:00AM - 9:00PM</td>
<td>$1,000 for initial infraction with up to $2,500 for each infraction thereafter</td>
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<td><strong>INDIANA</strong> State and Federal</td>
<td>Quarterly</td>
<td>1,812,319</td>
<td>No</td>
<td><a href="http://www.in.gov/attorneygeneral">http://www.in.gov/attorneygeneral</a></td>
<td>8:00AM - 9:00PM</td>
<td>$10,000 for initial infraction and $25,000 per infraction thereafter</td>
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DNC list effective as of 1/1/2002. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to [www.coi.regulatorguide.com](http://www.coi.regulatorguide.com).

| **IOWA** Federal | None | None | No | [http://www.state.ia.us/government](http://www.state.ia.us/government) | 8:00AM - 9:00PM | Proposed $100 to $2,500 |

No DNC list active. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to [www.coi.regulatorguide.com](http://www.coi.regulatorguide.com).

| **KANSAS** Federal | As Per FTC Rules | As Per FTC List | No | [http://www.ksag.org/contentpage](http://www.ksag.org/contentpage) | 8:00AM - 9:00PM | Up to $10,000 per infraction |

DNC list effective as of 1/1/2022. KS has designated the FTC as the list manager for the KS No Call list (separate state-run program terminated.) Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to [www.coi.regulatorguide.com](http://www.coi.regulatorguide.com).

| **KENTUCKY** Federal | As Per FTC Rules | As Per FTC List | No | [http://www.telemarker.com](http://www.telemarker.com) | 8:00AM - 9:00PM | Up to $10,000 per infraction depending on violation |

Legislative News: In April of 2007, KY Senate Bill 430 was signed into law. This bill changed the definition for KY’s “zero call” list to mean the Do Not Call registry maintained by the FTC. The KY Attorney General has now officially indicated that starting June 26, 2007, “any telemarketing company or merchant mailing telephones solicitations into Kentucky is required to obtain the Federal Do Not Call list from the Federal Trade Commission. Kentucky phone numbers on the Federal Do Not Call registry are deemed to be on the Kentucky Zero Call list and may not be called unless an exemption applies.” Therefore, starting June 26, the Zero Call list will no longer be maintained by the KY Attorney General’s office. HB 430 also makes it clear that only “telemarketing companies” (defined as a company whose primary business is to engage in telephone solicitation) must continue to register with the Attorney General’s office — “merchants” (defined as “the individual or business entity offering the consumer goods or services, an investment, business or employment opportunity, or a consumer loan”) are no longer required to register. For detailed information on all telemarketing related rules in this state, please go to [www.coi.regulatorguide.com](http://www.coi.regulatorguide.com).

| **LOUISIANA** State and Federal | Quarterly | 2,331,021 | No | [http://www.lpso.org/solicitors.asp](http://www.lpso.org/solicitors.asp) | 8:00PM - 8:00PM w/ No Sundays or Holidays | $1,500 per infraction and $3,000 per infraction when consumer over the age of sixty-five (65) |

DNC list launched as of 1/1/03; enforcement commenced as of 4/1/03. DNC list program managed by Louisiana Public Service Commission; bond required in LA for telephonic sellers, for Automated Dialer users, and for purchasing the DNC list. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to [www.coi.regulatorguide.com](http://www.coi.regulatorguide.com).

| **MAINE** Federal | As Per FTC Rules | As Per FTC List | No | [http://www.maine.gov/agg/consumer](http://www.maine.gov/agg/consumer) | 8:00AM - 9:00PM | $500 per infraction |

Maine rated for use of the FTC National DNC Registry in 2007. Legislative News: The state of Maine recently passed SB 764 which aligns state DNC established business/individual business rules with federal level rules (30 months for transactions and 3 months for inquiries.) SB 764 also enacted a safe harbor provision that similarly conforms with federal level rules. For detailed information on all telemarketing related rules in this state, please go to [www.coi.regulatorguide.com](http://www.coi.regulatorguide.com).

| **MARYLAND** Federal | As Per FTC | As Per FTC | No | [http://www.oag.state.md.us/Cons](http://www.oag.state.md.us/Cons) | 8:00AM - 9:00PM | $1,000 for initial infraction and up to |
On May 26th, 2004, Maryland governor Robert Ehrlich signed into law an amended version of Senate Bill 88. This bill makes it a violation (starting June 1, 2004) of MD deceptive trade practice rules to violate the Telecommunications Sales Rule (FTC rules) or the rules implemented by the POC pursuant to the Telephone Consumer Protection Act. Under MD state law, deceptive trade practices are subject to fines of up to $1,000 (up to $5,000 for violations after the first); and $500 gives individuals the right to seek $500 per violation plus reasonable attorney's fees. Legislative News: No recent developments to report. For detailed information on all telemarketing-related rules in this state, please go to www.cci.regulatoryguide.com.

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<tr>
<th>State</th>
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<th>Webpage</th>
<th>Calling Hour Restrictions</th>
<th>Penalties</th>
</tr>
</thead>
<tbody>
<tr>
<td>MASSACHUSETTS</td>
<td>State and Federal</td>
<td>Quarterly</td>
<td>2,191,874</td>
<td>No</td>
<td><a href="https://www.medonetcall.gov:443">https://www.medonetcall.gov:443</a></td>
<td>8:00AM - 8:00PM</td>
<td>Up to $5,000.00 per infraction</td>
</tr>
</tbody>
</table>


DNC list effective as of 1/1/2000 (enforcement began 4/1/03). MA has forwarded state DNC list information to the FTC. State list administered by Consumer Protection Office of the Office of the Attorney General. No consumer fees; telerecords are pay for list. MA also allows consumers right to contact their telephone company and request not to receive calls from any automated dialers. Legislative News: No recent developments to report. For detailed information on all telemarketing-related rules in this state, please go to www.cci.regulatoryguide.com.

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<th>Penalties</th>
</tr>
</thead>
<tbody>
<tr>
<td>MICHIGAN</td>
<td>Federal</td>
<td>As Per FTC Rules</td>
<td>As Per FTC List</td>
<td>No</td>
<td><a href="http://www.michigan.gov/mpsc/">http://www.michigan.gov/mpsc/</a> -158-16372_46328_48718- 00.html</td>
<td>9:00AM - 9:00PM</td>
<td>A misdemeanor with fines ranging from six ($6) months for the first violation to $1,000 plus court costs and up to $1,000.00 per violation</td>
</tr>
</tbody>
</table>


DNC list law signed into law by outgoing Governor John Engler on December 20, 2002. By order dated 4/17/2003, the Michigan PSC has officially designated the FTC's DNC list as the official state DNC list for Michigan. Legislative developments: Michigan House Bill 4425 was recently signed into law. This bill makes it illegal to misrepresent in a message left on an answering machine or voice mail a Michigan consumer's consent to receive calls from the telephone solicitor (or another person) who asks the consumer to return the call to discuss that matter. For detailed information on all telemarketing-related rules in this state, please go to www.cci.regulatoryguide.com.

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</thead>
<tbody>
<tr>
<td>MINNESOTA</td>
<td>Federal</td>
<td>As Per FTC Rules</td>
<td>As Per FTC List</td>
<td>No</td>
<td><a href="http://www.state.mn.us/cgl-">http://www.state.mn.us/cgl-</a> bin/portal/msfisp/content.do?content=5388051565&amp;content=</td>
<td>9:00AM - 9:00PM</td>
<td>$1,000 per infraction</td>
</tr>
</tbody>
</table>


The State of MN Department of Commerce, starting as of July 9th, 2008, is forwarding all consumer interests in signing up for the MN Do Not Call Program to the FTC's Do Not Call sign up page. As of this date, MN will no longer maintain a separate state-run Do Not Call list. All numbers listed on the now discontinued separate MN Do Not Call list either already are, or shortly will be, included on the national DNC registry. Telemarketers entities seeking to register with and pay for the MN DNC program are likewise being directed to the FTC DNC website. For detailed information on all telemarketing-related rules in this state, please go to www.cci.regulatoryguide.com.

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<th>Penalties</th>
</tr>
</thead>
<tbody>
<tr>
<td>MISSISSIPPI</td>
<td>State and Federal</td>
<td>Monthly</td>
<td>1,784,377</td>
<td>No</td>
<td><a href="http://www.psc.state.ms.us/tele">http://www.psc.state.ms.us/tele</a></td>
<td>8:00AM - 8:00PM w/ No Sundays or Holidays</td>
<td>$5,000 per infraction</td>
</tr>
</tbody>
</table>


DNC list effective as of 10/1/2003. DNC list maintained by MS PSC. Federal DNC information is included in the MS list. Legislative News: The Mississippi Public Service Commission formally adopted a set of Proposed Rules Implementing the Mississippi Telephone Solicitation Act on September 16. These new rules make significant changes, including: the cost to obtain MS DNC list is $4,500 (for either internet or CD-ROM delivery); a telephone solicitor is allowed to have two contracted companies call on its behalf under the $500 fee; and must pay an additional $100 for each subsequent contracted company beyond the first two; all companies contracted by a telephone solicitor to make calls on its behalf must be identified to the MS PSC; MS now joins AL, LA, and UT as states with a ban on “holiday” calling; telemarketers must submit affidavits to the effect that no blocking of caller ID is occurring; all telephone numbers to be used by a telephone solicitor for telemarketing purposes must be submitted to the MS PSC; telemarketers must provide disconnected numbers to the MS PSC for DNC list updating purposes; the time frame for the effectiveness of a consumer's DNC list has been shortened; specific rules regarding recordkeeping have been implemented. Full details are available at https://www.ms.gov/sec/mcsl/pdf/local_rules_and_regs.pdf. For detailed information on all telemarketing-related rules in this state, please go to www.cci.regulatoryguide.com.

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<tbody>
<tr>
<td>MISSOURI</td>
<td>State and Federal</td>
<td>Quarterly</td>
<td>4,000,771</td>
<td>No</td>
<td><a href="http://ago.mo.gov/nocalllaw/noce">http://ago.mo.gov/nocalllaw/noce</a></td>
<td>8:00AM - 8:00PM</td>
<td>$5,000 per infraction</td>
</tr>
</tbody>
</table>


DNC list effective as of 7/1/2001. Legislative News: The Missouri Attorney General’s office has confirmed that the cost for the Missouri DNC list is going to be increased. Currently set at $25 per area code, with a cap of $600, the new fee as of September 15th, 2006 will be $50 per area code, with a $1,200 cap. The determination to raise the fees completed a rulemaking proceeding that began in late 2001 (C. Miller, 2000). For detailed information on all telemarketing-related rules in this state, please go to www.cci.regulatoryguide.com.

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| State          | Posted | Updated | Enrollment | DMA List | Webpage                                                                                                                                 | Calling Hour Restrictions | Penalties          |

G-4
### Montana

Federal
As Per FTC Rules
As Per FTC List
No
http://www.doj.state.mt.us/consumers/8:00AM - 9:00PM
$5,000 per knowing infra

Effective 1/1/2004, the MT Dept. of Administration has adopted the FTC National registry as the official MT state DNC list. Legislative developments: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

### Nebraska

**State:**
Federal

**Posted:**
Proposed Quarterly

**Updated:**

**Enrollment:**
None

**DMA List:**
No

**Webpage:**
http://www.psc.state.ne.us/home

**Calling Hour Restrictions:**
8:00AM - 9:00PM

**Proposed $2,000 per infraction**

No DNC list active. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

### Nevada

**State:**
Federal

**Posted:**
As Per FTC Rules

**Updated:**
As Per FTC List

**Enrollment:**

**DMA List:**
No

**Webpage:**
http://leg.state.nv.us/asp/bcp/hroc

**Calling Hour Restrictions:**
9:00AM - 6:00PM

**Up to $10,000 per infraction**

Effective 1/1/2004, NV Attorney General has opted to make use of Federal Do Not Call registry. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

### New Hampshire

**State:**
Federal

**Posted:**
As Per FTC Rules

**Updated:**
As Per FTC List

**Enrollment:**

**DMA List:**
No

**Webpage:**
http://www.dog.nh.gov/consumer/sourc

**Calling Hour Restrictions:**
8:00AM - 9:00PM

**Proposed $2,000 per infraction**

By SB 99 (2003), NH has officially designated the FTC’s DNC list as the official state DNC list for NH. Legislative news: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

### New Jersey

**State:**
Federal

**Posted:**
As Per FTC Rules

**Updated:**
As Per FTC List

**Enrollment:**

**DMA List:**
No

**Webpage:**
http://www.state.nj.us/lps/ca/don

**Calling Hour Restrictions:**
8:00AM - 9:00PM

**Proposed $2,000 per infraction**

As of May 17, 2004, NJ has adopted the Federal level DNC registry as its official state DNC list. Legislative News: New Jersey Assembly Bill 773, which fine tunes the provisions of NJ Stat. 56:8-128, was recently signed into law (effective date of August 1, 2005). Specifically, AB 773 requires that the disclosure of a telemarketer’s name (which must be completed within the first 30 seconds of a telemarketing sales call) be made “accurately.” In addition, as a modification to existing NJ Col 120 blocking provisions, AB 773 states that a telemarketer may not use “any technology or method which displays a telephone number or name not associated with the telemarketer or intentionally designed to misrepresent the telemarketer’s identity.” For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

### New Mexico

**State:**
Federal

**Posted:**
As Per FTC Rules

**Updated:**
As Per FTC List

**Enrollment:**

**DMA List:**
No

**Webpage:**
https://telemarketing.doncall.gov

**Calling Hour Restrictions:**
9:00AM - 9:00PM

**$500 per infraction**

SB 573, adopting FTC list (but creating separate and more restrictive New Mexico DNC program) signed by Governor on April 5, 2003. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

### New York

**State:**
Federal

**Posted:**
As Per FTC Rules

**Updated:**
As Per FTC List

**Enrollment:**

**DMA List:**
No

**Webpage:**
http://www.consumer.state.ny.us

**Calling Hour Restrictions:**
8:00AM - 9:00PM

**$1,000 per infraction**

DNC list effective as of 4/1/2001. NY has adopted FTC list as official state list. Legislative News: The New York Consumer Protection Board has amended its regulations governing the state DNC call list to make these rules conform more with Federal level rules. Specifically, the NY CPB has amended its FR1 rules to delete the prior broad references to an “arrangement, agreement, contract or other such legal status of affairs” to a rule that closely follows FCC definitions (including 18 month transactional and 5 month inquiry rules). The NY CPB also made changes to its definitions for “telemarketing” and “telemarketing sales call” to include the FCC’s language regarding “encouraging” a sale. These changes are effective immediately. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.
<table>
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<tr>
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</thead>
<tbody>
<tr>
<td>NORTH DAKOTA</td>
<td>Federal</td>
<td>As Per FTC Rules</td>
<td>As Per FTC List</td>
<td>No</td>
<td><a href="http://www.ag.state.nd.us/nocall">http://www.ag.state.nd.us/nocall</a></td>
<td>8:00AM - 9:00PM</td>
<td>$2,000 per infraction</td>
</tr>
</tbody>
</table>

Attorney General has opted to adopt the FTC’s rules as the official state DNC list. No separate state program will be developed. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

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<tr>
<td>OHIO</td>
<td>Federal</td>
<td>As Per FTC Rules</td>
<td>As Per FTC List</td>
<td>No</td>
<td><a href="http://www.pucr.ohio.gov/PUCG/">http://www.pucr.ohio.gov/PUCG/</a> doc_id=458</td>
<td>8:00AM - 9:00PM</td>
<td>As Per Federal Rules</td>
</tr>
</tbody>
</table>

DNC list effective as of 1/1/2009. OH has forwarded state DNC list information to the FTC. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

<table>
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<tr>
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</thead>
<tbody>
<tr>
<td>OKLAHOMA</td>
<td>State and Federal</td>
<td>Quarterly</td>
<td>641,531</td>
<td>No</td>
<td><a href="http://www.occ.state.ok.us/teles/">http://www.occ.state.ok.us/teles/</a> OpenPage</td>
<td>8:00AM - 9:00PM</td>
<td>Between $500 and $1,500 per infraction</td>
</tr>
</tbody>
</table>

DNC list effective as of 1/1/2000. Legislative News: On 6/18/2007, the Attorney General of the State of Oklahoma, Terry Hass, officially designated the FTC’s National DNC Registry as the Oklahoma DNC List. Furthermore, the state of OK enacted new rule (OK C. R. 96) requiring the use of ADID to call winners and resident numbers within OK. These new rules repeal the “dial 411” statute (OKS 795.26) and enact new rules that allow the use of ADID to dial numbers randomly and sequentially, except in certain circumstances, including calls to DNC list numbers. (Note that such calls to DNC list numbers are allowed where the caller has an OSA with the subscriber consent, and in certain other circumstances.) Calls are only allowed from 9 AM to 9 PM, and a second “strawphone” rule is in place. OK 9.40 F 2(b) also prohibits making certain misrepresentations when using ADID. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

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<tbody>
<tr>
<td>PENNSYLVANIA</td>
<td>State and Federal</td>
<td>Quarterly</td>
<td>2,380,418</td>
<td>Yes</td>
<td><a href="http://www.attorneygeneral.gov/pennsylvania">http://www.attorneygeneral.gov/pennsylvania</a></td>
<td>8:00AM - 9:00PM</td>
<td>$1,000 per infraction; $2,500 if involving consumer age 60 or older</td>
</tr>
</tbody>
</table>

DNC list effective as of 7/1/2000. DMA list used by PA; blocking Caller ID prohibited. Legislative developments: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

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<tbody>
<tr>
<td>RHODE ISLAND</td>
<td>Federal</td>
<td>Proposed</td>
<td>Quarterly</td>
<td>None</td>
<td><a href="http://www.riag.state.ri.us/telelmts">http://www.riag.state.ri.us/telelmts</a></td>
<td>9:00AM - 6:00PM and 10:00AM - 12:00PM on Saturdays; No calls on Sundays.</td>
<td>Proposed $500 for first interaction with $1,000 for each subsequent interaction</td>
</tr>
</tbody>
</table>

No DNC list active. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.
<table>
<thead>
<tr>
<th>State</th>
<th>Federal</th>
<th>Proposed</th>
<th>Updated</th>
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<tbody>
<tr>
<td>SOUTH CAROLINA</td>
<td>Federal</td>
<td>None</td>
<td>4,250,186</td>
<td>No</td>
<td><a href="http://www.scdn.org/">http://www.scdn.org/</a></td>
<td>9:00AM - 9:00PM No Sundays</td>
<td>$5,000 per infraction</td>
<td></td>
</tr>
<tr>
<td>TENNESSEE</td>
<td>State and Federal</td>
<td>Monthly</td>
<td>4,250,186</td>
<td>No</td>
<td><a href="http://www.tennessee.gov/">http://www.tennessee.gov/</a></td>
<td>9:00AM - 9:00PM</td>
<td>$2,000 per infraction</td>
<td></td>
</tr>
<tr>
<td>TEXAS</td>
<td>State and Federal</td>
<td>Quarterly</td>
<td>12,683,180</td>
<td>No</td>
<td><a href="http://www.texas.gov/">http://www.texas.gov/</a></td>
<td>9:00AM - 9:00PM &amp; 12:00PM - 9:00PM on Sundays</td>
<td>$1,000 per infraction, but $500 per infraction if determined solicitor willfully violated the law</td>
<td></td>
</tr>
<tr>
<td>UTAH</td>
<td>Federal</td>
<td>As Per FTC Rules</td>
<td>As Per FTC List</td>
<td>No</td>
<td><a href="http://www.consumerprotection">http://www.consumerprotection</a>.</td>
<td>8:00AM - 9:00PM No Calls Sundays or Legal Holidays</td>
<td>$2,500 per infraction</td>
<td></td>
</tr>
<tr>
<td>VERMONT</td>
<td>Federal</td>
<td>As Per FTC Rules</td>
<td>As Per FTC List</td>
<td>No</td>
<td><a href="http://www.sec.state.vt.us/">http://www.sec.state.vt.us/</a></td>
<td>8:00AM - 9:00PM</td>
<td>$500 for first infraction with additional $1,000 for each subsequent infraction</td>
<td></td>
</tr>
<tr>
<td>VIRGINIA</td>
<td>Federal</td>
<td>As Per FTC Rules</td>
<td>As Per FTC List</td>
<td>No</td>
<td><a href="http://www.cqva.gov/">http://www.cqva.gov/</a></td>
<td>8:00AM - 9:00PM</td>
<td>None</td>
<td></td>
</tr>
</tbody>
</table>
**WASHINGTON** | Federal | Quarterly | None | No | -Privacy/DoNotCall.aspx | 8:00AM - 9:00PM | None
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No DNC list active. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

| **WEST VIRGINIA** | State and Federal | Proposed Quarterly | None | No | http://www.wvago.us/ | 8:00AM - 9:00PM | None
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No DNC list active. Legislative News: No recent developments to report. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

| **WISCONSIN** | State and Federal | Quarterly | 2,113,591 | No | https://nocall.wisconsin.gov/web/ | 8:00AM - 9:00PM | Fines range from $1,000 - $10,000 per infraction
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DNC list effective as of 1/1/2003. DNC list maintained by Department of Agriculture, Trade and Consumer Protection. Legislative News: The WI Department of Agriculture, Trade and Consumer Protection has advised registered telephone solicitors that the next quarterly update to the WI DNC list (to be distributed in September of 2000) will contain all phone numbers (as mandated by WI AB 226 passed earlier this year.) To accommodate this change, the WI list will now be distributed in six groups of telephone numbers, rather than five (the sixth group of numbers will contain area codes outside of the five WI area codes.) In addition, numbers from the National DNC Registry will no longer be included with the WI DNC list. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

| **WYOMING** | State and Federal | Quarterly | 979 | Yes | http://attorneygeneral.state.wy.us | 8:00AM to 8:00PM | $2,500 per infraction
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DNC list effective as of 7/1/2001. The Direct Marketing Association (DMA) list is recognized by Wyoming as its official state Do-Not-Call list. Legislative News: Wyoming has amended its laws pertaining to telephone solicitations made to cellular telephones. Calls to unpublished cellular telephones prohibited effective July 1, 2001. For detailed information on all telemarketing related rules in this state, please go to www.co.regulatoryguide.com.

### CANADA NATIONAL DO-NOT-CALL LIST

<table>
<thead>
<tr>
<th>Country</th>
<th>Posted</th>
<th>Updated</th>
<th>Enrollment</th>
<th>DMA List</th>
<th>Webpage</th>
<th>Calling Hour Restrictions</th>
<th>Penalties</th>
</tr>
</thead>
</table>
|CANADA | Federal | At Least Once Every 31 Days | 6,096,772 | No | https://www.crto.gc.ca/eic/site/dnd.nsf | 9:00AM - 9:00PM on Weekdays and 10:00AM to 6:00PM on Saturdays and Sundays | $1,500 for an individual and up to $15,000 for a Corporation per infraction

DNC list effective as of 9/30/2008. The Canadian Radio-Television and Telecommunications Commission (CRTC) launched the national Do-Not-Call List (DNCL) on September 30, 2008 designed to allow Canadians to reduce the number of telemarketing calls they receive. The CRTC is an independent agency responsible for regulating Canada’s broadcasting and telecommunications systems that report to Parliament through the Minister of Canadian Heritage. Recently, the Commission has approved Bell Canada's proposed revised rates for subscriptions to the National DNCL. The approved rates are effective for a twelve-month period, from August 1, 2009 to July 31, 2010. Subscriptions purchased before August 1, 2009 will be charged at the previous rates indicated on the National DNCL Web site. Subscription Options: Full List (all NPA’s) - 1 Annual ($17.25), 2) 1 Month ($2,675), 2) 2 Month ($5,350) and 6 Month ($15,750). Per NPA(’s) - 1 Annual ($1,620), 2) 1 Month ($144), 2) 2 Month ($448) and 4) 6 Month ($894). Per-Number Query Rate - $1.75/number. More information can be found at http://www.crtc.gc.ca/eng/dnd.htm

### DISCLAIMER
The rules governing Do-Not-Call both federally and on a state level can change rapidly. Amendments, adjournment of committee, majority defeat by the legislative body +/or veto, among many others, can all affect the immediate status of proposed legislation on its way to becoming law. As a result, Call Compliance, Inc. (CCI) stresses that the information contained in this document is solely for informational purposes, and CCI strongly recommends consulting your counsel +/or other legal resources as necessary.

Appendix H

Sample State Summary of Telemarketing and DNC Rules

Reprinted and used with permission from Call Compliance, Inc.

Indiana

Registration Requirements

<table>
<thead>
<tr>
<th>Telemarketer</th>
<th>&quot;Seller&quot; means a person who, personally, through salespersons, or through the use of an automated dialing device, makes a solicitation if in the solicitation any one (1) of the following occurs:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Defined:</td>
<td>(1) There is a false representation or implication that a prospect will receive a gift, prize, or the value of a gift or prize.</td>
</tr>
<tr>
<td></td>
<td>(2) There is an offer of a vacation at a reduced price if the vacation involves the prospect attending a presentation in which the prospect is solicited to purchase a time share or camping club membership and if the seller does not own the time share or camping club, does not represent the owner of the time share or camping club, or misrepresents the value of the vacation.</td>
</tr>
<tr>
<td></td>
<td>(3) There is a representation or implication that a prospect who buys office equipment or supplies will, because of some unusual event or imminent price increase, be able to buy these items at reduced prices.</td>
</tr>
<tr>
<td></td>
<td>(4) There is a false representation or implication as to the identity of the person making the solicitation.</td>
</tr>
<tr>
<td></td>
<td>(5) There is a representation or implication that the items for sale are manufactured or supplied by a person other than the actual manufacturer or supplier.</td>
</tr>
<tr>
<td></td>
<td>(6) There is an offer to sell the prospect precious metals/stones, coal, or other minerals, or any interest in oil, gas, or mineral fields, wells, or exploration sites, if the seller does not own the items, does not represent the owner, or misrepresents the value of the items.</td>
</tr>
</tbody>
</table>

Telemarketing "solicitation" means a telephone conversation or attempted telephone conversation in which the seller offers, or attempts to offer, an item to another person in exchange for money or other consideration.

Notes: Before doing business in Indiana a "seller" must register with the division if the seller attempts a solicitation under which the seller offers an item or items where the total consideration has a value of more than one hundred dollars ($100) and less than fifty thousand dollars ($50,000). Updates to information must be made whenever they occur. Filing includes: corporate information; information on individual officers, directors, managers; locations/numbers, scripts; gift disclosures.

Address: Office of the Attorney General
Consumer Protection Division
Indiana Government Center South, 5th Fl
402 West Washington Street
Indianapolis, IN 46204-2794

URL: http://www.in.gov/attorneygeneral/2444.htm
Fee: $50/year; $50 to renew.
Bond: None
Exemptions: Entities who do not fall into definition of "seller" and sellers who are offering items of less than $100 and more than $50,000

Cites
Burns Ind. Code Ann. § 24-5-12-8
Burns Ind. Code Ann. § 24-5-12-9
Burns Ind. Code Ann. § 24-5-12-10 et seq.
Fines: Class D felony; injunctions; sales voidable by purchasers

Calling Time Restrictions
None (Federal rules allowing calls from 8:00 AM to 9:00 PM apply).

Do-Not-Call Requirements
Telemarketer: "Telephone solicitor" means an individual, a firm, an organization, a partnership, an association, or a corporation, including affiliates and subsidiaries, doing business in Indiana.

Telemarketing: "Telephone sales call" means a telephone call made to a consumer for any of the following purposes: (1) Solicitation of a sale of consumer goods or services; (2) Solicitation of a charitable contribution; or (3) Obtaining information that will or may be used for the direct solicitation of a sale of consumer goods or services or an extension of credit for such purposes. The term includes a call made by use of automated dialing or recorded message devices.

Address: Office of the Indiana Attorney General
Indiana Government Center South, 5th Floor
302 West Washington Street
Indianapolis, In 46204

Cost: $750/year

Online Info: http://www.in.gov/attorneygeneral

Enforce: List Updated: Quarterly
Implementation Period: No days stated

Exemptions: Exemptions:
- express request
- a telephone call made primarily in connection with an existing debt or contract for which payment or performance has not been completed at the time of the call
- calls made by charitable organizations if: call made by volunteer or employee; caller immediately discloses caller’s first and last name, and name, address, telephone number of the charity
- calls made by licensed real estate brokers if sale is not until after face to face presentation
- calls by licensed insurance agents
- calls soliciting the sale of a newspaper of general circulation, but only if the telephone call is made by a volunteer or an employee of the newspaper.

NOTE: no EBR exemption included
Fines: Injunction; $10,000 for initial infraction and $25,000 per infraction thereafter.

Existing Business Relationship Rules
Definition: Indiana unique among the DNS registry states in that it does not exempt calls to existing customers (but see "existing debt or contract for which payment or performance has not been completed" exemption.)

Time Period: None

Solicitation Disclosures
A telephone solicitor who makes a telephone sales call to a telephone number shall immediately disclose the following information upon making contact with the consumer:
(1) The solicitor’s true first and last name; (2) The name of the business on whose behalf the telephone solicitor is soliciting.
All advertisements, pamphlets, brochures, or any other materials used in the solicitation or completion of telephonic sales must include the assigned registration number in the following manner: “C.P.D. Reg. No. T.S.____________________.”

Purchase Rules
A contract made under a telephone sales call void unless in writing and signed by consumer (terms and cancellation language as per statute.)

Exceptions to the above: (1) A sale in which: (A) no prior payment is made to a merchant; (B) an invoice accompanies the goods or services; and (C) a consumer is allowed 7 days to cancel without obligation for payment; (2) A contractual agreement that (A) requires payment; and (B) allows the consumer at least 10 days to cancel; (3) A sale by a telephone utility; or (4) A newspaper subscription executed through a telephone call.

No submission of charge by merchant until merchant receives from the consumer a signed copy of the contract. This rule regarding charge submissions does not apply to any of the following: (1) A transaction from a visit by a consumer to a merchant that operates a retail business with a permanent location; (2) A transaction in which: (A) a consumer may obtain a full refund of the return of undamaged and unused goods; or (B) a consumer may, within 7 days after receipt of merchandise by a consumer, give a cancellation of services notice to a seller and return the merchandise, and the seller must process the refund within 30 days after receipt of the returned merchandise. (3) A transaction in which a consumer purchases goods or services under a television, radio, or print advertisement or a sample, brochure, or catalog of a merchant that contains: (A) the name, address, and business telephone number of the merchant; (B) a description of the goods or services being sold; and (C) limitations or restrictions that apply to the offer. (4) A transaction in which a merchant is a bona fide charitable organization.

If seller does not register with Indiana, purchasers may cancel any contract with the seller. If a seller uses any untrue, misleading, or deceptive statement in a solicitation or sale; or fails to deliver an item ordered within four (4) weeks, the purchaser may void the contract within ninety (90) days from the date of the contract by giving written notice to the seller.
Charity Calls for Donations: Do the Do-Not-Call list rules apply to calls by:

<table>
<thead>
<tr>
<th>Employee/Volunteer?</th>
<th>Outsourced, For-Profit?</th>
</tr>
</thead>
<tbody>
<tr>
<td>No</td>
<td>Yes</td>
</tr>
</tbody>
</table>

Charity Calls Offering Goods: Do the Do-Not-Call list rules apply to calls by:

<table>
<thead>
<tr>
<th>Employee/Volunteer?</th>
<th>Outsourced, For-Profit?</th>
</tr>
</thead>
<tbody>
<tr>
<td>No</td>
<td>Yes</td>
</tr>
</tbody>
</table>

DNC Safe Harbor

In any proceeding brought against a telephone solicitor for violating DNC rules, the attorney general may consider the following as mitigating factors: (1) That the defendant has obtained the most recently published telephone privacy list; (2) That the defendant has maintained the records required by the DNC rules; (3) That the defendant has established and implemented reasonable practices and procedures to effectively prevent telephone solicitations in violation of the DNC rules; (4) That the defendant has not previously been found to have violated the DNC rules.

Caller ID Blocking

Yes

Permission to Continue

Language: None
Exemptions: n/a

No-Rebuttal Provisions

Language: None
Exemptions: n/a

Autodialer Rules

A caller may not use or connect to a telephone line an automatic dialing-announcing device unless:

1. The subscriber has knowingly or voluntarily requested, consented to, permitted, or authorized receipt of the message; or
2. The message is immediately preceded by a live operator who obtains the subscriber's consent before the message is delivered.

Also, a caller may not use an automatic dialing-announcing device for commercial telephone solicitation so that a subscriber receives a telephone call before 9 A.M. or after 8 P.M.

The two rules above do not apply to messages: (1) From school districts to students, parents, or employees; (2) To subscribers with whom the caller has a current business or personal relationship; or (3) Advising employees of work schedules.

The following rules apply to ALL automatic dialer calls:
A caller may not use an automatic dialing-announcing device unless the device is
designed and operated to disconnect within ten (10) seconds after termination of the telephone call by the subscriber.

When a message is immediately preceded by a live operator, the operator must, at the outset of the message, disclose the following:

1. The name of the entity for which the message is being made.
2. The purpose of the message.
3. The identity or kinds of goods or services the message is promoting.
4. If applicable, the fact that the message intends to solicit payment or the commitment of funds.

A caller may not use an automatic dialing-announcing device to make a telephone call to any emergency number.

**Predictive Dialer Rules**

None at present; federal 3% rate applicable.

**Wireless Rules**

Text Msg: None at present

Calls to Cells: Only residential numbers on DNC list.

**Facsimile Rules**


Fax on DNC? As per FTC rule

**Call Monitoring Requirements (See Topical Information for Federal rules)**

"Interception" means the intentional recording or acquisition of telephonic communication by a person other than a sender or receiver of that communication, without the consent of the sender or receiver, by means of any device. Unlawful to intercept communications without proper authorization or warrant.

Consent Rule: One party

**General Notes**
Appendix I

Summary of State Drug-Testing Laws and Relevant Workers’ and Unemployment Compensation Laws

From Mark A. de Bernardo & Matthew F. Nieman, GUIDE TO STATE AND FEDERAL DRUG-TESTING LAWS (Institute for a Drug Free Workplace/Jackson Lewis LLP, 15th ed. 2008). Reprinted and used with permission.

### SUMMARY OF STATE DRUG-TESTING LAWS AND RELEVANT WORKERS’ AND UNEMPLOYMENT COMPENSATION LAWS

The following is an overview which divides the states into eight categories: (1) states that do not have any statutory or case law affecting an employer’s right to drug test employees; (2) states that have case law on drug testing; (3) states that do not restrict the types of testing an employer may conduct, but statutorily set forth specific procedures an employer must follow when choosing to implement a drug-testing program; (4) states that statutorily restrict both the type of drug test administered (who and when) and the procedures used (how) to perform such drug testing; (5) states which have voluntary laws affecting drug testing; (6) states with voluntary workers’ compensation premium reduction laws that grant employers in compliance a discount on their workers’ compensation insurance; (7) states with related workers’ compensation statutes and/or cases; and (8) states with related unemployment statutes and/or cases.

<table>
<thead>
<tr>
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<tbody>
<tr>
<td>District of Columbia</td>
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</table>

<table>
<thead>
<tr>
<th>2. States with Drug-Testing Case Law (47 states and Puerto Rico):</th>
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</thead>
<tbody>
<tr>
<td>Alabama</td>
<td>Kentucky</td>
<td>Oklahoma</td>
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<tr>
<td>Alaska</td>
<td>Louisiana</td>
<td>Oregon</td>
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<tr>
<td>Arizona</td>
<td>Maine</td>
<td>Pennsylvania</td>
</tr>
<tr>
<td>Arkansas</td>
<td>Maryland</td>
<td>Puerto Rico</td>
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<tr>
<td>California</td>
<td>Massachusetts</td>
<td>Rhode Island</td>
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<tr>
<td>Colorado</td>
<td>Michigan</td>
<td>South Carolina</td>
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<td>Florida</td>
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<td>Hawaii</td>
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<tr>
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<td>Virginia</td>
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<tr>
<td>Iowa</td>
<td>North Carolina</td>
<td>Wisconsin</td>
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<td>Kansas</td>
<td>Ohio</td>
<td>Wyoming</td>
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<thead>
<tr>
<th>3. States with Mandatory Statutes Affecting Testing Procedures Only (7 states):</th>
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</thead>
<tbody>
<tr>
<td>Hawaii</td>
<td>Maryland</td>
<td>North Carolina</td>
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<tr>
<td>Kansas</td>
<td>Nebraska</td>
<td>Oregon</td>
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<tr>
<td>Louisiana</td>
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</tbody>
</table>
4. Jurisdictions with Mandatory Statutes Affecting Both the Circumstances in which Testing is Permitted and the Testing Procedures Used (8 states, 2 cities and Puerto Rico):

<table>
<thead>
<tr>
<th>State</th>
<th>State</th>
<th>State</th>
</tr>
</thead>
<tbody>
<tr>
<td>Boulder, CO</td>
<td>Minnesota</td>
<td>Rhode Island</td>
</tr>
<tr>
<td>Connecticut</td>
<td>Montana</td>
<td>San Francisco, CA</td>
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<tr>
<td>Iowa</td>
<td>Oklahoma</td>
<td>Vermont</td>
</tr>
<tr>
<td>Maine</td>
<td>Puerto Rico</td>
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</tr>
</tbody>
</table>

5. States with Voluntary Laws Affecting Drug Testing (12 states):

<table>
<thead>
<tr>
<th>State</th>
<th>State</th>
<th>State</th>
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<tbody>
<tr>
<td>Alabama</td>
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<td>Arkansas</td>
<td>Mississippi</td>
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<th>State</th>
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<td>Alabama</td>
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<td>Idaho</td>
<td>South Carolina</td>
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<tr>
<td>Florida</td>
<td>Mississippi</td>
<td>Tennessee</td>
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</tbody>
</table>

7. States with Related Workers’ Compensation Statutes (s) and/or Case Law (c) (48 states, the District of Columbia and Puerto Rico):

<table>
<thead>
<tr>
<th>State</th>
<th>State</th>
<th>State</th>
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<tbody>
<tr>
<td>Alabama</td>
<td>Kentucky</td>
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<td>South Dakota</td>
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<td>Distr. of Columbia</td>
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<tr>
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<td>Wisconsin</td>
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<tr>
<td>Iowa</td>
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<td>Wyoming</td>
</tr>
<tr>
<td>Kansas</td>
<td>North Dakota</td>
<td></td>
</tr>
</tbody>
</table>
8. States with Related Unemployment Compensation Statutes(s) and/or Case Law (c) (44 states, and the District of Columbia):

<table>
<thead>
<tr>
<th>Alabama</th>
<th>Kentucky (s/c)</th>
<th>North Carolina (s/c)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alaska</td>
<td>Louisiana (s/c)</td>
<td>North Dakota (c)</td>
</tr>
<tr>
<td>Arizona</td>
<td>Maine (c)</td>
<td>Ohio (c)</td>
</tr>
<tr>
<td>Arkansas</td>
<td>Maryland (c)</td>
<td>Oklahoma (s/c)</td>
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<td>Wisconsin (c)</td>
</tr>
<tr>
<td>Iowa</td>
<td>New York (c)</td>
<td>Wyoming (c)</td>
</tr>
<tr>
<td>Kansas</td>
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</tr>
</tbody>
</table>

9. States with Drug-Testing Falsification and/or Tampering Statutes.

<table>
<thead>
<tr>
<th>Arkansas</th>
<th>Nebraska</th>
<th>South Carolina</th>
</tr>
</thead>
<tbody>
<tr>
<td>Illinois</td>
<td>New Jersey</td>
<td>Texas</td>
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<tr>
<td>Kentucky</td>
<td>North Carolina</td>
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<td>Wyoming</td>
</tr>
<tr>
<td>Maryland</td>
<td>Pennsylvania</td>
<td>West Virginia</td>
</tr>
</tbody>
</table>
John R. F. Baer

John Baer is an officer in the Chicago, Illinois office of Greensfelder, Hemker & Gale, P.C. Mr. Baer has a broad transactions practice with extensive experience representing companies engaged in franchising and distribution, including the use of sales representatives, both domestically and internationally. His practice covers a wide range of other related areas, including commercial, sales, warranties, product safety and regulatory matters.

Mr. Baer is the Vice Chair of the International Franchising Committee of the International Bar Association’s International Sales, Franchising and Product Law Section, and a member of the Illinois State Bar Association’s Special Committee on Franchising and Distribution Law. He is Chair of the Illinois Attorney General’s Franchise Advisory Board and Editor of the CCH Sales Representative Law Guide. Mr. Baer is a member of the Industry Advisory Committee to the North America Securities Administrators Association Franchise Project Group. He was a member of the ABA Forum on Franchising’s Governing Committee from 2003 to 2006 and the first recipient of the Forum’s Lewis G. Rudnick Award in 2009.
Mark A. Kirsch

Mark Kirsch is a partner in the firm Plave Koch PLC in Reston, Virginia. Mark has been practicing in the field of franchise law for over 24 years, and his practice focuses on domestic and international franchising, licensing and distribution matters.

Mark has represented and counseled clients on various corporate, commercial, franchising and business development matters across a diverse range of industries, including restaurants and food service, hotels, retail, technology, health care, business services, educational and training businesses, car rental and automotive services, equipment manufacturing and product distribution. Mark has extensive experience in structuring franchise and distribution systems, mergers and acquisitions of franchise companies, compliance with state and federal regulatory issues, and developing co-branding and multiple-brand licensing and distribution arrangements.

Mark is admitted to practice in Washington, D.C., Maryland and Virginia, and was Chair of the Maryland Bar Franchise and Distribution Law Committee (1999-2001). Mark has a BA (cum laude) in Economics from the University of Rochester, and received his law degree from George Washington University Law School. Mark has been listed in *The Best Lawyers in America*, and the *International Who’s Who of Business Lawyers*, and recognized as a Virginia Super Lawyer, a Washington DC Super Lawyer, and as a “Legal Eagle” by *Franchise Times*.
Anthony J. Marks

Mr. Marks concentrates his practice in the areas of franchise and distribution, mergers and acquisitions, corporate finance, and general corporate law. He is certified by the State Bar of California as a Franchise and Distribution Law Specialist. Mr. Marks counsels clients in a wide range of industries in the spectrum of franchise law, including structuring new franchise programs, domestic and international franchise and distribution programs, franchise registration and disclosure matters, terminating and renewing franchise relationships, negotiating complex multi-unit transactions and transfers, and assessing the applicability of federal and state franchise and business opportunity laws. He also advises investors and franchise companies in connection with all aspects of franchise company acquisitions, divestitures and financings. Additionally, Mr. Marks represents privately held and publicly traded companies in various corporate transactions. He is experienced with formation matters, debt and equity finance, mergers, acquisitions, international and cross-border transactions, and day-to-day business operational transactions. Mr. Marks is a former Co-chair of the California Bar Association Franchise Law Committee. Mr. Marks has been named as a 2006-2010 Southern California "Rising Star" by Law & Politics. Mr. Marks is admitted to practice in California. Mr. Marks has a B.S. (cum laude) from the California State Polytechnic University, and received his law degree from Loyola Law School.