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Mandatory Arbitration of GM and Chrysler Dealer Terminations

Did It Work?

By Peter R. Silverman

In 2009, Chrysler and General Motors declared bankruptcy and terminated almost 2,000 of their dealers as part of overall restructuring. The dealers turned to Congress for relief. Congress responded by passing a bill, signed into law on Dec. 16, 2009, providing for mandatory arbitration for dealers seeking reinstatement.

Congress set aggressive deadlines for finishing the arbitrations. By Jan. 15, 2010, Chrysler and GM had to provide terminated dealers with the criteria used to terminate them. Dealers had until Jan. 25 to decide whether to invoke arbitration to contest the termination. Congress designated the American Arbitration Association ("AAA") to administer the arbitrations and required that the hearings be held in the dealer's state. Only limited document discovery was allowed, and each party was responsible for its costs and fees. All arbitrations had to be completed by June 14, 2010, which arbitrators could extend for 30 days for good cause.

Also, Congress set a broad legal standard for determining whether to reinstate a dealer: The arbitrator was required to balance the economic interest of the dealer, the manufacturer, and the public to decide whether the dealership should be reinstated. In doing so, the arbitrator was required to review seven specific factual matters, including the dealership's profitability, the manufacturer's overall business plan, the dealership's economic viability, whether the dealership met performance objectives in its franchise agreement, and the dealership's experience and length of service. The arbitrator's award could decide only whether the dealer should or should not be reinstated, and could not include damages.

The AAA responded promptly to the legislation and sent out a request to select panel members to serve, explicitly advising them they would need to represent that they would set aside the time to complete multiple arbitrations within the

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Expert Testimony And the Changes To FRCP Rule 26

Discovery of Electronically Stored Information and The Changes to Illustrative Form 52

By Bruce S. Schaeffer and Henry Chan

Federal rules will soon be changing to apply the work-product protections of Federal Rules of Civil Procedure Rule 26(3)(A) and (B) to experts' draft reports and expert-attorney communications. According to the report that led to these rule changes ("Report of the Judicial Conference Committee on Rules of Practice and Procedure to the Chief Justice of the United States and Members of the Judicial Conference of the United States"), this means such documents will no longer be discoverable except for:

- those that relate to the expert's compensation;
- facts and data provided by counsel that the expert considered; and
- assumptions provided by counsel that the expert considered.

The amendments will be effective Dec. 1, 2010, pursuant to ratification of the proposals by the U.S. Supreme Court on July 15, 2010; however, care must be taken because the changes will not be applied retroactively. Thus, it may be wise for counsel to request discovery delays

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in the next few months to give their experts the protection of the upcoming changes.

The report notes that expert testimony has become critical to the litigation process and that the new rules will eliminate the "tortuous" procedures experts had to take to avoid preparing draft reports, taking notes, or making records of preliminary opinions.

The rationale for the changes was basically common sense. The Report of the Judicial Conference Committee states: "The advisory committee was satisfied that discovery into draft reports and all communications between the expert and retaining counsel was not an effective way to learn or expose the weaknesses of the expert's opinions; was time-consuming and expensive; and led to wasteful litigation practices to avoid creating such communications and drafts in the first place."

The report also noted that the changes would remove the need to use two sets of experts — consulting and testifying — often the current practice. However, nothing in the Rule 26 changes affects the court's gatekeeping functions under *Daubert*.

The report makes clear that it was primarily law professors who had sought the total discovery regimen of the old Rule 26. But it was practitioners who argued strongly that the system was unworkable and caused litigators to resort to two sets of experts and a whole host of other specially designed procedures to get around the discovery rules. The new rules are an acceptance that practicality should trump egghead theories.

How the Rule Change Affects Experts

As someone who has provided expert and consulting services during the tenure of the old Rule 26, author Bruce S. Schaeffer can offer the following observations:

1. Cryptic billing. Under the old rules — and continuing under the new rules because the financial arrangement with an expert is still subject to discovery — experts have learned to use only the most generic language in preparing bills. Why? Because too much detail only opens the expert to more hostile questions from opposing counsel in the nature of "Aren't you being paid for this engagement?" and generates much heat but no light.
2. No e-mail correspondence. When working within Rule 26, experts have learned to use e-mail as infrequently as possible because it will become discoverable. This will change with the new rules and will reintroduce the efficiency of the electronic age into communications between expert and counsel.
3. Excessive phone discussions. Because of the general e-mail prohibitions, discussions between experts and counsel have been predominantly by phone. This removes the good-sense editing function that can be accomplished through written communication and may lead to misunderstandings among members of the same team. Under the new rules, I imagine there will be many and more-concise written memos exchanged between counsel and experts.
4. Working report only. Under the current Rule 26 regimen, experts have learned never to use drafts, but instead rely on

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Arbitration

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time limits, and that they would be expected to limit their fees. Based on the response, the AAA picked a group of panel members to circulate to parties for streamlined selection. (Disclosure: I was on the panel and was selected for 10 cases.)

The AAA provided extensive training to the arbitrators. The goal was to encourage a process that would be streamlined, user-friendly, and reasonably consistent nationwide. For example, arbitrators were encouraged to engage the parties to determine whether they wanted to combine certain aspects of multiple hearings, such as having experts testify once for use in all hearings, or whether parties wanted to use affidavits or other time- and cost-saving procedures.

Dealers filed almost 1,600 cases, and all were closed by July 23. About 1,000 cases were resolved before an administrative hearing was held in the case. In total, 160 cases were tried through to award, but the AAA does not release information on results.

Participant Reaction

Participants have written very little about the process. I sent out a general request for opinions on the ABA Forum on Franchising ListServe, but I received only one substantive reply. It came from a dealer's lawyer, who expressed disappointment that the AAA administratively decided that the location of all hearings would be in his state's largest city, which added cost for his dealer clients from all around the state.

One published article to date has summarized the experience of Dady & Gardner, P.A., one of the nation's premiere franchisee firms (www.bluemaumau.org/9089/chrysler_dealer_reinstated_through_arbitration). According to the article, Michael Dady said his clients were very pleased with the results of the process, stating that "[o]f the 25 cases our firm was honored to be asked to handle for adversely affected dealers, 20 of our dealer clients are being reinstated, and five have settled their claims for cash settlements acceptable to them."

One of Dady & Gardner's cases went all the way to award. It's the only public review of an award that I'm aware of. The hearing in that case was held on June 9-11, the briefs were due June 18, and the award was issued on June 25. According to the article, the award analyzed each of Congress' seven statutory factors in detail, noting that some favored the dealer and some favored the manufacturer. After what appears to be a careful and thorough review of all the specified balancing factors, including the public interest of consumers, the arbitrator found in favor of reinstatement.

The debate about the benefits of arbitration and ways to reform the process is complex and multi-faceted. But Congress and the AAA seem to have gotten it right on this one.

Based on this limited public commentary on the process, drawing conclusions is tricky. But I think it's fair to say that when processes are unfair, it's common for those upset with the process to voice their complaints and criticism loudly and often. To the extent that's true, the absence of complaints and criticism suggests that the parties to the process were reasonably satisfied.

Lessons Learned

More data need to be gathered before drawing definitive conclusions from the overall process. But some preliminary issues can be considered now. First, one interesting aspect of the process is that Congress chose mandatory arbitration as the best vehicle for delivering a fast, cost-effective, fair procedure. And it did so at the same time it's considering the Arbitration Fairness Act, which would ban mandatory arbitration agreements in franchise agreements. How can this apparent inconsistency be squared?

Supporters of the Arbitration Fairness Act might claim that this is comparing apples and oranges; that mandatory arbitration may be appropriate for an emergency situation like the dealer terminations, but it's not appropriate for ordinary-course franchise agreements. Further, Congress dictated the terms of these arbitrations, whereas franchisors dictate the terms in the franchise agreement.

While these are valid points, the dealer arbitrations do show how mandatory arbitration — if fairly structured — can be an excellent tool for resolving franchise disputes quickly, inexpensively, and fairly. The time pressures created by the tight deadlines in the auto dealer arbitrations resulted in many settlements, and arbitrators were explicitly instructed to seek cost savings in the arbitration procedures. Furthermore, even in the cases that were tried, the awards were issued within six months of the case's initiation (if a dealer received a favorable judgment).

The debate about the benefits of arbitration and ways to reform the process is complex and multi-faceted. But Congress and the AAA seem to have gotten it right on this one. We should all look hard at the process as it is analyzed over the upcoming months to see what we can learn about making dispute resolution faster, cheaper, and fairer for franchisors and franchisees.

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Rule Changes

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a "working" report on which revisions simply overwrite prior paragraphs. Why? Again, it's to avoid monstrous cross-examinations that focus more on what experts considered cosmetic changes or rejected opinions than on the opinions they came to. This can cause disputes between counsel and the experts retained by them because nobody has a prior draft to show where the changes came from. But under the current (old) rules, it is a small price to pay to avoid senseless and often *ad hominem* attacks by opposing counsel on portions of a report that may be irrelevant, for example, if they were originally copied from a report for a prior engagement.

5. Internet-based review prior to delivery of final report. Another of the circumventions devised in the relationships between counsel and experts is the electronic review of working reports without delivery. This gets around the need to disclose "drafts" and allows some form of continuing update from both counsel and experts before delivery of the final report. This legal subterfuge will no longer be necessary under the new rules because "drafts" will no longer be discoverable.

How the Rule Change Affects e-Discovery

There are also changes to Illustrative Form 52 "Report of the Parties Planning Meeting" to be prepared after the Rule 26(f) conference. Particular note should be paid to Paragraph 3(b), which reads as follows: "(b) Disclosure or discovery of electronically stored information should be handled as follows: *(briefly describe the parties' proposals including the form or forms for production).*"

In author Henry Chan's experience as a computer forensics expert, he has found it is always better (and cheaper, in the long run) to engage e-discovery experts before there's trouble, rather than after. Only a fool ignores what should be learned from experience. Here are a few things Chan has learned.

Lesson #1: The day of the 26(f) conference is not the time to develop a party's proposals relating to the form or forms for production. It is always better to have company policies and procedures in place, such as implementing an archiving system, long before the 26(f) conference. Because of the vast amounts of data created in the course of doing business and the courts' imposition of stricter discovery requirements, a system for managing Electronically Stored Information ("ESI") is critical.

Lesson #2: In a past engagement, a plaintiff decided that data from its backup tapes, not archived data, were enough to make the case a "slam dunk." But such backup tapes are generally not admissible because the rules of evidence demand that parties use the correct forensic processes and procedures in collecting and copying ESI; and courts have begun to impose sanctions on counsel for failing to adequately supervise a client's collection and preservation of ESI. In a recent case, the court sanctioned both the client and its outside attorney, noting that although neither had acted in bad faith, sanctions were appropriate because outside counsel "simply did not understand the technical depths to which electronic discovery can sometimes go." (*In re A&M Florida Properties*. No. 09-01162, 2010 WL 1418861, at *6-7 (S.D.N.Y. Apr. 7, 2010).

Backup data is not the same as archived data, and the methods for collecting evidence on drives must adhere to strict imaging procedures. A forensic examiner makes what's called a "raw" or "dd" ("data dump") image of an evidence drive. In a dd image, the content of the evidence media is bit streamed directly to a file without adding any header information or Cyclical Redundancy Check ("CRC") and hash values. The content of the drive being imaged is copied (by default) in data "blocks" of 32KB, and each block is subjected to a CRC, which mathematically verifies the accuracy of the data in the block. The CRC value for each block is stored after the block. When all of the data are imaged, an MD5 hash value for the acquired data is appended to the file. The important point here is that the content of the evidence drive being imaged is mirrored exactly in ones and zeros. If you take that data by itself and lay it out in a new file as a single continuous sequence, you'll have all the same ones and zeros as exist on the evidence drive in exactly the same sequence.

Lesson #3: To deal with what could easily amount to terabytes of ESI, all franchise companies are advised to implement an archiving system right now — even if no litigation is currently anticipated. Then, in the event of a dispute, e-mail and file archiving will allow the company's legal, IT, and compliance teams to locate, preserve, and produce relevant ESI and will help with enforcement of the company's document retention and "legal hold" policies. Otherwise, a party is confronted with the dilemma of having to build a firetruck during the fire.

Lesson #4: The case law makes clear that issuing written "legal holds" is essential to comply with the new ESI rules. And the holds must be communicated appropriately to all department heads, IT personnel, and pertinent support staff. Internal automatic destruction must also be suspended, which includes halting defragmentation software and other forms of automatic or routine drive "cleanup" activities.

Conclusion

The new rules will bring good sense to discovery with respect to expert witnesses. They also serve to emphasize the need to properly organize and preserve ESI using e-discovery experts before and during litigation or arbitration.

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NEWS BRIEFS

FDA Issues Menu-Labeling Guidance; Enforcement Still Several Months Away

Franchisors now have a better glimpse at new requirements for restaurant menu labels, after the Food and Drug Administration ("FDA") released two guidance documents under the massive health care bill known as the Patient Protection and Affordable Care Act ("PPACA"). The menu-labeling provisions are designed to standardize rules across the country, in response to increasing numbers of municipalities enacting individual statutes.

"The law explicitly recognizes that uniformity is designed for restaurants with 20 or more units under a similar brand that operate across multiple jurisdictions," stated the International Franchise Association ("IFA"), adding that the organization supports uniformity.

The FDA issued two guidance documents on Aug. 25. The first document states that menus or menu boards displayed at restaurants (as well as menus on Web sites) must contain the following disclosures:

- the number of calories in each standard menu item "as usually prepared and offered for sale" in a "clear and conspicuous" manner that is "adjacent to" the name of the standard menu item;
- a statement that puts the calorie information in the context of a total daily caloric intake; and
- a statement regarding the availability of additional nutrition information (in 10 categories, such as total fat, saturated fat, cholesterol, and dietary fiber).

The guidance also states that movie theaters, coffee shops, convenience stores, and vending machines are covered by the law, and that information must be provided about meat and alcohol.

Large franchisors are probably already operating in some localities that have menu-labeling rules, said Kristin Eads, a partner with Faegre & Benson LLP (Minneapolis). "It's a natural extension of what's been going on at the local level," she said. "Those franchisors [already operating under local labeling requirements] might have to design new menu boards and signage. Even restaurants that have not had to comply will find that it's not that tough to do — just sitting down and figuring out the calories and nutritional content in their foods."

Smaller restaurant chains may opt in to the PPACA requirements and seek exemptions from state or local requirements. But states and local governments may petition the FDA for exemption from federal preemption, too.

The biggest threat to restaurants could come from lawsuits spurred indirectly by the new legislation, said Eads. She called it "a very real possibility" that consumer groups will test the foods and challenge restaurants if the disclosures are inaccurate.

The second FDA guidance document is a draft guidance that asks for comments on matters such as disclosure for variable-ingredient items (pizza with different toppings) and custom orders. The guidance also indicates that the FDA will not enforce labeling rules in the finalized guidance document until the issues in the draft document also are finalized — even though some of the rules became effective when the PPACA was enacted in March 2010. This position drew some criticism from the IFA. "The dual track of implementation outlined by the FDA is a regulatory 'shoot-first, ask questions later' approach that will require restaurants to change their menus twice and create confusion among small-business owners and consumers during the process," said David French, IFA senior vice president of government relations and public policy.

The FDA said it anticipates finalizing its guidance in December 2010. "I think the FDA will be thoughtful in its enforcement of the rules because they realize they have kinks that need to be worked out," said Eads.

Century 21 Franchisees Win Nationwide Class Certification

On Aug. 17, New Jersey Superior Court Judge Robert J. Brennan certified a national class action by current and former Century 21® franchisees who alleged that Cendant Corp., which owned Century 21, misused national advertising royalty payments and did not deliver promised support services. Cendant purchased Century 21 in 1995 and instituted a number of operational changes that led to the filing of the lawsuit in January 2002. Today, Century 21 is owned by Cendant spin-off Realogy Corp.

Attorneys for the four representative plaintiffs estimate that at least 1,000 franchisees are covered by the class action, but they say that as many as 4,000 franchisees could be included in the class. "Right now we're working with the defendants to come up with a notification plan for the potential class members," said Dan Drachler, of counsel to the Seattle office of Zwerling, Schachter & Zwerling, LLP, which filed the lawsuit on behalf of the franchisees. "Cendant has the contact information for franchisees during the class period of 1995 to 2002."

On Aug. 18, Realogy issued a press statement, and it would not elaborate further to *FBLA*. The statement said, "The assertions put forth in this litigation are unfounded and without merit. We have capably managed the Century 21 brand since its acquisition in 1995 and have continuously enhanced the brand through many market cycles, including the worst downturn in housing in the history

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of our country. … The claims in this 2002 lawsuit were without merit, and they remain so today. We will aggressively defend against these erroneous claims. This is a class action in which the complaint does not properly reflect the strong relationships we have with our current franchisees."

On Sept. 7, Realogy filed with the appellate court, seeking to appeal to dismiss the class action.

Among the many twists and turns in the litigation, the franchisees at one point were denied class action standing, and they filed an appeal, which was denied. The judge who declined to certify the class action retired, and new opinions from the New Jersey Supreme Court changed the landscape for class actions in the state — both of which developments possibly contributed to the certification this time, according to Drachler.

Franchisees have two primary complaints. The first is about alleged misuse and misappropriation of the National Advertising Fund ("NAF"). Century 21's Master Franchise Agreements required franchisees to contribute 2% of their gross revenue to the NAF. Those fees exceeded $40 million per year at their peak, and franchisees allege that some funds were used by Cendant for purposes not allowed under the terms of the NAF trust.

"All of this started when Cendant bought Century 21 in 1995," said Drachler. "Shortly thereafter, it also bought two of Century 21's competitors, Coldwell Banker and ERA. Coldwell Banker came with a large number of company-owned stores … and franchisees were told that these would be walled-off so that they would not compete with franchises. … Instead, those company-owned stores eventually became part of National Realty Trust when Cendant acquired NRT in 2002. NRT is the world's largest residential real estate brokerage, and a big competitor of Century 21. Funds from the NAF were used by Cendant for its overhead and other expenses that benefited competitors of Century 21, instead of the Century 21 franchisees."

As an example, the lawsuit cites use of NAF funds to pay the salaries of Cendant employees and the breach of the "85-15 Rule" that required that 85% of NAF spending be used to directly promote the Century 21 brand. Also, the franchisees allege that the Century 21 NAF developed a popular real estate Web site, Move.com, which was later sold for a significant profit to Homestore.com. Cendant kept the money, which the franchisees argue belongs to the NAF.

The second set of complaints relates to the 6% "franchise service fee" that franchisees are assessed. "Franchisees allege that Cendant has not been providing the services called for in the franchise agreement and paid for with the service fee, which has now been renamed a 'royalty fee,'" said Drachler. "At the time of Cendant's purchase, Century 21 had an extensive network of regional offices that provided training and support. It had about 5,000 employees. Cendant centralized in New Jersey and reduced staffing to a few hundred people. They eliminated the very successful broker training program, and they did not reduce the service fees to reflect the much lower level of support."

In some ways, it's been a bitter fight, according to Drachler. "Usually, when we work on a class action, it's difficult to get current franchisees who will take on the franchisor; they fear repercussions. The former franchisees are the ones who want to 'get' those guys," said Drachler. "In this situation, it's the opposite. I can't tell you how many active franchisees over the years have called me to say, 'I love Century 21. I hate what's going on now, what Cendant is doing to us.'"

One of the uncertainties in the lawsuit is the number of franchisees who are in the class — the wide discrepancy between the 1,000 identified franchisees and the 4,000 franchisees that plaintiffs' attorneys estimate might be eligible. The discrepancy reflects developments since the lawsuit was filed in January 2002. "Cendant has been trying to whittle down the class by including a release in any modification of a franchise contract," said Drachler, citing specifically franchise renewals that were offered to franchisees in which the only language that was changed was a release about the lawsuit. The first judge in the case prohibited Cendant from presenting those releases, on the grounds that franchisees were not fully informed about the possible class action.

A few years later, according to Drachler, franchisees were offered another modification of the franchise agreement in which Cendant would not enforce the payment of the monthly required minimum royalty fee — which can be difficult for small franchisees working in an industry in which sales are so unpredictable. In exchange for the fee accommodation, franchisees had to release Cendant from the lawsuit. "The original judge allowed these offers to be made because he said he did not want to get involved in the day-to-day interaction of franchisor and franchisee," said Drachler. "Cendant says as many as 2,000 franchisees have signed this agreement, but we don't know at this time."

Given Cendant's actions, Drachler said that the most significant impact of the class certification at this point is that Cendant now cannot propose any type of release to franchisees — or even talk with them about the lawsuit — without permission of the plaintiffs. "This is stopping the signing of more releases," he said.

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COURT WATCH

By Darryl A. Hart
and Charles G. Miller

Cooperation with Government Might Not Avoid Equitable Relief Payment — and Attorneys Beware!

Reported cases brought by the Federal Trade Commission under the FTC Franchise Rule are rare, largely because most targets do not have the resources to go to battle with the federal government. In *Federal Trade Commission v. Network Services Depot, Inc.* 2010 WL 3211724 (9th Cir. Aug. 16, 2010), the FTC filed suit in Nevada against the promoters of an Internet kiosk business opportunity. The case is worthy of attention because of its interesting facts that deal with the quantum of proof necessary to hold individual owners and executives liable for equitable monetary relief. Further, the case is important for the franchise bar because it imposed a constructive trust on legal fees paid to the attorneys representing the defendants.

The business opportunity — the sale of Internet kiosks to be located in airports, hotels, etc., with minimum guaranteed returns to the purchasers — proved to be a Ponzi scheme, with a small fraction of kiosks ever installed and the "guarantees" being paid by new investors. The original promoter, Network Services Depot, Inc. ("NSD"), contracted with a vending company, Bikini Vending Corp., and its related entities ("BVC"), to install the kiosks. BVC managed the enterprise and guaranteed NSD's customers would receive a minimum return each month. BVC falsely reported robust sales, but the scheme unraveled as a result of a TV exposé and employees jumping ship. NSD also claimed to be a victim, paying BVC millions for installation of kiosks that never were installed. When BVC's activities became public, NSD's owner went to the FBI and cooperated in recording incriminating conversations with BVC.

While it may seem that the owner of NSD should not have been targeted by the FTC after having cooperated with another arm of the government, the evidence showed that some time before his cooperation with the FBI, he had received customer complaints about kiosks not being installed, but he did not investigate, and he accepted BVC's explanations at face value. In fact, despite numerous customer complaints, NSD chose not to delve too deeply into BVC's activities, presumably in order to claim a lack of knowledge of BVC's fraudulent claims.

All of this worked to NSD's disadvantage, resulting in affirmation of summary judgment in the FTC's favor on the question of whether NSD's owner and another of its executives had knowledge that NSD or BVC engaged in dishonest or fraudulent conduct. Both defendants also admitted that they were aware that some of the representations were not true, thus weakening the impact of their cooperation with the FBI. The undisputed facts supported a reasonable inference that the owner and one of its executives satisfied the "knowledge" requirement by acting with either: 1) actual knowledge, 2) reckless indifference to truth or falsity, or 3) an awareness of a high probability of fraud and an intentional avoidance of the truth with respect to any of the admitted misrepresentations.

The owner and its executive were not the only losers. The court ruled that attorneys' fees that the owner paid to his lawyer could not be retained by the attorney. In this case, like in the defense of most government actions, the attorney requested a sizeable retainer of $375,000, and his co-counsel (who settled) received a $500,000 retainer. It turns out that this money came from some "custodial" accounts that the owner had told the FTC had been set up years ago for his children. However, the evidence showed that the true source of the funds was the kiosk scheme.

The owner's attorney argued that he should be allowed keep the retainer because he was a "*bona fide* purchaser" and was entitled to rely on statements from his client that the money came from a legitimate source. The problem was that the attorney was aware of a draft FTC complaint at the time he negotiated his fee. The complaint named all of his client's businesses as participants in the kiosk scheme. A review of the client's financial records would have shown that those businesses were the source of the funds in the custodial accounts. Thus, the attorney could not simply rely on his client's statements, and the court ruled that his failure to investigate defeated his *bona fide* purchaser claim.

This case should serve as a good lesson to the franchise bar that it is extremely important when undertaking representation in a governmental action to conduct an independent investigation of the source of the payment of legal fees so that they might not later be subjected to a constructive trust and lost.

Wisconsin Cases Tackle 'Community of Interest' Definition

The Wisconsin Fair Dealership Law ("WFDL"), Wisconsin Statutes, Ch. 135, Secs. 135.01 through 135.07 defines a "Dealership" as an arrangement where one party — the "grantor" — gives the other party — the "grantee" — the right to sell or distribute goods or services, or use a mark or symbol, in which there is a "community of interest" in the sale, lease, etc., of the goods or services. The Wisconsin Franchise Investment Law, Wisconsin Statutes, Ch. 553, Secs. 553.01 through 553.78, uses the "marketing plan or system" element in determining whether a business arrangement is a franchise. However, since a franchise contains both the community of interest and the marketing plan or system elements, it is also a "dealership" under the WFDL.

The question of whether an arrangement contains a marketing plan

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Movers & Shakers

Joycia Young is departing from **DLA Piper**'s Dubai, UAE, office, and joining the firm **Clyde & Co LLP**, also in Dubai. Young was the head of DLA Piper's intellectual property practice in the Middle East, South Asia, and Africa. She was named to the International Who's Who of Franchise Lawyers in 2009 and 2010. "She will now be working in conjunction with Clyde & Co.'s Head of IP, Rob Deans, in leading Clyde & Co.'s IP group, as well as taking a lead role in further developing the firm's regional franchising offering," according to a statement issued by Clyde & Co.

Lonnie Helgerson has launched **Veteran Franchise Centers**, which he describes as providing "free guidance to veterans and military families entering into franchise opportunities through the International Franchise Association VetFran program."

Court Watch

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or system or the parties have a community of interest has led to countless disputes as franchisees and dealers seek to avoid the termination, non-renewal, or other actions prevented by franchise relationship laws such as the WFDL. Two Wisconsin federal cases and one state court case revisited the definition of "community of interest" question in recent months, with slightly different results.

The cases turned to some degree on the list of criteria to be considered when pondering the community of interest question detailed in *Ziegler Co., Inc. v. Rexnord, Inc.* 433 N.W.2d 8 (Supreme Court of Wisconsin, 1987) and a Seventh Circuit case interpreting the WFDL, *Home Protective Services, Inc., v. ADT Securities Services, Inc.*, 438 F.3d 716 (7th Cir. 2006). *Home Protective Services*, while acknowledging the *Ziegler* list, boiled down the community of interest definition to the percentage of revenues and profits the alleged dealer derived from the grantor and the amount of time and money a purported dealer had sunk into the relationship. The bottom line, according to *Home Protective Services*, is whether the grantor had the alleged dealer "over a barrel." In that case, even though Home Protective Services derived 95% of its revenue from the sale of ADT products and services, the court held that since it could, and did, find another source, it was not over a barrel and, as such, was not protected by the WFDL — even though the new business was not as advantageous as the old.

In *Stucchi USA, Inc. v. Hyquip, Inc.,* Bus. Franchise Guide (CCH) ¶14,437 (USDC E.D. Wisconsin, July 28, 2010), a U.S. District Court struggled with whether a relationship between the U.S. subsidiary of an Italian corporation and a Wisconsin distributor of its hydraulic equipment constituted a "dealership" under the WFDL. The court relied on the two-pronged test of *Home Protective Services* in finding that the purported dealer's sales of the grantor's products were only a small percentage of the "dealer's" sales and, since the alleged dealer sold similar products for a competing manufacturer, it was not over a barrel. Hence, the dealer did not have WFDL protection against termination.

Another federal district court case, *The Dry Dock, LLC, v. The Godfrey Conveyor Company, Inc.,* Bus. Franchise Guide (CCH) ¶14,403 (USDC W.D. Wisconsin, June 7, 2010), considered whether the termination of a boat dealer's distribution agreement violated the WFDL. The court found that since the plaintiff sold many other brands of boats and a small percentage of the plaintiff's sales came from the sale of the defendant's products, the manufacturer did not have the plaintiff "over a barrel." In addition, the court reviewed the parties' relationship against the extensive list of factors detailed in *Ziegler*, the results of which dictated against finding the existence of a dealership.

What makes the foregoing cases of interest is the rejection of the percentage-of-sales test of the federal cases by a Wisconsin state court within weeks of the two federal cases. In *The Water Quality Store, LLC v. Dynasty Spas, Inc.,* Bus. Franchise Guide (CCH) ¶14,426 (Court of Appeals of Wisconsin, Dist. IV, July 15, 2010), the court found that *Home Protective Services* does not provide the proper standard for determining "community of interest," since it is a variance with the guidance provided by *Ziegler*. Since *Ziegler* is a Wisconsin Supreme Court case interpreting Wisconsin law, the court stated that it took precedence over federal cases interpreting that state's law. The court also cited a not-for-publication Wisconsin Supreme Court case, *Central Corporation v. Research Products Corporation,* 681 N.W.2d 178 (2004), which reversed a summary judgment for the manufacturer against the purported dealer, even though the manufacturer's products comprised only 8%-9% of the dealer's sales.

While it is usually clear whether a franchise fee and a trademark license is present in a business arrangement, the imprecise nature of "marketing plan or system" and "community of interest" will lead to continued confusion and disputes. Since it is unlikely that more exact definitions can be crafted, the continuing ambiguity should keep franchise litigators in business for the foreseeable future.

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