

# Defaults and Terminations: An Unfortunate Reality of a Challenging Economy

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Franchise systems are not immune from the negative impact of the current economic climate. The effects manifest themselves in numerous ways. Franchisors may be reducing services to franchisees or spending less on research and development or marketing. At the unit level, franchisees may be cutting staff, taking short cuts complying with brand standards, or failing to pay royalties or other amounts owed the franchisor or other creditors.

During these times, it is advisable for franchisors to attempt to work with their franchisees because the closure of a unit, for whatever reason, arguably impacts the goodwill of the brand. A franchisor can only work with a franchisee for so long, however. The length of time depends upon various factors; but at a certain point, the franchisor may choose to resort to the default and termination process, ultimately resulting in the termination of the franchise relationship. Regardless of the reason, termination results in serious consequences. The investment made by both parties in the relationship will presumably be lost. The goodwill established through a combination of each party's hard work will also be lost. The relationship of the parties will forever be changed and, in most cases, they will never work together again. Customers may also be left in the lurch, innocent bystanders collaterally damaged by the actions of the parties, whether right or wrong.

Most franchise agreements carefully prescribe procedures for terminating the franchise relationship. Statutes also provide rules that govern termination. Failure to follow these procedures or rules can lead to serious consequences for the party that has failed to follow them.<sup>1</sup> Procedures imposed by contract will, for the most part, be trumped by franchise termination laws applicable to the relationship; however, there is still no federal law<sup>2</sup> that regulates the franchise relationship generally and the termination of that relationship specifically.<sup>3</sup> This leaves a patchwork of state laws that generally regulate the franchise relationship and place restrictions on termination.<sup>4</sup>

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This article first provides an overview of state relationship laws, including an analysis of incurable defaults and buyback provisions. It then discusses the application of state relationship laws to exempt franchises and highlights those unique state relationship law provisions that sometimes catch even seasoned practitioners by surprise. Finally, it considers several issues of importance to franchisors in the default and termination process.

## I. OVERVIEW OF STATE RELATIONSHIP LAWS<sup>5</sup>

As of April 2009, nineteen states and two territories had relationship laws that govern the termination or nonrenewal of the franchise relationship.<sup>6</sup> The oldest of these laws is the Puerto Rico Dealers' Contracts Law, adopted in 1964, which applied to dealers without regard to industry. Other states began enacting franchise relationship laws in the mid-1970s.

The newest state relationship law is the Rhode Island Fair Dealership Act, adopted on June 14, 2007. Rhode Island's adoption of the act marked the end of a seventeen-year period during which no state enacted a franchise relationship law of general application.<sup>7</sup> However, this lack of newly adopted legislation has not been for a lack of trying, as seen by the recent efforts in Kansas and Tennessee to adopt the Kansas Responsible Franchise Practices Act and the Tennessee Franchise Disclosure Act of 2007, respectively, which both address franchise relationship issues.

In any event, navigating the state relationship statutes can be a tricky endeavor because no two statutes are exactly the same. Among other things, states vary in the conditions required to terminate or fail to renew a franchise agreement. States also vary in the mechanics of termination and nonrenewal.

### A. Conditions Required Prior to Termination

Perhaps the most widely varied provisions in the state relationship laws are the conditions required to be present before the franchisor can terminate the franchise relationship. Most states generally require "good cause" prior to termination.<sup>8</sup> However, circumstances that constitute good cause in one state may not be good cause in another, and a critical analysis of the applicable state relationship law must be made to ascertain the appropriate standard for termination.

#### I. Good Cause

The state relationship laws requiring good cause generally fall along a spectrum as to the factual circumstances or conditions that must be present to satisfy the definition of good cause. At one end of the spectrum are the statutes of Delaware and Virginia, which require good cause prior to termination but fail to provide any guidance on the circumstances constituting good cause.<sup>9</sup>

In the middle of the spectrum are those states that provide a general definition of good cause. These states define good cause as the failure to comply substantially with the “lawful, material provisions” of the franchise agreement. States that maintain this simple definition of good cause or a close variation of it include California, Connecticut, Hawaii, Illinois, Indiana, Michigan, Minnesota, Nebraska, New Jersey, Rhode Island, and Washington.<sup>10</sup>

A subset of these states includes specific examples of factual circumstances of the definition in their statutes. States with specific bases constituting good cause include Connecticut, Illinois, Minnesota, and Rhode Island. The most common statutory examples include the franchisee’s bankruptcy, voluntary abandonment of the franchised business, failure to pay sums due, conduct that materially impairs the goodwill of the franchised business or impairment of the trademark or trade name, and certain types of repeated defaults under the franchise agreement. Most states that list specific circumstances constituting good cause provide that the list is not exhaustive, implying that other factual circumstances would meet the definition of good cause in the applicable state statute.

In this same vein, certain states allow a franchisor to terminate the relationship due to circumstances existing outside of good cause. For example, the Hawaii statute provides that termination may occur either for good cause, or in accordance with the franchisor’s current terms and standards, as equally applied systemwide.<sup>11</sup> On the other hand, Arkansas specifically limits good cause to the specific enumerated circumstances in the statute, one of which is the failure by the franchisee to act in good faith.<sup>12</sup>

Finally, on the far end of the spectrum are those states that impose a heightened good cause standard to terminate the relationship.<sup>13</sup> Iowa is one of those states, defining good cause as “cause based upon a legitimate business reason.” Iowa’s law also cites to the generic definition of good cause discussed above but then imposes an arbitrary and capricious standard. However, the franchisee must prove that the franchisor has acted arbitrarily or capriciously.<sup>14</sup>

Wisconsin and the Virgin Islands define good cause as a failure by the franchisee to substantially comply with essential and reasonable requirements of the franchisor, which are not discriminatory as compared with requirements imposed upon other similarly situated franchisees, or bad faith by the franchisee in carrying out the terms of the franchise. This arguably means that good cause exists only if the franchisee has “materially” breached an obligation to the franchisor that has been uniformly enforced across its franchise system (or if the franchisor demonstrates the franchisee’s bad faith).<sup>15</sup>

The definition of good cause under the Puerto Rico Dealers’ Contracts Law arguably imposes the highest standard on a franchisor seeking to terminate a franchisee. The Puerto Rico law provides that “just cause” only occurs upon a franchisee’s non-performance of any essential provision in the franchise agreement, or an act or omission that “adversely and substantially” affects the interests of the franchisor in promoting the marketing or distribution of merchandise or services. Puerto Rico’s law limits the franchisor’s ability to terminate to “just cause”; but unlike other statutes, it also requires the franchisor to satisfy

two other thresholds prior to termination. First, if the violation by the franchisee relates to a provision in the franchise agreement restricting certain changes in the operation of the business, the franchisor must show that the violation “may affect, or has truly and effectively affected” the interests of the franchisor in an adverse and substantial manner. Additionally, if the violation by the franchisee relates to a provision in the franchise agreement specifying conduct, quotas, or goals, such as sales quotas, the franchisor must prove that the provision was reasonable in the Puerto Rican market at the time of the violation.<sup>16</sup>

## 2. Cure and Termination Periods

Even if the franchisee has breached the franchise agreement or engaged in other behavior that constitutes good cause, many state relationship laws impose an obligation on the franchisor to provide the franchisee with notice, an opportunity to cure the breach, or both before the franchise relationship can be terminated. Like the good cause requirement, the time periods required to be provided by a franchisor to cure a default or terminate the relationship vary widely. Generally speaking, the state franchise relationship laws can be broken down into three categories when analyzing cure periods: (1) those state laws that require the franchisor to provide the franchise with a “reasonable” opportunity to cure but do not mandate a specified number of days to cure, (2) those that provide for a specified number of days to cure, and (3) those that do not mandate a cure period.

The first category includes California, Hawaii, Illinois, Michigan, and Washington. All of them impose an obligation on the franchisor to provide the franchisee with a “reasonable” cure period.<sup>17</sup> In each except Hawaii, this cure period need not be more than thirty days long, implying that it could be much shorter as long as it is deemed reasonable.<sup>18</sup> Each of these states also requires the franchisor to provide a termination notice but does not specify a period that must pass between the time such a notice is issued and the effective date of termination.

Arkansas, Maryland, Minnesota, Rhode Island, and Wisconsin, on the other hand, remove much of the franchisor’s discretion in determining the length of the cure period because they impose a cure period of a specified number of days depending upon the default. Generally speaking, Arkansas, Maryland, and Rhode Island require thirty days, and Minnesota and Wisconsin require sixty days. These cure periods decrease to ten days in Rhode Island and Wisconsin if the default is financial; and ten days in Arkansas if the default is one in a series of repeated failures in a twelve-month period to substantially comply with the nondiscriminatory requirements of the franchise agreement, or if the franchisee does not act in good faith and in a commercially reasonable manner.<sup>19</sup>

Each of these states also requires a notice period prior to termination in addition to the cure period. For example, in Minnesota, although a sixty-day cure period is required, the franchisor must also provide ninety days’ notice prior to termination of the relationship. The notice periods range from ninety days in Arkansas and Wisconsin to sixty days in Maryland and Rhode Island. However, as with the cure periods specified above, in many cases these notice periods decrease depending upon the type of default.

# PRACTICE POINTERS

## Drafting Notices of Default and Termination

**Be clear, specific, and concise.** The notice should clearly specify the defaults under the franchise agreement and how long the franchisee has to cure the defaults.<sup>1</sup>

**State what events will constitute cure.** This is easy in a monetary default situation, i.e., payment of the amount outstanding by a date certain. But it may not be as clear for nonmonetary defaults, such as failure to maintain certain standards or to meet construction timelines and the like.

**Consider using interim milestones.** In nonmonetary default situations, more time may be needed to cure the default than what is required by law or the franchise agreement. In this situation, a franchisor may be within its rights to provide only for the minimum cure period required by statute or the franchise agreement. But such an action may trigger a claim for unlawful termination or breach of the covenant of good faith and fair dealing—based upon the fact that the franchisor knew the franchisee could not effect a cure within the allotted time.<sup>2</sup> In this situation, the franchisee could be required to satisfy interim milestones that lead to the ultimate cure. As long as the franchisee has been given the minimum required time period to complete the first step, its failure to complete the first step or an interim step should be appropriate grounds for termination. This approach should forestall any argument that the franchisor was not acting in good faith, and it gives the franchisee a reasonable opportunity to cure the default without the franchisor having to wait 60, 90, or 120 days to find out if the franchisee is actually going to cure.

**Guard against waivers.** Clearly state in the notice of default/termination that its terms cannot be waived or amended by the franchisor unless the waiver/amendment is in writing and signed by an officer of the franchisor. Otherwise, a danger exists that an employee of the franchisor—who may not be aware that the franchisee is in default—may do or say something that could lead to a claim of waiver or amendment of the provisions of the notice. This is a very real concern in larger organizations where various personnel may be working with the franchisee on different matters.

**Preserve rights.** Specifically indicate in the notice of termination that (1) the termination does not relieve the franchisee

Finally, Connecticut, Delaware, Indiana, Mississippi, Missouri, Nebraska, New Jersey, Virginia, the Virgin Islands, and Puerto Rico do not specify a cure period for defaults under the franchise agreement. Most require the franchisor to provide notice a specified number of days prior to termination, notably Connecticut, Delaware, Indiana, Mississippi, Missouri, Nebraska, New Jersey, and the Virgin Islands. This notice period ranges from sixty days in Connecticut, Nebraska, and New Jersey to ninety days in Delaware, Indiana, Mississippi and Missouri to 120 days in the Virgin Islands. Virginia and Puerto Rico are the only jurisdictions with relationship laws that do not mandate that any kind of notice be provided to the franchisee prior to termination.<sup>20</sup>

## B. Incurable Default Analysis

For the most part, up to this point, this article has presumed that for every default, there must be a right to cure. That may not always be the case. For example, the default may be of the type for which no cure period is required or that cannot possibly be cured within the time frame allotted for cure by the applicable state relationship law or franchise agreement; or it may be so serious or egregious, such as certain criminal conduct or damage to a franchisor's trademarks, that it could never be cured irrespective of any cure period.

Many state relationship laws attempt to identify certain incurable defaults within the statute by providing no cure period for these defaults, specifically allowing termination without cure for defaults such as abandonment, misrepresentation in the purchase of the franchise, danger to public health and safety, or criminal conduct. However, certain types of defaults can also arise that do not fall under these specific statutory provisions but may nonetheless be incurable. In these circumstances, a franchisor may be left with a Hobson's choice: provide additional time for cure, therefore arguably granting the franchisee rights greater than those required by law; or provide either only the cure period required by law or no cure period at all, thereby possibly subjecting itself to a claim for unlawful termination based upon various theories, including failure to act in good faith.

In this context, the threshold question is "what constitutes an incurable default?" In the general commercial context, courts have often held that when the provisions of an agreement require the terminating party to allow an opportunity to cure, an incurable default occurs only when the nonterminating party breaches the agreement in such an egregious manner that it goes to the essence of the contract.<sup>21</sup> This reasoning was extended to the franchise context in *LJL Transportation, Inc. v. Pilot Air Freight Corp.*, where the court found that when a breach of a franchise agreement goes to the essence of the agreement and is so "exceedingly grave" as to "irreparably damage the trust between the contracting parties," the franchise agreement may be terminated without notice or opportunity to cure.<sup>22</sup>

A line of cases in Wisconsin extends this reasoning to situations in which "bad acts" of the franchisee play a role in the termination. For example, in *Harnischfager Corp. v. Superior Crane Corp.*,<sup>23</sup> the court found that when a franchisee commits certain acts in "bad faith," the franchisor is not subject to the cure provisions of the Wisconsin Fair Dealership Law. In that

case, the manufacturer terminated a dealer for misappropriating its designs and other proprietary material and pirating and selling certain parts. The court found that the franchisor had a high likelihood of success on the merits of its claims; and due to the bad faith of the franchisee, the franchisee was not entitled to the benefits of the Wisconsin Fair Dealership Law. Thus, no cure period was required. Other examples of incurable defaults cited in Wisconsin include a franchisee that was accused of switching the label on products for the purpose of charging higher prices and hiding expired products<sup>24</sup> and an income tax franchisee's failure to file his own tax returns.<sup>25</sup>

Similarly, a Dunkin' Donuts case in Florida provides an example of a type of default considered incurable. In this case,

of any post-term obligations and (2) the termination does not waive and the franchisor specifically reserves any rights it may have against the guarantors of the franchise agreement. Inclusion of #2 should prevent a franchisee from successfully arguing that the termination in some way released the guarantors of the franchisee's obligations from their obligations under their guaranties.

**Review all ancillary agreements.** If these agreements are to be terminated simultaneously with the termination of the franchise agreement, the franchisor must confirm that these agreements contain cross-default language or otherwise allow for termination in such an event. The franchisor should also determine if it is required to provide any additional notices of termination under these agreements.<sup>3</sup>

### Endnotes

1. See, e.g., *Culligan Int'l Co. v. Culligan Water Conditioning, Inc.*, 563 F. Supp. 1265, 1270 (D. Minn. 1983) (finding that under Minnesota law, a notice of termination was insufficient because the notice did not state with particularity what the franchisee was required to do to cure. The notice at issue provided that the franchisee owed sums past due but did not state the specific amounts). However, a subsequent case, *Novus Franchising, Inc. v. Taylor*, 795 F. Supp. 122, 130 (D. Pa. 1992), held that when the unpaid amount is clear, the specific amount does not need to be included in the termination notice).

2. See *Al Bishop Agency, Inc. v. Lithonia-Div. of Nat'l Serv. Indus., Inc.*, 474 F. Supp. 828 (E.D. Wis. 1979) (holding that a franchisor must provide a cure period that is "reasonable" in light of the circumstances, regardless of the statutory requirements. In a situation in which it was impossible for the franchisee to cure within a sixty-day time period, such cure period was held to be per se unreasonable even though it complied with the requirements of the Wisconsin Fair Dealership Law).

3. Franchisors should ensure that franchise agreements and any ancillary agreements contain cross-default provisions. In Virginia, franchisors with these cross-default provisions in their franchise documents are required to highlight this fact to any prospect in a Virginia specific addendum.

the franchisee sold cigarettes to minors in violation of Florida law.<sup>26</sup> The court found that this willful criminal conduct constituted a default under the franchise agreement that did not require a cure period prior to termination.

Minnesota courts have undertaken a similar analysis, as shown by *AAMCO Industries, Inc. v. DeWolf*.<sup>27</sup> In this case, the Supreme Court of Minnesota found that where the franchisee had been accused by the Minnesota Attorney General of committing numerous instances of consumer fraud, providing the franchisee an opportunity to cure would be a "futile gesture," and thus no cure period was required.

Unfortunately, however, not all courts agree on what constitutes an incurable default. Another Wisconsin case, *Manpower*

*Inc. v. Mason*,<sup>28</sup> illustrates the differing interpretation of situations constituting an incurable default and the confusion that can arise in this situation. In *Manpower*, a franchisee operating a temporary employment agency failed to provide I-9 forms to temporary employees, and the franchisor subsequently terminated the franchise agreement based upon this default. The franchisor argued, as in the above cases, that no cure period was required because the breach was incurable as it "went to the essence of the franchise agreement."

The *Manpower* court found instead that an incurable default is "one that the contract provides no opportunity to cure or one that cannot logically be cured." It is not, as some have argued, a breach so serious that it goes to the essence of the contract between the parties. In this regard, the court found that the only immediate remedy for a material default that goes to the essence of the contract is rescission of the agreement, not termination. Although the same outcome, i.e., the franchisee out of the system, takes place, post-termination covenants cannot be enforced against the franchisee when rescission is the remedy.<sup>29</sup>

Another type of incurable default arises in situations in which a default occurs that cannot in actuality be remedied within the specified cure period, or at all. One commonly cited example is a franchisee's failure to satisfy sales quotas within a certain specified time period. For example, if a franchisee does not meet its 2008 sales quota, nothing that the franchisee does in 2009 or going forward can remedy this default. In dealing with the type of default that by its nature cannot be cured within the statutory cure period, some courts have applied a reasonableness standard to the cure period required to be provided.

One example of this analysis was *Wadena Implement Co. v. Deere & Co., Inc.*<sup>30</sup> The franchisor in this case terminated a dealer that failed to meet its annual market penetration requirement. The franchisor provided the dealer with the statutory cure period, but the dealer argued that this cure period did not comply with the requirements of the statute because it was impossible to cure an annual default in sixty days. The court found that when sales performance is measured on an annual basis, it is a practical impossibility to improve sales from the preceding year.<sup>31</sup> Although not explicitly stating that the cure period must be "reasonable," the court reasoned that termination was defective because the franchisor was required to provide a cure period with which the franchisee could practicably comply. In so holding, the court reasoned that to do so, the franchisor may be required to provide the franchisee with an additional sales performance measuring period in which to remedy the breach.

In *Al Bishop Agency, Inc. v. Lithonia-Division of National Service Industries, Inc.*,<sup>32</sup> a Wisconsin court explicitly adopted a reasonableness standard in dealing with this type of incurable default situation. A Wisconsin franchisee had failed to meet its yearly minimum sales goals. The franchisor subsequently provided a notice of termination and complied with the requisite ninety-day notice and sixty-day cure periods required under the Wisconsin Fair Dealership Law. The court nevertheless found that the notice and cure periods were inadequate because it was a logical impossibility for the franchisee to bring up its sales to the point where it would be in compliance with the franchise agreement within sixty days. The court observed that a complete cure

by the franchisee was not necessary and required only that the franchisee take reasonable steps to cure on a going-forward basis.

In a more recent case,<sup>33</sup> a Minnesota district court held that cure in the context of a material breach means to “engage in subsequent conduct that substantially performs or performs without material failure.” Based upon this rationale, one could argue that a franchisee can cure a breach without repairing harm done in the past by simply going forward without a material failure. The court’s opinion in this case indicates that franchisors should consider providing the required cure period under the statute because even a default that appears to be incurable at the time of the notice of default may arguably be cured by the franchisee on a going-forward basis.

Washington statutorily addresses the issue of incurable defaults by providing that if a default cannot be cured within thirty days (the maximum cure period required under state law), the franchisee may initiate substantial and continuing action within the thirty-day cure period to cure the default and therefore render the notice of default void. Accordingly, at least in Washington, franchisors should be aware that although a franchisee’s breach may not be cured by the expiration of the cure period, the franchisor is prohibited from terminating if the franchisee has taken steps to correct the deficiency.<sup>34</sup> In addition, the Maryland Fair Distributorship Act addresses cure provisions in a unique manner, as further discussed in section III.D below.

### C. Buyback Provisions

Even if a franchisor has good cause or another sufficient basis to terminate the relationship and otherwise complies with the notice and cure requirements mandated by contract or an applicable statute, an applicable state relationship law may also impose certain post-termination obligations on the franchisor. In Arkansas, California, Connecticut, Hawaii, Maryland, Rhode Island, Washington, and Wisconsin, the franchisor is subject to buyback provisions requiring the franchisor to repurchase certain items if it terminates the franchise.<sup>35</sup> As with other statutory elements related to termination, the requirements setting forth how and what the franchisor must repurchase vary widely.

States differ as to the circumstances under which a franchisor must buy back items from the franchisee upon termination. Arkansas and California subject the franchisor to a buyback requirement only when the franchise was not terminated with good cause. California’s statute extends the buyback obligation to a franchisor that fails to meet any of the termination requirements of the California Franchise Relations Act.<sup>36</sup> In Arkansas, termination may occur upon good cause or in accordance with the franchisor’s nonarbitrary current policies; however, if the termination is based on the latter, the franchisor must repurchase certain items from the franchisee. In Maryland, the franchisor is subject to the buyback requirement upon all terminations except for termination based upon certain specified “egregious” acts or omissions by the franchisee, including the failure to pay for items received, bankruptcy or insolvency, danger to public health, abandonment, expressly prohibited conduct that materially affects the relationship, bad faith, and other fraudulent or illegal acts.<sup>37</sup> In the remaining buyback states, the buyback requirement is absolute.

States differ as to what items must be repurchased.<sup>38</sup> California, Rhode Island, and Wisconsin require the buyback of the franchisee’s inventory regardless of whether it was purchased from the franchisor. This obligation is limited in other states, including Arkansas, Connecticut, Hawaii, and Washington, which require repurchase of only inventory, supplies, equipment, and furnishings purchased from the franchisor or its approved sources.<sup>39</sup> Maryland requires the repurchase only of merchandise sold by the franchisor to the franchisee. Further, in Arkansas, California, Connecticut, Hawaii, and Washington, the franchisor is not required to repurchase any personalized items of the franchisee. Rhode Island and Wisconsin require the franchisor to repurchase only the inventory and products containing identifying marks of the franchisor. Finally, in Washington, franchisors are not required to repurchase items not reasonably required in the operation of the business; and if the franchisee retains control of the premises, the franchisor is only required to repurchase items purchased based on the express requirements of the franchisor.

Finally, states differ as to the sales price.<sup>40</sup> The Arkansas statute provides that the purchase price must be equal to the franchisee’s net cost less a reasonable deduction for depreciation or obsolescence. Other states tie the purchase price to market value, such as Hawaii and Washington,<sup>41</sup> which require fair market value at the time of termination, and Rhode Island, which requires the fair wholesale market value. California requires purchase at the lesser of (1) wholesale market value or (2) the price paid by the franchisee. In Maryland, the required price depends on the item and the timing of the original purchase of the item.<sup>42</sup>

### D. Jurisdictional Application of State Relationship Laws

As with most aspects of the state relationship laws, states also vary in the jurisdictional application of such laws.<sup>43</sup> On one side of the spectrum are Hawaii, Mississippi, Washington, and the Virgin Islands, which do not include any specific provisions in their statutes regarding jurisdictional application of the termination provisions of such laws.<sup>44</sup> But Arkansas, Connecticut, Illinois, Iowa, Maryland,<sup>45</sup> Missouri, Nebraska, New Jersey, Rhode Island, Virginia, Wisconsin, and Puerto Rico all provide that if the franchised location itself is located within that state, the franchisor must comply with the applicable relationship law.

Slightly more comprehensive are the jurisdictional aspects of the state relationship laws of California and Indiana, which apply either (1) when the franchised location is located in the applicable state; or (2) in California, when the franchisee is domiciled in California, and in Indiana, if the franchisee is a resident of Indiana.

Even more comprehensive are the Michigan Franchise Investment Law and the Minnesota Franchise Act. The Michigan law provides that it applies if the franchised location is in Michigan, the franchisee is domiciled in Michigan, or if the offer to sell the franchise is made or the offer to buy the franchise is accepted in Michigan. The Minnesota law applies when a sale or offer to sell is made in Minnesota, an offer to purchase is made or accepted in Minnesota, or the franchise location is in Minnesota.

When drafting a franchise agreement, franchisors and their

counsel should pay particular attention to the general choice of law provision. Many franchisors choose the law of their home state to govern the franchise agreement. By doing so, these franchisors may unwittingly be subjecting themselves to an argument as to the applicability of that state's relationship law, even if it would not otherwise apply.<sup>46</sup> To protect against this situation, franchisors that are electing a governing state law having a relationship law or relationship provisions in its franchise law should carve out the application of the state relationship law or provisions unless otherwise applicable.

## II. EXEMPT FRANCHISES

This article has presumed that the state relationship laws apply to every franchise relationship and that each franchisor, regardless of any other factors, must comply with that law, assuming the jurisdictional requirements of that law are satisfied. However, that may not uniformly be the case. Accordingly, in those states where the franchise transaction is exempt from the registration provisions of a state disclosure law—whether based upon the characteristics of the franchisor, the franchisee, or the relationship itself—franchise counsel faced with a termination situation should perform a statutory analysis to determine whether that exemption also exempts the franchisor from application of that state's relationship law.<sup>47</sup>

In certain states, the franchise disclosure requirements and the franchise relationship prohibitions are enacted as separate laws, and in others these subjects are addressed in the same statute. The registration states with the latter statutory framework are Hawaii, Illinois, Michigan, Minnesota, Virginia, and Washington.<sup>48</sup> Of these states, only the statute in Illinois provides certain exemptions from the entire statute, including both the relationship provisions and the registration and disclosure provisions, for both a fractional franchise and a franchise that is operated by the franchisee on the premises of the franchisor and incidental to the franchisor's business.<sup>49</sup> The remainder of these states, however, only exempt the franchisor from the registration and, to a certain extent, disclosure provisions of the applicable state franchise law. These exemptions have no effect on the franchisor's obligation to comply with the termination provisions of the applicable state's law.

On the other side of the spectrum are states like California, which has two separate statutes. In California, various exemptions exempt the franchisor from the registration and, in certain circumstances, disclosure provisions contained in the California Franchise Investment Act,<sup>50</sup> but these exemptions do not exempt the franchisor from compliance with the California Franchise Relations Act. Rhode Island is similar. The Rhode Island Franchise Investment Act exempts certain franchisors from its registration requirements, but these exemptions do not exempt the franchisor from the Rhode Island Fair Dealership Act. Wisconsin maintains a similar statutory framework with the Wisconsin Franchise Investment Law and the Wisconsin Fair Dealership Law.<sup>51</sup>

The lone holdout in this regard may be Indiana. The Indiana Deceptive Franchise Practices Act defines a franchise subject to the act as being a franchise as the term is defined in certain

subsections of the Indiana disclosure law.<sup>52</sup> The Indiana disclosure law, however, specifically excludes from its definition what is commonly known as a "fractional franchise."<sup>53</sup> Therefore, in Indiana, it is arguable that a franchisor in a fractional franchise relationship would not have to comply with the limitations on termination contained in the Indiana Deceptive Franchise Practices Act. It is notable that the other states with fractional franchise exemptions, except for Illinois, as noted above, only exempt the relationship from the registration and disclosure requirements of the applicable state law but not from the law's relationship termination provisions. Accordingly, franchisors engaged in fractional franchise relationships in these states should comply with the relationship termination provisions of the applicable state law.

## III. UNIQUE AND OFTEN OVERLOOKED PROVISIONS

### A. California Notice Requirements

The California Franchise Relations Act provides very specific requirements with which the franchisor must comply when drafting a notice of termination. Section 20030 mandates that any such notice must be in writing; sent by registered, certified, or other receipted mail; or delivered by telegram or personal delivery. In addition, the notice must contain a statement of the franchisor's intent to terminate, set forth the reasons for such termination, and include the effective date of termination.

As discussed earlier, a franchisor that fails to comply with the termination provisions of the California Franchise Relations Act will be required to offer to repurchase the terminated franchisee's then-current resaleable inventory. Certain case law in California indicates that this repurchase obligation is the franchisee's exclusive remedy in the event of a termination not in compliance with the act.<sup>54</sup> However, the act specifies that the franchisee may pursue any other remedies it may have under other laws, and another more recent case interpreting California law found that a franchisee may pursue a breach of contract claim seeking damages in the event of a termination without good cause or other unlawful termination.<sup>55</sup>

### B. Connecticut Notice Requirements

The Connecticut statute places extra burdens on the franchisor that leases the underlying premises of the franchised business to the franchisee where that lease terminates upon termination of the franchise agreement. In this situation, in order to effect termination of the franchise agreement and lease, the notice of default must be served upon the franchisee by a sheriff or other indifferent person and must provide in the notice that the lease will terminate upon termination of the franchise. In addition, the notice must provide that the franchisee may have certain rights under the Connecticut statute. Finally, the franchisor also must attach certain sections of the statute to the notice itself.

### C. Iowa Statutory Scheme

Determining the appropriate application of the Iowa relationship

provisions is particularly tricky because Iowa currently has two relationship laws in effect. The Iowa Franchise Act was originally enacted in 1992 but the Iowa legislature adopted a substantially amended statute eight years later. Significantly, the amended statute applies only to franchise agreements entered into on or after July 1, 2000. Both of these statutes contain the same definition of good cause, but some differences exist as to the circumstances constituting good cause and the required mechanics of termination.

Iowa's law also diverges with respect to a franchisor's post-term buyback obligations. Under the 1992 law, the franchisor may not enforce a terminated franchisee's post-term noncompete covenant unless the competing business relies on a substantially similar marketing plan as the terminated business, or the franchisor first offers to purchase the assets of the franchised business for its fair market value as a going concern. This requirement applies only to supplies purchased from the franchisor itself or its agents, and the value of the assets does not include the goodwill of the business attributable to the trademark licensed under the franchise agreement. Additionally, the offer for the assets may be conditioned upon a determination of the fair market value by an impartial appraiser. The amended relationship law does not impose a post-termination buyback requirement on franchisors.

#### **D. Maryland Cure Provisions**

The Maryland Fair Distributorship Act provides for a specific procedure relating to a franchisee's cure of any stated deficiencies.<sup>56</sup> Under § 11-1305, the franchisee may void any notice of default or termination by, within thirty days after receipt of the notice, submitting to the franchisor a notice of its intent to oppose the termination and implementing a plan for the cure of any deficiencies identified by the franchisor. Under this section, both the franchisee and franchisor must "make good faith" efforts to adopt the franchisee's plan, which is subject to franchisor approval; and if the franchisor adopts the plan, the notice of default or termination becomes ineffective. Notably, however, the statute does not apply where the franchisee's defaults are deemed to be incurable. Also importantly, the statute provides that the franchisor may not alter payment, credit, or delivery terms affecting the franchisee during the cure period, thus protecting the franchisee from retaliatory practices by the franchisor.<sup>57</sup>

### **IV. DEFAULT AND TERMINATION PROCESS**

As discussed above, prior to termination, many state relationship laws require the franchisor to provide the franchisee with written notice of the default and, in many cases, an opportunity to cure the default. Even if a state relationship law is not applicable, most franchise agreements give the franchisee a right to cure most defaults before the franchisor can terminate the relationship.<sup>58</sup>

The first question in any termination analysis is whether a state relationship law applies to the termination.<sup>59</sup> Unfortunately, this analysis may well lead to even more questions because of the potential applicability of more than one law

and the conflict between these laws or between these laws and the franchise agreement. In this situation, what law is the franchisor to follow? The best practice is to determine what law, or what parts of the applicable laws, are the most "franchisee friendly" and then comply with those laws. This approach should allow the franchisor to effectively thwart any argument that the franchisor violated a relationship law by complying with an applicable law that did not give the franchisee the greatest protection. A similar situation occurs when the applicable franchise law does not provide protections that are as great as those contained in the franchise agreement. For example, a law may only require ten days to cure a monetary default but the franchise agreement may require a thirty-day cure period. The franchisor should give the franchisee the greatest protections and comply with its franchise agreement, again to forestall any claim that the franchisor breached the franchise agreement.

One other area that can haunt a franchisor is a failure to provide the required time period to cure any default or to terminate the agreement. This should be fairly straightforward. The franchisor looks to the applicable law and the franchise agreement for the number of days required to cure the default or to terminate the agreement and provides the franchisee with the appropriate number of days. However, if this is all the franchisor is looking at, a claim of wrongful termination may result. The notice provision of the franchise agreement must be scrutinized to determine how that provision affects the number of days the franchisor is required to provide. For example, many notice provisions provide that the notice is not effective until a specified number of days after it is sent, depending on the delivery method. If the franchisor does not take these days into account when calculating the time period for curing a default or terminating the agreement, it is arguable that the franchisor has failed to provide the franchisee with the appropriate time period. Further, if the notice was sent by improper means, it could be argued that the time period did not start to run.

As there are different strokes for different folks, there are different types of notices for different types of situations. The type of notice is for the most part dictated by the applicability of a state relationship law. To that end, the most prominent notices are notices of default and notices of termination. However, a hybrid notice that can be used is a notice of default and termination. As discussed above, some state relationship laws require time periods to cure, others do not require any cure period but do require notice a specified number of days in advance of termination, and still others require both a cure period and a termination notice period.

One state requiring both a cure period and a notice of termination period is Minnesota. The Minnesota Franchise Act generally requires a franchisor to provide a franchisee with a period of sixty days to cure most defaults and ninety days' notice prior to termination of the relationship. This does not mean that a franchisor must wait 150 days before terminating the franchise relationship. Rather, the franchisor can provide the franchisee with a notice of default and termination giving the franchisee sixty days to cure the default and notifying

the franchisee in that notice that if the default is not cured within the sixty-day period, the franchise agreement will terminate ninety days after the date of the letter. This limits the entire time period to ninety days because the ninety-day time period for termination will run concurrently with the sixty-day cure period.

A couple of words of caution with respect to using notices of default and termination:

- Certain state relationship laws arguably require two notices, one that deals with the default and another that deals with the termination.
- The language of the franchise agreement should be reviewed carefully. Many franchise agreements contemplate two notices, a notice of default and a second notice of termination if the notice of default is not cured.
- If the franchisor sends a notice of default and termination and the franchisee fails to cure, the franchisor must be prepared to pursue its post-term rights under the franchise agreement. Failure to do so may lead to a claim of waiver in the current case or waiver or discrimination in subsequent cases.

## V. PRETERMINATION OPTIONS OF THE FRANCHISOR

Many franchisors are frustrated by the lack of options provided by most franchise agreements in dealing with defaulting franchisees. Most agreements provide only for notice and termination but do not give the franchisor any rights in the interim period. Arguably at this point in the relationship, the franchisor's goodwill is at greatest risk because it may be negatively affected by the defaulting franchisee. Franchisors with franchise agreements that do not contain language providing the franchisor with different options during this period may be able to do nothing except wait for the cure periods to expire and terminate the agreement, assuming no cure. Just as a franchisee cannot withhold royalty payments to a franchisor who it claims is in default under the franchise agreement,<sup>60</sup> a franchisor cannot withhold services to or support from a franchisee that is in default unless the franchise agreement provides such a right.

For the most part, language providing the franchisor with the right to withhold services or other benefits during this interim period is limited only by the creativity of the drafter. The services and benefits that the franchisor may withhold vary by system and industry<sup>61</sup> but usually include removal of the franchisee from any advertising published by the franchisor and any website of the franchisor, termination of the franchisee's right to receive leads from the franchisor, and termination of the franchisee's right to attend meetings or seminars sponsored by the franchisor.

If a franchisor adopts this concept in its franchise agreement, it should consider the following points. First, the franchisee may see the franchisor's actions as a constructive termination of the franchise agreement.<sup>62</sup> Accordingly, the franchisor should be sure not to take any actions that would effectively

deprive the franchisee of the essential benefits of the franchise agreement. To that end, the franchisor should add language to the agreement whereby the franchisee acknowledges that the franchisor's specified pretermination actions do not constitute a constructive termination of the franchise agreement. The franchisor should also include language in the agreement allowing the franchisor to take any such actions until the franchisee cures its defaults under the franchise agreement and the franchisor has acknowledged the cure in writing. Finally, the franchisor should be sure to provide that the franchisor's taking of any such actions does not suspend or terminate the franchisee's obligations to the franchisor or its affiliates under the franchise agreement or otherwise.

## VI. CONCLUSION

Because of the serious consequences and potential complications associated with terminating the franchise relationship, the decision on whether to take this action is one that should not be entered into lightly. In fact, many argue that termination should be used as a last resort only when all other measures have failed. Regardless of one's position on this point, one thing is undisputed. The termination notice will in many cases result in a lawsuit by the franchisee in an attempt to prevent termination or by the franchisor if the franchisee ignores the termination and fails to comply with its post-term obligations under the franchise agreement. For this reason, the franchisor must take great care to ensure that it has performed a thoughtful analysis of the reasons for termination and has satisfied all applicable laws and contractual provisions governing termination of the franchise relationship. To that end, the franchisor should first confer with its counsel to confirm that its default/termination analysis is correct as many times the notice will be Exhibit A in an improper termination case.

## Endnotes

1. See *Quiznos Franchising II, LLC v. Zig Zag Rest. Group, LLC*, Bus. Franchise Guide (CCH) ¶ 14,046 (D. Colo. 2008) (finding that a franchisor's termination of a franchise agreement and conduct surrounding the termination was unreasonable, and thus the terminated franchisee was entitled to rescissory damages, including recovery of direct investment, lost alternative investment opportunities, and the costs of default on a real estate lease); see also *Otto Dental Supply v. Kerr Corp.*, Bus. Franchise Guide (CCH) ¶ 14,025 (D. Ark. 2008) (finding that a manufacturer may be liable for treble and punitive damages for an alleged unlawful termination of a distributor under the Arkansas Franchise Practices Act).

2. Although the Petroleum Marketing Practice Act (15 U.S.C. § 2801) regulates the termination of motor fuel franchises, there is no federal relationship law applicable to franchises generally.

3. Many argued for the adoption of such a law when the FTC Franchise Rule was amended in 2007; however, the FTC determined that the disclosure required by the amended rule allows franchisees to avoid many of the harms that a relationship law would address. See Federal Trade Commission, Amended Franchise Rule Statement of Basis and Purpose, 16 C.F.R. pts. 436, 437, at 15446 (Mar. 2007); Bureau of Consumer Protection, Staff Report to the Federal Trade Commission and Proposed Revised Trade Regulation Rule, 16 C.F.R. pt. 436 (Aug. 2004).



4. This article focuses on state and U.S. territory franchise and dealership relationship laws of general application. As such, termination laws specific to a given industry, such as heavy equipment dealers, are beyond the scope of this article, as well as the coverage of state business opportunity laws that may contain relationship termination provisions and foreign laws limiting a franchisor's right to terminate the franchise relationship. Many relationship laws also restrict a franchisor's right to not renew the franchise relationship. As the focus of this article is on termination, it does not address provisions covering nonrenewal.

5. The authors gratefully acknowledge the following articles: Russell Barrios & William L. Killion, *State Franchise Relationship Laws on Termination: Issues in Litigation*, ABA FORUM ON FRANCHISING (2001); Jason S. Stover, *No Cure, No Problem: State Franchise Laws and Termination for Incurable Defaults*, 23 FRANCHISE L.J. 217 (2004); Genevieve Beck & Ellen R. Lokker, *THE MATERIALITY REQUIREMENT FOR FRANCHISE TERMINATIONS*, ABA Forum on Franchising (2006) materials.

6. See Arkansas Franchise Practices Act, ARK. CODE ANN. §§ 4-72-201 *et seq.*; California Franchise Relations Act, CAL. BUS. & PROF. CODE §§ 2000 *et seq.*; Connecticut Franchises Law, CONN. GEN. STAT. §§ 42-133e *et seq.*; Delaware Franchise Security Law, DEL. CODE ANN. tit. 6, §§ 2551 *et seq.*; Hawaii Franchise Investment Act, HAW. REV. STAT. §§ 482E-6 *et seq.*; Illinois Franchise Disclosure Act of 1987, 815 ILL. COMP. STAT. § 705/18 *et seq.*; Indiana Deceptive Franchise Practices Act, IND. CODE §§ 23-2-2.7.1 *et seq.*; Iowa Franchise Act, IOWA CODE §§ 523H.1 *et seq.*; Maryland Fair Distributorship Act, MD. CODE ANN. §§ 11-1301 *et seq.*; Michigan Franchise Investment Law, MICH. COMP. LAWS §§ 445.1527-27 *et seq.*; Minnesota Franchise Act, MINN. STAT. §§ 80C.14 *et seq.*; Mississippi Franchises Law, MISS. CODE ANN. §§ 75-24-51 *et seq.*; Missouri Franchise Act, MO. REV. STAT. §§ 407.400 *et seq.*; Nebraska Franchise Practices Act, NEB. REV. STAT. §§ 81-401 *et seq.*; New Jersey Franchise Practices Act, N.J. STAT. ANN. §§ 56:10-1 *et seq.*; Rhode Island Fair Dealership Act, R.I. PUB. LAWS §§ 60-50-1 *et seq.*; Virginia Retail Franchising Act, VA. CODE ANN. §§ 13.1-564 *et seq.*; Washington Franchise Investment Protection Act, WASH. REV. CODE §§ 19.100.180 *et seq.*; Wisconsin Fair Dealership Law, WIS. STAT. §§ 135.01 *et seq.*; Puerto Rico Dealers' Contracts Law, P.R. LAWS ANN. tit. 10, §§ 14-278 *et seq.*; Virgin Islands Franchised Business Law, V.I. CODE ANN. tit. 12A, §§ 2-130 *et seq.*

Arguably, Alaska's statute applying to distributorships could be considered a franchise relationship law. ALASKA STAT. § 45.45700.

7. Although no new states enacted relationship laws during this period, Iowa passed a second relationship law that applies to franchise agreements entered into after July 1, 2000.

8. The Mississippi Franchises Law and the Missouri Franchise Act do not expressly require franchisors to have any sort of cause prior to termination. The Maryland Fair Distributorship Act also does not expressly require any specific cause prior to termination, but it does require a franchisor to list all reasons for its action and allow a time to cure in its termination notice. See MD. CODE ANN. § 11-1303. Thus, although not explicitly specified, a for-cause standard may be implied in the Maryland statute.

9. See DEL. CODE ANN. tit. 6, § 2552; VA. CODE ANN. § 13.1-564. Although Virginia's statute references "reasonable cause" as opposed to good cause, it does not define what constitutes reasonable cause.

10. Similarly, the Rhode Island Fair Dealership Act provides that good cause includes the failure to comply with the reasonable requirements imposed by the grantor. R.I. Pub. Laws § 6-50-2(4).

11. See HAW. REV. STAT. § 482E-6(2)(H). If standards are not equally applied across the system, the franchisor may still prove that any

classification or discrimination among franchisees is reasonable, not arbitrary, and based upon proper justifiable distinctions.

12. See ARK. CODE ANN. § 4-72-202(7).

13 For example, Delaware and Indiana not only require good cause but that the termination not be in bad faith. See DEL. CODE ANN. tit. 6, § 2552; IND. CODE ANN. § 23-2-2.7-1(7).

14. See IOWA CODE § 523H.7.

15. See WIS. STAT. § 135.02(4); V.I. CODE ANN. tit. 12A, § 132.

16. The Puerto Rico law also lists several situations in which it is presumed that the franchisor does not have just cause to terminate the franchise agreement. See Puerto Rico Dealers' Contracts Law, P.R. LAWS ANN. tit. 10, § 278a-1.

17. However, California, Illinois, and Washington do not require the franchisor to provide the franchisee with any opportunity to cure in certain specified circumstances, which include the franchisee's bankruptcy or assignment on behalf of creditors, noncompliance with laws after notification, criminal misconduct or violation of franchise laws, repeated defaults, failure to pay sums due within five days of an overdue notice, or the existence of an imminent danger to public health. These types of defaults would be classified as incurable defaults and are discussed below in section I.B.

18. Iowa is a hybrid state in that it arguably fits into each of the first two categories, requiring a reasonable opportunity to cure that must be at least thirty days long but no more than ninety days.

19. Just like the statutes in California, Illinois, and Washington, the statutes of Arkansas, Maryland, Minnesota, Rhode Island, and Wisconsin allow for immediate termination without any cure period in certain situations.

20. Nevertheless, the authors would always recommend written notices of termination.

21. See, e.g., *Olin Corp. v. Cent. Indus., Inc.*, 576 F.2d 642 (5th Cir. 1978); *D.C. Films, Inc. v. Best Film & Video Corp.*, 46 Bankr. 861 (E.D.N.Y. 1985).

22. Bus. Franchise Guide (CCH) ¶ 14,058 (Pa. Jan. 22, 2009). Note that in this case, the relationship was not governed by a state relationship law, and the court interpreted the agreement between the parties.

23. Bus Franchise Guide (CCH) ¶ 10,618 (E.D. Wis. 1995).

24. *Miller Brewing Co. v. Hoff Distrib. Co. Inc.*, No. 82-CV-159 (Wis. Cir. Ct., Portage County Oct. 28, 1992).

25. *H & R Block, Inc. v. Otto*, No. 80-CV-7409 (Wis. Cir. Ct., Dane County May 5, 1980).

26. See *Dunkin' Donuts, Inc. v. Chetminal, Inc.*, Bus. Franchise Guide (CCH) ¶ 11, 290 (S.D. Fla. 1997). The termination was not subject to a state relationship law, and the court was interpreting contract terms.

27. 250 N.W.2d 835 (Minn. 1977).

28. 377 F. Supp. 2d 672 (E.D. Wis. 2005).

29. *Id.* at 679-80.

30. 480 N.W. 2d 383 (Minn. Ct. App. 1992). Note that this case interprets the Minnesota Agricultural Equipment Dealership Act, a statute described as "nearly identical" to the Wisconsin Fair Dealership Law. See Stover, *supra* note 5, at 222.

31. *Id.* at 388.

32. 474 F. Supp. 828 (E.D. Wis. 1979).

33. *Anacapa Tech., Inc. v. ADC Telecomms., Inc.*, 241 F. Supp. 2d 1016, 1019-20 (D. Minn. 2002).

34. The Washington statute also provides that the franchisor may terminate the franchise agreement without an opportunity to cure upon the

franchisee's fourth breach in a one-year period of the same provision of the franchise agreement, if the breach is willful, and if the franchisor gives proper notice and opportunity to cure for the prior three breaches. See Washington Franchise Investment Protection Act, WASH. REV. CODE ANN. § 19.100.180(j).

35. Iowa also imposes a buyback requirement. See *infra* section III.C.

36. In this event, franchisees may also have additional remedies. See *infra* section III.A.

37. See Arkansas Franchise Practices Act, ARK. CODE ANN. § 4-72-209; California Franchise Relations Act, CAL. BUS. & PROF. CODE § 20035; Delaware Franchise Security Law, DEL. CODE ANN. tit. 6, § 2553(c)(1); Maryland Fair Distributorship Act, MD. CODE ANN. § 11-304.

38. See California Franchise Relations Act, CAL. BUS. & PROF. CODE § 20035; Rhode Island Fair Dealership Law, R.I. PUB. LAWS § 6-50; Wisconsin Fair Dealership Law, WIS. STAT. § 135.045; Arkansas Franchise Practices Act, ARK. CODE ANN. § 4-72-209; Connecticut Franchise Act, CONN. GEN. STAT. § 42-133f(c); Hawaii Franchise Investment Law, HAW. REV. STAT. § 482E-6(3); Washington Franchise Investment Protection Act, WASH. REV. CODE § 19.100.180(i).

39. However, because many franchise systems require the franchisee to purchase most, if not all, items from the franchisor or an approved supplier, this distinction may be illusory.

40. See *id.*

41. As noted in *Coast to Coast Stores, Inc. v. Gruschus*, Bus. Franchise Guide (CCH) ¶ 8040 (Wash. 1983), the actual price determined by fair market value can vary widely. In this case, the court found that the price of items purchased at a "commercially reasonable sale" was the measure to be used for determining fair market value under the statute.

42. For example, if the product is still in its original condition, is part of the franchisor's current product line, and was shipped within six months of the termination, the franchisor must pay the original purchase price. The purchase price for special tools, accessories, and display equipment is the price paid by the franchisee, less depreciation. Finally, the purchase price of other merchandise is the lesser of either wholesale fair market value less depreciation or the purchase price paid by the franchisee. See Maryland Fair Distributorship Act, MD. CODE ANN. § 11-1304.

43. Note that under principles of constitutional law, the relationship laws would not apply to contracts that were entered into prior to the adoption of the law, when the law substantially impairs the preexisting contractual relationship. See, e.g., *McDonald's Corp. v. Nelson*, 822 F. Supp. 597, 609 (S.D. Iowa 1993).

44. The most conservative approach in these cases is to comply with the state relationship law if the offer is made or accepted in such state, the franchised location is in that state, or the franchisee is a resident of such state.

45. Franchisors regulated under the Maryland Franchise Registration and Disclosure Law are exempt from the Maryland Fair Distribution Act, Maryland's relationship law. Specifically, the relationship law provides that "notwithstanding any other provisions" of the subtitle, the subtitle does not apply to "a franchisor regulated under the Maryland Franchise Registration and Disclosure Law." MD. CODE ANN. § 11-1302(b).

46. See *Century Pac., Inc., Becker Enters., Inc. v. Hilton Hotels Corp.*, Bus. Franchise Guide (CCH) ¶ 12,800 (S.D.N.Y. 2004), in which two franchisees, a Texas corporation and a Nevada corporation, brought claims against the franchisor under the New York Franchise Sales Act (NYFSA), claiming application of this act because the choice of law provision provided for the laws of the State of New York.

The court declined to apply the NYFSA to the dispute because the franchise agreement expressly excluded its application unless it would otherwise apply.

As an aside, the franchisor that attempts to contract around a state relationship law that would otherwise apply by indicating that the parties waive application of the law will generally lose this battle based upon the antiwaiver provisions of the applicable state relationship law. See, e.g., California Franchise Relations Act, CAL. BUS. & PROF. CODE § 20010. The franchisor that chooses application of a different state law may be more successful. For example, in *Armstrong Business Services, Inc. v. H & R Block*, the court determined that the choice of law provision in the agreement between the parties superseded contrary requirements of state laws. 96 S.W.3d 867, 873 (Mo. Ct. App. 2002).

47. As discussed above, those franchisors regulated under the Maryland Franchise Registration and Disclosure Law are exempt from Maryland's relationship law. In an interesting twist, one could argue that franchisors exempt from registration under the Maryland disclosure law would have to comply with the Maryland relationship law because they would then not be "regulated" under the disclosure law. However, it appears that the definition of *franchise* under the Maryland registration law would still consider as exempt franchisors offering and selling franchises regulated by the Maryland disclosure law; and, accordingly, those franchisors would not have to comply with the Maryland relationship law.

48. See Hawaii Franchise Investment Law, HAW. REV. STAT. § 482E-4-1; Illinois Franchise Disclosure Act, 815 ILL. COMP. STAT. 705/9; Michigan Franchise Investment Law, MICH. COMP. LAWS § 445.1506; Minnesota Franchise Act, MINN. STAT. ANN. § 80C.03; Virginia Retail Franchising Act, VA. CODE ANN. § 13.1-560; Washington Franchise Investment Protection Act, WASH. REV. CODE ANN. § 19.100.180.

49. See Illinois Franchise Disclosure Act, 815 ILL. COMP. STAT. 705/13. An additional exemption from the entire statute applies to a franchise agreement offering a franchise for a bona fide service for evaluation or certification of goods or services. All other exemptions from registration and disclosure in the Illinois statute are still subject to the relationship provisions.

50. California Franchise Investment Act, CAL. BUS. & PROF. CODE § 31000. Certain of these exemptions also only require the franchisor to provide limited disclosure to the franchisee and, in at least one situation, exempt the franchisor from disclosure altogether.

51. See Rhode Island Franchise Investment Act, R.I. PUB. LAWS § 19-28.1-6; Wisconsin Franchise Investment Law, WIS. STAT. § 553.22.

52. See Indiana Deceptive Franchise Practices Act, IND. CODE ANN. § 23-2-2.5, § 5.

53. See Indiana Franchise Law, IND. CODE ANN. § 23-2-2.5.1. Certain exemptions other than the fractional franchise exemption exist within the Indiana Franchises Law; however, such exemptions only apply to certain subsections of the statute, and these franchises are still included in the definition of *franchise* within the law. Thus, such exempt franchisors are still subject to the Indiana Deceptive Franchise Practices Act.

54. See *Boat & Motor Mart v. Sea Ray Boats, Inc.*, 825 F.2d 1285 (9th Cir. 1987).

55. See *JRS Prods., Inc. v. Matsushita Elec. Corp. of Am.*, 115 Cal. App. 4th 168 (Ct. App. 2004).

56. Maryland Fair Distributorship Act, MD. CODE ANN. § 11-1305.

57. *Id.* § 11-1303(a)(2)(iv)(c).

58. This presumes that the default is not an incurable default.

59. The franchise agreement and the receipt pages of the UFOC

or FDD given to the franchisee should be reviewed to confirm that no issues exist with regard to the franchise agreement that may adversely affect the franchisor's rights. For example, the name of the franchisee on the front of the franchise agreement should be the same as the name of the franchisee signatory. Personal guarantees, if applicable, must be duly executed; and any amendments to the franchise agreement that may adversely affect the franchisor's rights should be identified. The receipt pages should also be reviewed to confirm that all pre-sale waiting periods were satisfied and, with respect to a transaction post-Amended Rule, that the franchise seller information was appropriately disclosed. If violations of the law are found, the applicable statute of limitations should be examined to see if any claims that the franchisee may have against the franchisor based upon the violation are barred.

60. *See, e.g.*, *Burger King Corp. v. Hall*, 770 F. Supp. 633 (S.D. Fla. 1991).

61. For example, in a lodging system, the language may give the franchisor the right to terminate the franchisee's right to use a reservation system.

62. *See, e.g.*, *Am. Bus. Interiors, Inc. v. Haworth, Inc.*, *Bus. Franchise Guide (CCH) ¶ 8642* (8th Cir. 1986) (finding that a manufacturer effectively terminated a dealer by refusing services to the dealer during the ninety-day notice of termination period required under the Missouri Franchise Law. In this particular case, the manufacturer refused to provide price information to the dealer, thus interfering with the ability of the dealer to order products).