

RESOLVING THE CATCH 22: FRANCHISOR VICARIOUS LIABILITY FOR EMPLOYEE SEXUAL HARASSMENT CLAIMS AGAINST FRANCHISEES

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INTRODUCTION

During the last fifty years, modern business format franchising has emerged as one of the most popular and lucrative forms of doing business. Throughout the country, franchised businesses now employ significant numbers of workers and bring in billions of dollars in income annually.¹ The success of the franchising model is attributable to several factors, most notably its focus on creating a uniform public image and requiring consistency of operations at each location.²

What makes franchising unique is that it has successfully blended two opposing concepts of control. On one hand, a franchisor creates a comprehensive operating system and must exercise control over its franchisees to enforce that system.³ A central premise of franchising is that each location is uniform in appearance, practices, and services provided.⁴ Franchisors routinely perform inspections at each location to ensure compliance.⁵ Additionally, franchisors frequently promulgate training regimes and marketing plans that are used system-wide to enhance uniformity of results.⁶ Without such control, a franchisor arguably could not maintain its uniform brand image or the consistency of operations across its locations.

On the other hand, a franchisor heavily relies on the monetary investments as well as the motivation, skill, and local knowledge of its franchisees to implement the comprehensive operating system on a daily basis.⁷ In other words, franchisees function simultaneously as quasi-independent owners and as quasi-dependent managers.⁸ This duality has allowed franchisors to cash in on the

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1. NATIONAL ECONOMIC CONSULTING PRACTICE OF PRICEWATERHOUSE COOPERS, ECONOMIC IMPACT OF FRANCHISED BUSINESSES 10 (2004), available at http://www.franchise.org/files/EIS6_2.pdf [hereinafter ECONOMIC IMPACT].

2. THOMAS S. DICKE, FRANCHISING IN AMERICA 155 (1992).

3. See ROGER G. BLAIR & FRANCIS LAFONTAINE, THE ECONOMICS OF FRANCHISING 118-121 (2005).

4. See DICKE, *supra* note 2, at 155.

5. See, e.g., *Miller v. D.F. Zee's, Inc.*, 31 F. Supp. 2d 792, 807 (D. Or. 1998); *Miller v. McDonald's Corp.*, 945 P.2d 1107, 1110 (Or. Ct. App. 1997).

6. BLAIR & LAFONTAINE, *supra* note 3, at 119-120.

7. DONALD D. BOROIAN & PATRICK J. BOROIAN, THE FRANCHISE ADVANTAGE 50-52 (1987).

8. See generally John Stanworth, *The Franchise Relationship: Entrepreneurship or Dependence?*, in FRANCHISING: CONTEMPORARY ISSUES AND RESEARCH 161 (Patrick J. Kaufmann & Rajiv P. Dant eds., 1995).

benefits of operating large national chains without having the burden of overseeing every detail of daily operations. It has also allowed thousands of individual franchisees to become small business owners without taking on the full risks of starting a business.

Although this novel form of control is at the heart of the franchising model's success, it also has given rise to an important and controversial question, namely, to what extent should a franchisor be held vicariously liable for the wrongful acts of its franchisees? Traditionally, courts have turned to the Restatement (Second) of Agency to answer this question.⁹ In making determinations of vicarious liability, the Restatement analysis, as it has been formulated by the courts, focuses on the degree of control a franchisor exercises over the daily operations of a franchisee.¹⁰ The more control the franchisor exercises, the more likely a franchisor is to be found vicariously liable.

At first glance, the test appears straightforward. However, in application, different jurisdictions have reached widely divergent results on very similar fact patterns.¹¹ This judicial split is particularly concerning since most franchises are national or at least regional operations and, therefore, frequently have locations in a number of different jurisdictions. As a result, a particular franchisor's exercise of control over its franchisees might be held insufficient in one jurisdiction to give rise to vicarious liability, while another jurisdiction might reach the opposite conclusion when reviewing the same exercise of control.¹²

Although the broader question of franchisor vicarious liability is beyond the scope of this Note, the ultimate goal here will be more narrow and will focus on the formulation of a more consistent approach towards resolving questions of franchisor vicarious liability for sexual harassment and discrimination claims which are made against franchisees.

Title VII of the Civil Rights Act of 1964 ("Title VII") prohibits, inter alia, employers from discriminating against employees on the basis of sex.¹³ Following the lead of the Equal Employment Opportunity Commission, the Supreme Court held, in the landmark case of *Meritor Savings Bank v. Vinson*,¹⁴ that discrimination on the basis of sex includes sexual harassment.¹⁵ This Note posits that a franchisor should be held vicariously liable as an employer under Title VII for sexual harassment and discrimination claims against its franchisees.

The central premise of this Note is that public policy, as evidenced by Title

9. These cases are discussed *infra* Part II.B.

10. *Miller*, 945 P.2d at 1110.

11. These cases are discussed *infra* Part II.B.

12. Quite a few commentators have questioned the fairness of this result. See, e.g., William L. Killion, *Franchisor Vicarious Liability—The Proverbial Assault on the Citadel*, 24 FRANCHISE L.J. 162 (2005); Kevin M. Shelley & Susan H. Morton, "Control" in *Franchising and the Common Law*, 19 FRANCHISE L.J. 119 (2000). Both articles are discussed *infra* Part III.

13. 42 U.S.C. §§ 2000e to -17 (2000).

14. 477 U.S. 57 (1986).

15. *Id.* at 66-67.

VII, favors equal opportunity in employment practices¹⁶ and that franchisors are in a unique position to implement and enforce the mandates of Title VII. Imposing franchisor vicarious liability would serve as a strong incentive for franchisors to stop relying on the divergent practices of their franchisees and, instead, to implement uniform, system-wide practices and procedures, which would lead to more effective efforts to prevent and investigate incidents of sexual harassment.

At the same time, this Note also argues for the creation of a franchisor affirmative defense, which would shield franchisors from vicarious liability in sexual harassment and discrimination cases if the franchisor meets a series of requirements.¹⁷ This defense would vitiate the effect of the current Restatement test, which provides a strong disincentive for franchisors to get too involved in daily operations of franchisees. More specifically, this proposal retains remnants of agency theory by holding the franchisor vicariously liable. However, it provides an incentive (i.e., the avoidance of vicarious liability) to franchisors that take an active part in solving the problem.

Part I of this Note briefly explores the history of modern franchising, from its rise in the first half of the twentieth century to the present. This section also provides statistical data on the impact franchised businesses have on the economy and the workforce. Part II discusses the development of theories of franchisor vicarious liability. It focuses primarily on agency theory, but also briefly discusses the employer-independent contractor and single employer models as well. Part III critiques the prevailing view amongst commentators who have strongly advocated against imposing any form of franchisor vicarious liability. Finally, in Part IV, this Note offers a plan for retaining franchisor vicarious liability for sexual harassment and discrimination claims and the creation of an affirmative defense.

I. A BRIEF INTRODUCTION TO FRANCHISING

A. *Economic Significance*

Franchising has a strong impact on our national economy. In fact, franchised businesses today provide almost ten million jobs in the United States with a combined payroll of more than \$229 billion dollars.¹⁸ In addition, franchises account for 3.2% of all business establishments and 7.4% of all private-sector

16. See, e.g., H.R. REP. NO. 92-238 (1971), as reprinted in 1972 U.S.C.C.A.N. 2137.

17. This affirmative defense is somewhat similar to the Ellerth/Faragher defense (discussed in more detail *infra* Part IV), which was created by the Supreme Court in the companion cases of *Burlington Industries, Inc. v. Ellerth*, 524 U.S. 742 (1998), and *Faragher v. City of Boca Raton*, 524 U.S. 775 (1998).

18. ECONOMIC IMPACT, *supra* note 1, at 10. In fact, “[p]ayrolls distributed because of franchised businesses were at least 10 percent of the private-sector payroll in all but 10 states and the District of Columbia.” *Id.* at 14.

jobs in the United States.¹⁹ Moreover, “franchised business provided more jobs in 2001 than the financial activities industry (including banks, insurance carriers, and real estate), construction industry, or information industry (including software and print publishing, motion pictures and videos, radio and television broadcasting, and telecommunications carriers and resellers).”²⁰ In examining the indirect or “ripple effect” of franchising activities, one study found that franchising actually creates over eighteen million jobs and more than \$1.5 trillion in economic output.²¹

B. Historical Background

1. *Product Distribution Franchising.*—Beginning in the mid-nineteenth century, an early form of franchising emerged when the Singer Sewing Machine Company sold individual salesmen the right to distribute its sewing machines in particular geographic regions.²² Another early product distribution franchisor was the McCormick Harvesting Machine Company, which manufactured its much famed reaper beginning in the 1840s.²³ Other industries soon embraced the product distribution model as car dealerships, gas stations, and soft drink bottling companies followed the trend in the late 1800s and early 1900s.²⁴

Under this form of franchising, the product manufacturer was primarily focused on developing a large distribution network for its products without having to invest large sums of economic and human capital in the process.²⁵ That is, the manufacturer hoped to gain a large retail market for its products without having to incur the costs and management responsibilities of establishing and maintaining local retail distribution chains.

A major impetus for the franchising model was the ever-expanding nineteenth century national economy, driven by the needs of a growing and evermore urbanized population.²⁶ Vast improvements in transportation, communications, and manufacturing characterized the new economy.²⁷ These factors combined to provide manufacturers with “dense and easily accessible

19. *Id.* at 10.

20. *Id.*

21. *Id.* at 11. The term “ripple effect” takes into account the indirect economic impact franchised businesses have on other industries by stimulating those outside industries to produce more products and, consequently, hire more employees.

22. BOROIAN & BOROIAN, *supra* note 7, at 28. During this time period, the relationship between many product manufacturers and the retailers of their products was gradually shifting from that of a principal and an independent agent to more “symbiotic relationships of franchisor and franchisee.” DICKE, *supra* note 2, at 152.

23. For a more detailed account of the development of these two companies, see DICKE, *supra* note 2, at 12-47.

24. BOROIAN & BOROIAN, *supra* note 7, at 28.

25. *Id.*

26. DICKE, *supra* note 2, at 13-14.

27. *Id.*

markets for their wares.”²⁸

Many companies, such as Singer and McCormick, which were newer and had fewer economic resources, quickly learned that it was not possible to function effectively both as a manufacturer and a national marketer of their products.²⁹ The financial and administrative expense of setting up company shops was simply cost-prohibitive.³⁰ Instead, these companies developed networks of authorized agents, on whom the companies relied to bring their products to the nation’s consumers.³¹ Initially, such companies exercised minimal control over their agents, but, as companies became more experienced with this new business model, they found this was not the best approach.³²

Companies soon realized that their brand image was closely tied to the business activities of their agents.³³ A manufacturer’s agent represented the face of the company to consumers, which was particularly true when the agent owned the exclusive right to market the company’s products in a certain geographic region.³⁴ As a result, a single wayward agent’s poor business practices might tarnish the company’s reputation for a whole geographic segment of the population. In response, franchisors gradually increased the amount of control they held over their agents by imposing more restrictions, being more selective in choosing agents, and establishing regional offices to oversee the activities of agents.³⁵

2. *Business Format Franchising.*—Following World War II, franchising underwent a gradual transition from product distribution franchising to a more complex and comprehensive mode of doing business, often described as business format franchising.³⁶ The advent of quick-service restaurants such as A & W, McDonald’s, Burger King, and Dunkin’ Donuts is the most visible marker of this transition.³⁷ Business format franchises now employ four times as many workers, generate 2.5 times the payroll, and produce three times the output of product distribution franchises.³⁸

Under the business format model, a franchisor allows another party (i.e., the franchisee) to market its products and/or services under the franchisor’s name

28. *Id.* at 15.

29. *Id.* at 16.

30. *Id.*

31. Initially, many selling agents had agreements with more than one manufacturer and sold multiple products. *Id.* The result of this arrangement was that a particular agent, more often than not, had no incentive to sell one product over another. *Id.*

32. BLAIR & LAFONTAINE, *supra* note 3, at 5.

33. *Id.*

34. *Id.*

35. *Id.*

36. BOROIAN & BOROIAN, *supra* note 7, at 29. Use of the term “franchising” in this Note refers to business format franchising, as it has become the dominant form of franchising in the modern era.

37. *Id.* Business format franchising is described in more detail in *infra* Part I.C.

38. ECONOMIC IMPACT, *supra* note 1, at 11.

and trademark using a pre-developed “system” or method of doing business, which the franchisor has created.³⁹ It is the marketing of the franchisor’s system which separates business format franchising from its product distribution predecessor. The franchisor sells not only the right to market its products and use its trademark in a particular geographic region, but also the right to use its “proven business system.”⁴⁰ In addition to comprehensive operational manuals, a franchisor’s system also includes the use of “an established name, training, and a host of professional services such as site selection, managerial assistance, and national advertising, all of which lay beyond the reach of the typical small business person.”⁴¹

Strict adherence by the franchisee to the franchisor’s system is a hallmark of the business format model.⁴² The rapid growth of franchising has been due in large part to the public’s increasing preference for proven quality and uniformity in goods and services.⁴³ By creating, marketing, and ultimately enforcing its system, a franchisor ensures that its core product or service is presented to the consuming public in a consistent and uniform manner. “[I]t is the consistency of [a] system’s operations, service, and product quality that attracts customers and induces loyalty; customers become loyal if the experiences they enjoy at diverse units of these chains routinely meet their expectations.”⁴⁴

C. *The (In)dependent Franchisee*

Like its product distribution predecessor, business format franchising allows the franchisor to rapidly expand into regional, national, and even international markets by tapping into the capital, time, and energy of highly motivated local agents known as franchisees.⁴⁵ The franchisee’s role is best described by

39. BOROIAN & BOROIAN, *supra* note 7, at 16; RIEVA LESONSKY & MARIA ANTON-CONLEY, ENTREPRENEUR MAGAZINE’S ULTIMATE BOOK OF FRANCHISES 11 (2005) [hereinafter *ULTIMATE BOOK*].

40. BOROIAN & BOROIAN, *supra* note 7, at 29. Ray Kroc, who developed the highly successful McDonald’s franchising system beginning in the 1950s, is often described as a revolutionary in the field of franchising. *Id.* at 28. Kroc realized early on that the “hands-off” approach used by the McDonald’s brothers would prove fatal with time. *Id.* at 31. Instead, he believed that the franchisor should play an active role in the training and ongoing support to its franchisees. *Id.* at 32. Today, McDonald’s has more than 30,000 locations worldwide, of which almost 22,000 are owned by franchisees. *ULTIMATE BOOK*, *supra* note 39, at 274.

41. DICKE, *supra* note 2, at 154.

42. BOROIAN & BOROIAN, *supra* note 7, at 16.

43. DICKE, *supra* note 2, at 155.

44. BLAIR & LAFONTAINE, *supra* note 3, at 117.

45. BOROIAN & BOROIAN, *supra* note 7, at 51. Describing franchisees as highly motivated “managers” rings especially true for franchisors such as Domino’s, who specifically target successful store managers at company owned locations to purchase whole or partial ownership shares of its locations, even assisting the managers to obtain financing. *Id.* at 52. *See also* BLAIR & LAFONTAINE, *supra* note 3, at 217 (noting that a franchisee will typically be much more

examining two dichotomies. First, franchisees are simultaneously quasi-independent managers⁴⁶ and also quasi-dependent small business owners.⁴⁷ Second, franchisees are both entrepreneurial⁴⁸ and risk adverse.⁴⁹

On the one hand, franchisees often invest significant amounts of their own financial capital to purchase a franchise.⁵⁰ For this reason, franchisees, much like any other small business owner, have a direct and motivating financial incentive to make their location successful: they want to earn a return on their investment. In addition to the financial investment, franchisees typically make an investment of their time, insofar as most franchise agreements require franchisees to personally manage the daily operations of their location, which is usually done with very little direct supervision by the franchisor on a day-to-day basis.⁵¹ In these ways, franchisees are both entrepreneurial and independent.

On the other hand, franchisees are also risk adverse and dependent. First, a franchisee must operate its location pursuant to the terms of the franchise agreement and strictly adhere to the franchisor's operating system.⁵² More often than not, this includes being subject to periodic site inspections by the franchisor.⁵³ Such agreements might also involve obtaining the franchisor's approval before selecting a site for a new location and also adhering to franchisor-specified building and design specifications.⁵⁴ Franchisees often rely on advertising and marketing schemes promulgated by the franchisor.⁵⁵ Finally, franchisees have the added benefit of being able to seek guidance from the franchisor whenever problems arise.⁵⁶ In these ways, the franchisee's role involves a good deal of dependence on the franchisor.

Second, franchisees typically assume significantly less risk in starting their business than other small business owners.⁵⁷ In fact, the failure rate for franchised businesses is five percent compared to a failure rate of sixty-five to ninety percent for the average start-up business.⁵⁸ The primary reason for this is

motivated than a typical company store manager since the franchisee "has his own money on the line").

46. See ULTIMATE BOOK, *supra* note 39, at 12-13.

47. See Stanworth, *supra* note 8, at 162.

48. *Id.*

49. See BOROIAN & BOROIAN, *supra* note 7, at 66-67; John L. Hanks, *Franchisor Liability for the Torts of Its Franchisees: The Case for Substituting Liability as a Guarantor for the Current Vicarious Liability*, 24 OKLA. CITY U. L. REV. 1, 27 (1999).

50. ULTIMATE BOOK, *supra* note 39, at 13.

51. *Id.* at 2.

52. BLAIR & LAFONTAINE, *supra* note 3, at 54.

53. Stanworth, *supra* note 8, at 168. The frequency of inspections, however, can vary widely amongst franchisors. *Id.*

54. BLAIR & LAFONTAINE, *supra* note 3, at 79, 130-31.

55. *Id.* at 246.

56. BOROIAN & BOROIAN, *supra* note 7, at 17.

57. *Id.* at 66.

58. *Id.*; but see BLAIR & LAFONTAINE, *supra* note 3, at 42-46. Blair notes that some

that, to some extent, all business format franchising systems provide franchisees with operating manuals, training, periodic inspections, and, perhaps most importantly, advice.⁵⁹ Succinctly stated:

For the franchisee it is a shot at attaining the American dream of owning a business—but with much of the risk removed. In effect, the franchisee is able to launch a new business without any of the attendant growing pains. Someone else has already made—and corrected—the most important mistakes, ironed out most of the wrinkles, and invented a system that works.⁶⁰

In sum, one cannot accurately describe franchisees as wholly independent entities vis-à-vis franchisors, nor as glorified local managers.⁶¹ The first assertion ignores the fact that the very existence and success of franchised locations is heavily dependent on an ongoing relationship with the franchisor and the use of the franchisor's business system.⁶² The second assumption ignores the fact that franchisees take real financial risks in starting and managing the operations of their locations.⁶³

D. The Benefits and Burdens of Being a Franchisor

The franchising relationship benefits franchisors in several ways. Most importantly, the franchisor does not have to expend the economic capital necessary to develop a national chain of outlets.⁶⁴ This allows the franchisor to get its product or service out to a large market quickly. In addition, franchisors benefit from the fact that franchisees typically have a better understanding of the local markets in which they operate.⁶⁵ Moreover, as compared to the typical company-employed manager, franchisees have a very strong built-in incentive to be profitable and efficient managers (i.e., franchisees want to make a return on

commentators have challenged such statistics and report that the failure rate of franchised locations might, in fact, be the same or even higher than the rate for independent start-ups. *Id.* Nevertheless, the authors point out that, failure rates notwithstanding, well-established franchisors offer potential franchisees the opportunity to “start” a business that will have an immediately recognizable brand image, access to products and suppliers, managerial support, and access to the franchisor's operating system. *Id.* at 46. Thus, “while franchising is not risk free, it does make it possible for people who might otherwise not have this opportunity to develop a business locally and, with some luck, thrive as part of a larger business entity.” *Id.*

59. BOROIAN & BOROIAN, *supra* note 7, at 17.

60. *Id.*

61. See BLAIR & LAFONTAINE, *supra* note 3, at 291-93.

62. *Id.*

63. *Id.*

64. BOROIAN & BOROIAN, *supra* note 7, at 28; see generally BLAIR & LAFONTAINE, *supra* note 3, at 56-78.

65. BOROIAN & BOROIAN, *supra* note 7, at 52.

their monetary investments).⁶⁶

Second, the franchise relationship allows franchisors to enjoy a steady and continuous stream of income from each franchised location.⁶⁷ Franchisors extract both an upfront franchising fee as well as ongoing royalties, which can range from more than 12.5% of sales at McDonald's to as low as four percent at Arby's.⁶⁸ Additionally, some franchisors enjoy additional streams of income by retaining ownership of the land and buildings used by franchisees and charging them rent.⁶⁹

The franchising model also brings some trade-offs for the franchisor. The primary trade-off comes in the form of a loss of rigorous control over daily operations.⁷⁰ Boroian has described the situation as follows: "[The franchisor's] role in the day-to-day operation of the franchisee's business is more that of a grandparent than a parent. [The franchisor is] there when needed for advice and counsel, but [the franchisor does not] have the day-to-day responsibility for direct management."⁷¹

Since consistency and uniformity of operations play such a central role in modern business format franchising, franchisors have a legitimate concern that a wayward franchisee might do considerable harm to the franchisor's brand image and, consequently, to its ultimate profitability.⁷² While the franchisor's overall success depends largely on the uniform quality of products and services offered at each location, individual franchisees might be pulled by an opposite incentive.⁷³ For instance, a franchisee whose customer base is largely transient (e.g., a fast food restaurant located near a major interstate) might be motivated to increase profits by utilizing lower quality products and service, thereby capitalizing on the brand to attract customers while not suffering the

66. *Id.*

67. BLAIR & LAFONTAINE, *supra* note 3, at 56.

68. ULTIMATE BOOK, *supra* note 39, at 274, 320. The average royalty rate in 2001 was 5.2%. BLAIR & LAFONTAINE, *supra* note 3, at 66. Nevertheless, royalties can range from flat yearly fees in some franchise relationships to royalties of more than twenty percent in some low-overhead industries. *Id.* at 65-66.

69. This is especially true for McDonald's, the largest retail property owner in the world. ERIC SCHLOSSER, FAST FOOD NATION 4 (2001). In fact, McDonald's earns more collecting rent on its properties than it does selling burgers. *Id.*

70. BOROIAN & BOROIAN, *supra* note 7, at 61-62.

71. *Id.* at 52; *see also* Stanworth, *supra* note 8, at 169. In reviewing both the language of franchise agreements as well as conducting interviews with franchisors and franchisees, this study concluded that, although provisions of the agreement were often very restrictive of franchisees, in practice franchisees more often described the relationship with their franchisors as one of give and take and semi-autonomy rather than close supervision. *Id.* 163-66. This is not to say, however, that franchisors do not occasionally exercise very tight control over a particular franchised location when problems arise. *Id.* at 169.

72. *See generally* BLAIR & LAFONTAINE, *supra* note 3, at 118-21.

73. *Id.*

consequences of dissatisfied customers.⁷⁴ Such behavior would ultimately be detrimental to other franchisees and, consequently, to the franchisor.

Perhaps it is just for this reason that many franchisees report that franchise agreements have become more strict and more strictly enforced with time.⁷⁵ Most franchisors retain the right to periodically inspect franchised locations to ensure compliance with the franchise agreement and business system.⁷⁶ Additionally, many franchisors require that franchisees attend franchisor-sponsored training prior to operating their own location.⁷⁷ In the end, however, the franchisor's ability to control the franchisee's operations is most striking in the franchisor's retained right to terminate the relationship if the franchisee's performance is inadequate.⁷⁸ Thus, although the franchisor does not directly manage daily operations, the franchisor holds an impressive club with which to control and punish wayward franchisees that deviate significantly from the franchisor's wishes.⁷⁹

II. THEORIES OF FRANCHISOR VICARIOUS LIABILITY IN THE CASE LAW

A. Introduction

Title VII of the Civil Rights Act of 1964 (the "Act") prohibits employers from discriminating against employees and applicants for employment on the basis of sex.⁸⁰ Thus, the Act specifically requires that discrimination against an

74. *Id.*

75. Stanworth, *supra* note 8, at 174.

76. *Id.* at 168.

77. The amount of training required varies by franchisor. For example, McDonald's requires one week of training at the company's headquarters followed by one to two years of training at a local store. ULTIMATE BOOK, *supra* note 39, at 274. Jackson Hewitt Tax Service requires five days of training at company headquarters followed by two days of regional training. *Id.* at 211.

78. BLAIR & LAFONTAINE, *supra* note 3, at 269.

79. *Id.*

80. 42 U.S.C. §2000e-2(a) (2000). The provision states:

It shall be an unlawful employment practice for an employer—

(1) to fail or refuse to hire or to discharge an individual, or otherwise to discriminate against any individual with respect to his compensation, terms, conditions, or privileges of employment because of such individuals race, color, religion, sex, or national origin; or

(2) to limit, segregate, or classify his employees or applicants for employment in any way which would deprive or tend to deprive any individual of employment opportunities or otherwise adversely affect his status as an employee, because of such individual's race, color, religion, sex, or national origin.

Id. As noted previously, the Supreme Court held in the case of *Meritor Savings Bank, FSB v.*

employee be attributable to his or her employer before a cognizable claim comes into existence. Generally, Title VII defines an employer as one who employs at least fifteen people.⁸¹

The question then becomes can the franchisor be considered, for the purpose of bringing a Title VII claim, the employer of its franchisee's employees? Courts in different jurisdictions have split when deciding this issue. The biggest challenge, of course, is finding a legal tie between the franchisor and the franchisee that would allow liability for discrimination claims to pass from the franchisee, as the employee's direct employer, to the franchisor through its close relationship with the franchisee.

Courts have struggled with various theories of vicarious liability when plaintiffs attempt to establish such a connection. The concept of vicarious liability allows legal fault to be attributed to a party who neither directly acted to cause the victim's damages nor failed to act when he or she had a duty to do so.⁸² At first glance, this principle seems a bit unfair, for it goes against many basic notions about tort liability (i.e., that a person should only be held liable when he or she is directly at fault).⁸³

Nevertheless, various justifications have been offered in support of vicarious liability. For instance, it can be argued that when one party chooses another as his or her representative, that party should be held accountable if he or she chooses a poor representative.⁸⁴ Alternatively, one might argue that a person and his or her representative can best be described as a single or unitary enterprise and that the person who stands to benefit from his or her representative's actions should also bear the loss of the representative's actions which result in harm to others.⁸⁵ On broader public policy grounds, vicarious liability has another important justification, the principle of loss distribution.⁸⁶ When principal actors are held liable for the actions of their servants, agents, or employees, and particularly when those actors are businesses, the costs of tort judgments are effectively stretched thinly across a large portion of the public rather than forcing any one individual to bear the often debilitating costs of a single tort claim.⁸⁷

This Note addresses three of the most common theories of vicarious liability used in the franchising cases. Most often, a court examines the issue through the lens of agency theory.⁸⁸ Briefly, agency is a legal relationship between two

Vinson, 477 U.S. 57, 66-67 (1986), that the term discrimination under Title VII includes sexual harassment.

81. 42 U.S.C. § 2000e(b) (2000).

82. P. S. ATIYAH, VICARIOUS LIABILITY IN THE LAW OF TORTS 3, 12 (1967).

83. *Id.* at 12.

84. *Id.* at 19.

85. *Id.* at 19-20.

86. *Id.* at 23.

87. *Id.* This cost spreading usually takes the form of higher insurance premiums for businesses as well as slightly increased costs to the individual consumer for the goods and services produced by those businesses. *Id.*

88. The statutory language of Title VII seems to support this approach in particular. Under

parties, most often formed by an agreement, which allows one party (i.e., the agent) to act on behalf of and, consequently, affect the legal position of the other party (i.e., the principle) with respect to third parties.⁸⁹ Under this approach, the court must determine whether the franchisee is the agent of the franchisor before the franchisor may be held liable.

More recently, two additional approaches have been used by some courts to address franchisor vicarious liability. One of these approaches is the employer-independent contractor model found in the Restatement (Second) of Torts.⁹⁰ The other approach is the single employer test, which was first developed by the National Labor Relations Board for use in resolving labor disputes.⁹¹ Under these models, the court must determine, respectively, whether the franchisor employs the franchisee as an independent contractor or whether the franchisor and franchisee qualify as a “single employer.”

B. Agency Theory

Although a franchisor and franchisee function in most respects as separate legal entities, a franchisor might be held liable for the acts of its franchisee, particularly if a court finds that the franchisee was acting as the franchisor’s agent. The franchisor’s right to control the franchisee is the key factor examined when making such a determination.⁹² In fact, “[u]nder the right to control test it does not matter whether the putative principal actually exercises control; what is important is that it has the right to do so.”⁹³

There are two primary forms of agency.⁹⁴ Typically an agency relationship arises after two parties have entered into some form of a consensual agreement.⁹⁵ The Restatement defines “agency” as:

the fiduciary relation which results from the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act. The one for whom action is to be taken is the principal. The one who is to act is the agent.⁹⁶

This form of agency is often referred to as actual agency, as opposed to the

42 U.S.C. §2000e(b) (2000), an employer’s *agents* are also considered its employees.

89. G.H.L. FRIDMAN, *THE LAW OF AGENCY* 8-9 (1966).

90. RESTATEMENT (SECOND) OF TORTS § 414 (1965).

91. *See, e.g.,* Lockard v. Pizza Hut, Inc., 162 F.3d 1062, 1069 (10th Cir. 1998); Alberter v. McDonald’s Corp., 70 F. Supp. 2d 1138, 1142 (D. Nev. 1999). Both cases are discussed in greater detail below.

92. Miller v. McDonald’s Corp., 945 P.2d 1107, 1110 (Or. Ct. App. 1997); *see also* Butler v. McDonald’s Corp., 110 F. Supp. 2d 62, 66 (D.R.I. 2000).

93. Miller, 945 P.2d at 1110 n.3; *see also* Billops v. Magness Const. Co., 391 A.2d 196, 197-98 (Del. 1978).

94. FRIDMAN, *supra* note 89, at 33.

95. *Id.*

96. RESTATEMENT (SECOND) OF AGENCY § 1 (1958).

related concept of apparent agency (or agency by estoppel).⁹⁷

Under the doctrine of apparent agency, no overt agreement is required.⁹⁸ Rather, such a relationship arises when the words or acts of one party (the putative principal) vis-à-vis another party (the putative agent) lead outsiders to believe that an agency relationship exists.⁹⁹ If an outsider to the relationship detrimentally relies on such a belief, the doctrine holds that the putative principal will be treated as if the agent had acted with the principal's consent.¹⁰⁰ Courts that utilize the agency approach often address both actual and apparent agency.

1. *Actual Agency Found.*—In *Miller v. D.F. Zee's, Inc.*,¹⁰¹ the court held that Denny's, in its capacity as franchisor, was responsible for acts of harassment perpetrated by the franchisee's managers and supervisors through a theory of agency.¹⁰² Although the franchise agreement contained an explicit provision stating that the franchisee was not the franchisor's agent, the court held that such a provision was not by itself dispositive.¹⁰³ The court noted several factors which led it to find that the franchisor had retained sufficient control over the franchisee to justify a finding of an actual agency relationship. First, "the franchise agreement require[d] adherence to comprehensive, detailed manuals for the operation of the restaurant."¹⁰⁴ Second, the agreement required strict compliance and allowed for termination of the agreement by the franchisor.¹⁰⁵ Third, the agreement allowed the franchisor to control training and discipline of

97. FRIDMAN, *supra* note 89, at 33.

98. *Id.* at 61.

99. *Id.*

100. *Id.*; see also *Miller v. McDonald's Corp.*, 945 P.2d 1107, 1112 (Or. Ct. App. 1997); RESTATEMENT (SECOND) OF AGENCY § 267 (1958). The Restatement defines apparent agency as follows:

One who represents that another is his servant or other agent and thereby causes a third person justifiably to rely upon the care or skill of such apparent agent is subject to liability to the third person for harm caused by the lack of care or skill of the one appearing to be a servant or other agent as if he were such.

Id.

101. 31 F. Supp. 2d 792 (D. Or. 1998). Several employees of a Denny's restaurant sued the local franchisee (D.F. Zee's) and the franchisor (Denny's, Inc.) alleging, inter alia, sex discrimination and harassment under Title VII. *Id.* at 797. The court noted thirty-two separate incidents of sex discrimination, sexual harassment, and retaliation perpetrated by supervisors, co-workers, and upper management at the local Denny's location. *Id.* at 800-01. The franchisor moved for summary judgment claiming it could not be liable under Title VII since it did not employ the plaintiffs. The court denied the motion. *Id.* at 797.

102. *Id.* at 806.

103. *Id.* at 807; see also *Miller*, 945 P.2d at 1109; but see *Alberter v. McDonald's Corp.*, 70 F. Supp. 2d 1138 (D. Nev. 1999); *Kennedy v. Western Sizzlin Corp.*, 857 So. 2d 71, 78 (Ala. 2003).

104. *D.F. Zee's*, 31 F. Supp. 2d at 806-07.

105. *Id.* at 807.

employees.¹⁰⁶ In fact, all franchisees and their managers were required to attend the franchisor's training, which included diversity and non-discrimination components.¹⁰⁷ Finally, the company's operations manual specifically allowed the franchisor to be involved directly with complaints, investigation, and discipline as a result of a franchisee employee's claims of discrimination.¹⁰⁸

Even in suits not related to employee sexual harassment or discrimination claims, courts have used similar rationales to justify findings of an agency relationship between a franchisor and franchisee. For instance, in *Miller v. McDonald's Corp.*,¹⁰⁹ the court held that a reasonable jury could find that McDonald's retained sufficient control over its franchisee's daily operations to indicate the existence of an actual agency relationship.¹¹⁰ The company's manuals and franchise agreement went beyond simply setting standards insofar as they laid out precise methods for food handling and preparation, and the franchisor sent inspectors to monitor the franchisee and to ensure compliance.¹¹¹ Moreover, the franchisor retained the right to terminate the relationship.¹¹² The court also noted several other factors justifying a finding of actual agency; the agreement included provisions governing the franchisee's hours of operation, restaurant appearance and cleanliness, employee uniforms, food containers and packaging, food and beverage ingredients, and training standards.¹¹³

In another case, *Butler v. McDonald's Corp.*,¹¹⁴ the court held that a "no agency" provision inserted into a franchise agreement is not controlling.¹¹⁵ Moreover, the court stated that the comprehensive McDonald's system, as evidenced in the agreement and operating manuals and enforced through frequent inspections and the franchisor's right to terminate the agreement, along with the

106. *Id.*

107. *Id.*

108. *Id.*

109. 945 P.2d 1107 (Or. Ct. App. 1997). A customer bit into a Big Mac containing a sapphire stone and sustained injuries. *Id.* at 1108. She sued the local franchisee (3-K Restaurants) as well as the franchisor (McDonald's Corp.). Although the trial court granted the franchisor's motion for summary judgment on the grounds that the franchisor neither owned nor operated the local restaurant, the Oregon Court of Appeals reversed. *Id.*

110. *Id.* at 1111.

111. *Id.*

112. *Id.*

113. *Id.* at 1109.

114. 110 F. Supp. 2d 62 (D.R.I. 2000). In this case, a fast food restaurant customer pushed against a glass door, which shattered, causing serious injury. *Id.* at 64. The customer sued both the franchisee (Cooper) and the franchisor (McDonald's Corp.) under a theory of negligence, alleging that a crack had existed for two weeks and that the restaurant knew or should have known about it and corrected the problem. *Id.* The franchisor moved for summary judgment claiming, inter alia, that it was not vicariously liable for the negligence of its franchisee. *Id.* However, the court denied the motion. *Id.* at 68.

115. *Id.* at 67. "However, a party cannot simply rely on statements in an agreement to establish or deny agency." *Id.*

franchisor's taking of profits from the franchisee's operations supported a finding that the franchisor retained sufficient control over its franchisee to justify a finding of an agency relationship.¹¹⁶

2. *No Actual Agency Found.*—Although the cases discussed above demonstrate an emerging trend towards finding franchisors liable for the acts of franchisees under agency theory, many courts remain reluctant to find that franchisors retain enough control over their franchisees to justify a finding of an agency relationship. For instance, in *Kennedy v. Western Sizzlin Corp.*,¹¹⁷ the Alabama Supreme Court held that the existence of “[a] franchise agreement, without more, does not make the franchisee an agent of the franchisor.”¹¹⁸ As in the previously discussed cases, this court focused on whether the franchisor retained a right of control over the franchisee as an alleged agent. However, here the court noted that a franchisor's retention of a right to supervise its franchisee merely to determine if the franchisee's performance is in conformance with the agreement is not enough to establish the necessary level of retained control.¹¹⁹

In this case, the franchise agreement required the franchisee to comply strictly with the franchisor's operations manual, and it gave the franchisor the right to inspect regularly the franchisee's restaurant without notice.¹²⁰ The agreement also required franchisees to attend training provided by the franchisor.¹²¹ Nevertheless, the court held that the operations manual, right of inspection, and training requirements did not rise to a level indicating that the franchisor actually controlled daily operations; the franchisor's “control was limited to ensuring that [the franchisee] complied with the franchise agreement and, in turn, the operations manual.”¹²² In essence, the court drew a distinction between ensuring compliance with a comprehensive set of guidelines and actually carrying out those guidelines on a daily basis.

116. *Id.* at 66-67. Although it is difficult to imagine a case in which a franchisor would not oppose a finding of an agency relationship between itself and its franchisee, see *Martin v. McDonald's Corp.*, 572 N.E.2d 1073 (Ill. App. Ct. 1991). In that case, the franchisor argued that the franchisee was in fact its agent and, thus, the franchisee's employees were also its employees for purposes of the state's Workers' Compensation Act. *Id.* at 1080.

117. 857 So. 2d 71 (Ala. 2003). The plaintiffs alleged that one of the franchisee-partners committed forcible rape, unwanted sexual touching, and inappropriate sexual remarks. *Id.* at 73 n.1. The franchisee-partner (Lambert) had previously been terminated from his position as a district manager at Waffle House after claims of sexual harassment were made against him. *Id.* Lambert had also been convicted of criminal attempted sexual abuse. However, it is unclear from the opinion whether this conviction arose from the Waffle House incident or was in addition to it. *See id.*

118. *Id.* at 77.

119. *Id.*

120. *Id.* at 76.

121. *Id.* at 75-76. The scope of the operations manual was quite broad and included, among others, provisions relating to management and personnel, payroll procedures, training, safety and sanitation, uniforms, and hours of operation. *Id.*

122. *Id.* at 77.

3. *Apparent Agency Found.*—The franchising model's focus on creating a uniform brand image makes it vulnerable to attack when viewed through the lens of the apparent agency test.¹²³ Specifically, when a franchisor is successful in selecting and monitoring its franchisees, members of the general public should not be able to tell a difference between a location that is owned by an individual franchisee versus one owned by the franchisor itself.¹²⁴ That is to say, an effective franchise operation creates an image of uniformity and consistency across its locations.¹²⁵ It is exactly this image of uniformity and consistency which is at the core of the franchising model's success because it functions to build a loyal customer base.¹²⁶

For instance, returning to the case of *Miller v. D.F. Zee's, Inc.*,¹²⁷ the court held that, in addition to the existence of an actual agency relationship between Denny's and its franchisee, there was sufficient evidence to create an issue of fact as to whether an apparent agency relationship existed as well.¹²⁸ The court noted that the Denny's trademark and logos were prominently displayed on employees' uniforms as well as restaurant signs and menus.¹²⁹ Moreover, all advertising for the company's franchised locations was done at an institutional level (with no right of control by franchisee).¹³⁰

These findings gave rise to a genuine issue of fact as to whether the franchisor's actions created an impression in the minds of outsiders that the franchisee acted under the franchisor's apparent authority.¹³¹ Moreover, since the employees were told explicitly that they were Denny's employees and because they had no reason to believe otherwise, the court held that there was also an issue of fact as to whether or not the employees justifiably believed that an agency relationship existed.¹³²

Similarly, in *Miller v. McDonald's Corp.*,¹³³ the court found that the situation presented a sufficient issue of fact for the jury as to whether McDonald's held out its franchisee as an agent.¹³⁴ Once again, the franchisee was required to

123. Jeffrey A. Brimer & Bryan C. Bacon, *Franchisor Liability for Gender Discrimination and Sexual Misconduct*, 20 FRANCHISE L.J. 188, 192 (2001).

124. BLAIR & LAFONTAINE, *supra* note 3, at 117.

125. *Id.*

126. *Id.*

127. 31 F. Supp. 2d 792 (D. Or. 1998).

128. *Id.* at 807.

129. *Id.* at 808.

130. *Id.*

131. *Id.* at 807.

132. *Id.* at 808. Although the court found only that the plaintiffs presented enough facts to defeat the franchisor's motion for summary judgment (and not necessarily to be successful at trial), it is interesting to note that this action was dismissed by the court shortly after this decision was announced because the parties had entered into settlement negotiations. See Docket Entry 197, *Miller v. D.F. Zee's*, 31 F. Supp. 2d 792 (D. Or. 1998) (No. 96-CV-01170).

133. 945 P.2d 1107 (Or. Ct. App. 1997).

134. *Id.* at 1113. The court went on to find:

comply with a “common image” created through “national advertising, common signs and uniforms, common menus, common appearance, and common standards.”¹³⁵ Interestingly, the court noted that a sign posted in the restaurant stating that the location was owned by a franchisee was not, by itself, enough to defeat a finding of apparent agency.¹³⁶

Finally, in *Butler v. McDonald’s Corp.*,¹³⁷ the court echoed these sentiments, finding that when a franchisor creates an impression of uniformity by engaging in national advertising and using highly visible logos and recognizable employee uniforms, it acts “in [a] manner that would lead a reasonable person to conclude that the [franchisee] and/or employees of the franchise restaurant [are] employees or agents of the [franchisor].”¹³⁸ That is to say, the franchisor, by its own actions, encouraged outsiders to believe that they were dealing with the franchisor whenever they dealt with the franchisee. Whether an outsider’s belief that the franchisee acts with the franchisor’s apparent authority is genuine and justifiable always becomes a question of fact for the jury. However, the court noted that in this case, such a finding arguably would be reasonable.¹³⁹

4. *No Apparent Agency Found.*—In other jurisdictions, however, a plaintiff might find that the bar is set significantly higher for establishing apparent agency. For instance, the court in *Kennedy v. Western Sizzlin Corp.*,¹⁴⁰ when viewing facts very similar to those in *D.F. Zee’s*, *Miller*, and *Butler*, found that the franchisor did nothing to create an appearance of authority in the franchisee; in fact, the court noted that the franchise agreement contained an explicit no agency provision.¹⁴¹ Making no mention of advertising schemes, logos, employee uniforms, or other potential indicia of apparent agency, the *Kennedy* court attributed a great deal of weight to this contractual provision, which expressly prohibited the franchisee from doing anything that would create an impression of agency.¹⁴² For this court, no amount of reasonable, justifiable, and detrimental reliance on the part of an outsider can serve to create a claim of apparent agency when the franchise agreement expressly prohibits the franchisee

[T]he franchise agreement require[s] the franchisee to act in ways that identif[y] it with the franchisor. The franchisor impose[s] those requirements as part of maintaining an image of uniformity of operations and appearance for the franchisor’s entire system. Its purpose [is] to attract the patronage of the public to that entire system. The centrally imposed uniformity is the fundamental basis for the courts’ conclusion that there [is] an issue of fact whether the franchisors h[o]ld the franchisees out as the franchisors’ agents.

Id. at 1112-13 (citation omitted).

135. *Id.* at 1113.

136. *Id.*

137. 110 F. Supp. 2d 62 (D.R.I. 2000).

138. *Id.* at 69-70.

139. *Id.* at 70.

140. 857 So. 2d 71 (Ala. 2003).

141. *Id.* at 78.

142. *Id.*

from acting as an agent.¹⁴³

C. Employer-Independent Contractor

Although many jurisdictions traditionally have relied on the principal-agent analysis to determine whether or not a franchisor is liable for the acts of its franchisee, some jurisdictions have employed other tests.¹⁴⁴ One such test is the employer-independent contractor analysis which can be found in the Restatement (Second) of Torts.¹⁴⁵

The difference between an agent and an independent contractor can often be difficult to identify.¹⁴⁶ Both agents and independent contractors have the ability to affect the legal position of the principal, and, in many instances, the terms can be used synonymously.¹⁴⁷ Moreover, courts who utilize the employer-independent contractor model focus primarily on the extent to which the franchisor retained control over the franchisee's operations, much like courts that use the agency approach.¹⁴⁸ Finally, as the case below indicates, many courts traditionally have been unwilling to impose liability upon franchisors for the acts of their franchisees even under the employer-independent contractor approach.¹⁴⁹

For example, in *Hoffnagle v. McDonald's Corp.*,¹⁵⁰ the court held that a franchisor did not retain enough control over the daily operations of its franchisee's restaurant (specifically its security procedures) to warrant

143. *Id.* at 78 n.3.

144. *See, e.g.,* *Coty v. U.S. Slicing Mach. Co. Inc.*, 373 N.E.2d 1371, 1374-76 (Ill. App. Ct. 1978).

145. RESTATEMENT (SECOND) OF TORTS § 414 (1965) states:

One who entrusts work to an independent contractor, but who retains the control of any part of the work, is subject to liability for physical harm to others for whose safety the employer owes a duty to exercise reasonable care, which is caused by his failure to exercise his control with reasonable care.

146. FRIDMAN, *supra* note 89, at 18.

147. *Id.* at 21.

148. *Compare* *Miller v. McDonald's Corp.*, 945 P.2d 1107, 1110 (Or. Ct. App. 1997) (pointing out that the *agency* analysis turns on the franchisor's retained right to control its franchisee), *with* *Hoffnagle v. McDonald's Corp.*, 522 N.W.2d 808, 813 (Iowa 1994) (noting that the *independent contractor* analysis turns on issues of retained control).

149. *See, e.g., Hoffnagle*, 522 N.W.2d at 814; *Coty*, 373 N.E.2d at 1375-76.

150. 522 N.W.2d at 808. A McDonald's employee sued both the franchisee (Rapid-Mac, Inc.) and the franchisor (McDonald's Corp.) for injuries suffered after being assaulted by a third party while at work. *Id.* at 810. Two men entered the restaurant, dragged the plaintiff out of the restaurant, and attempted to put her in their car. *Id.* The manager on duty intervened and foiled the attempt by bringing the employee back into the restaurant. *Id.* The men remained in the parking lot. However, the manager did not call the police or lock the doors. *Id.* Subsequently, the men returned and again attempted to take the plaintiff out of the restaurant. *Id.* Once again, the manager intervened and the men left. *Id.* This time the manager called the police. *Id.*

liability.¹⁵¹ Echoing the sentiments of the court in *Kennedy*, this court stated that “[t]he general right of supervision by the franchisor to see that business is conducted in a generally uniform manner cannot mean the franchisor . . . is responsible . . .” for the acts of its franchisee.¹⁵² The court’s analysis focused on section 414 of the Restatement (Second) of Torts,¹⁵³ under which its decision “turn[ed] on the extent of the franchisor’s retained control over the property and the daily operations of the restaurant”¹⁵⁴ The court continued, stating that “McDonald’s simply ha[d] the authority to require the franchisee to adhere to the ‘McDonald’s system,’ to adopt and use McDonald’s business manuals, and to follow other general guidelines outlined by McDonald’s.”¹⁵⁵ Moreover, the court emphasized that the franchisee controlled the daily operations of the restaurant, such as wage setting, daily training, and hiring, firing, supervising, and disciplining its employees.¹⁵⁶

D. Single Employer

In addition to the agency and employer-independent contractor approaches, a third test has become popular in some jurisdictions and especially within the federal courts of appeal.¹⁵⁷ The single employer test was originally developed by the National Labor Relations Board (NLRB) for use in resolving labor disputes. However, it has been applied subsequently by the Second, Fifth, Sixth, Eighth, Ninth, and Tenth Circuits in Title VII cases.¹⁵⁸

151. *Id.* at 814.

152. *Id.* at 815.

153. *Id.* at 813. The court also addressed section 344, since the plaintiff raised the issue in her argument. In this case, McDonald’s was not only a franchisor but also owned the land and leased it to the franchisee. Section 344 states:

A possessor of land who holds it open to the public for entry for his business purposes is subject to liability to members of the public while they are upon the land for such purpose, for physical harm caused by the accidental, negligent, or intentionally harmful acts of third persons or animals, and by the failure of the possessor to exercise reasonable care to (a) discover that such acts are being done or are likely to be done, or (b) give a warning adequate to enable the visitors to avoid the harm, or otherwise to protect them against it.

RESTATEMENT (SECOND) OF TORTS § 344 (1965). The court went on to say that an analysis under section 414 was, nevertheless, preferable. *Hoffnagle*, 522 N.W.2d at 813. Under either section, the analysis turns on the amount of control the principal exercises. In the case of section 344, it is control exercised over the property, while under section 414 it is control exercised over the daily operations of the business. *Id.*

154. *Id.*

155. *Id.* at 814.

156. *Id.*

157. *See, e.g.,* *Lockard v. Pizza Hut, Inc.*, 162 F.3d 1062, 1070 (10th Cir. 1998); *Alberter v. McDonald’s Corp.*, 70 F. Supp 2d 1138, 1142 (D. Nev. 1999) (both discussed below).

158. *Lockard*, 162 F.3d at 1070; *Garcia v. Elf Atochem N. Am.*, 28 F.3d 446 (5th Cir. 1994);

The test has four factors: interrelation of operations, centralized control of labor relations, common management, and common ownership or financial control.¹⁵⁹ Of the four factors, however, “[t]he key factor . . . is . . . whether the putative employer has centralized control of labor relations.”¹⁶⁰ More specifically, such control must be over the *daily employment decisions* of the franchisee.¹⁶¹

For example, in *Lockard v. Pizza Hut, Inc.*,¹⁶² although the franchisor had published policy statements, complaint procedures, and a training handbook, each of which addressed sexual harassment and were used by all Pizza Hut locations,¹⁶³ the court held that this was insufficient to satisfy the control requirement under the second prong of the single employer test.¹⁶⁴ Even though the franchisee’s employees were encouraged to contact the franchisor’s officials for assistance with sexual harassment claims,¹⁶⁵ the court declared that the plaintiff had failed to demonstrate how the franchisor controlled day-to-day employment decisions, that is, “what role, if any, Pizza Hut played in *implementing or effecting* these policies.”¹⁶⁶

In *Alberter v. McDonald’s Corp.*,¹⁶⁷ the court also focused on the centralized control of labor relations prong, stating that the key focus should be on “which business entity had the power to make employment decisions with respect to the

Morgan v. Safeway Stores, Inc., 884 F.2d 1211, 1213 (9th Cir. 1989); Armbruster v. Quinn, 711 F.2d 1332 (6th Cir. 1983); Baker v. Stuart Broad. Co., 560 F.2d 389 (8th Cir. 1977); *Alberter*, 70 F. Supp. 2d at 1142 (citing *Cook v. Arrowsmith Shelburne, Inc.*, 69 F.3d 1235 (2d Cir. 1995)).

159. *Lockard*, 162 F.3d at 1070.

160. *Id.*

161. *Id.*

162. 162 F.3d 1062 (10th Cir. 1998). A Pizza Hut waitress sued both the franchisee (A & M Food Service, Inc.) and the franchisor (Pizza Hut, Inc.) under Title VII for sexual harassment (hostile work environment). The plaintiff’s claim arose when two customers made repeated sexually offensive comments on one visit and physical contact with her on a subsequent visit. *Id.* at 1067. The waitress informed her supervisor, who ordered her to wait on the men nevertheless. *Id.* Upon returning to the table, one of the men grabbed her breast and put his mouth on it. *Id.* The jury found both the franchisor and the franchisee liable and awarded the plaintiff over \$200,000 in compensatory damages and costs. *Id.* at 1068. On appeal, this court affirmed the judgment against the franchisee but reversed the judgment against the franchisor. *Id.* at 1077.

163. *Id.* at 1066.

164. *Id.* at 1071.

165. *Id.* at 1066.

166. *Id.* at 1071 (emphasis added).

167. 70 F. Supp. 2d 1138 (D. Nev. 1999). A fifteen-year-old McDonald’s employee sued the franchisee (Ledbetter/McDonald’s of Lemmon Valley) and the franchisor (McDonald’s Corp.) under Title VII for sex discrimination and sexual harassment. *Id.* at 1140. The employee’s claim arose when a manager at the restaurant made repeated gender based epithets and physically touched and confined the employee. *Id.*

person claiming discrimination.”¹⁶⁸ Amongst other things, the franchisee was responsible for paying employees, establishing personnel policies, hiring and firing employees, employee discipline, employee performance evaluations, training, and approval of time off.¹⁶⁹ The franchise agreement incorporated by reference several operating manuals that the franchisee was required to follow.¹⁷⁰ However, the franchisee had the explicit option of not using the personnel manual created by the franchisor and instead could establish his own personnel policies.¹⁷¹ As a result, the court held that the franchisor did not have sufficient control over the franchisee’s labor relations to give rise to liability for the franchisor.¹⁷²

E. Summary

Regardless of which analytical framework a particular jurisdiction uses, whether it is the agency model, the employer-independent contractor approach, or the single employer test, control is the key factor examined by the courts when determining if a franchisor should be held vicariously liable for the tortious acts of its franchisee.¹⁷³ The majority of courts have traditionally turned a skeptical eye towards a plaintiff who attempts to recover from a franchisor for damages resulting from the acts of a franchisee.¹⁷⁴ Nevertheless, a distinct trend has emerged in some jurisdictions that is notably more sympathetic to the plight of the injured plaintiff.¹⁷⁵

The result is that franchisors have found themselves in a “catch 22.” In those jurisdictions that are more apt to impose vicarious liability, franchisors actually have a compelling incentive to take a more active role in supervising the operations of their franchisees in order to limit potential exposure for future claims, including claims arising under Title VII for sexual harassment and discrimination. On the other hand, in those jurisdictions that follow the more traditional approach and are less likely to impose vicarious liability, franchisors continue to be compelled to do just the opposite. That is, they have a good

168. *Id.* at 1143.

169. *Id.* at 1144.

170. *Id.*

171. *Id.* at 1144-45.

172. *Id.* at 1145. The court went on to explore the franchisor’s liability under agency principles. The court noted that the franchise agreement contained a “no agency” provision, and the court therefore held that the franchisor had not consented to the franchisee acting as its agent and could not be liable under the agency approach. *Id.* Cf. *Miller v. D.F. Zee’s, Inc.*, 31 F. Supp. 2d 792, 807 (D. Or. 1998); *Miller v. McDonald’s Corp.*, 945 P.2d 1107, 1109 (Or. Ct. App. 1997).

173. *Shelley & Morton*, *supra* note 12, at 19-20; *see also* FRIDMAN, *supra* note 89, at 18.

174. *See* *Lockard v. Pizza Hut, Inc.*, 162 F.3d 1062 (10th Cir. 1998); *Alberter*, 70 F. Supp. 2d at 1138; *Kennedy v. Western Sizzlin Corp.*, 857 So. 2d 71 (Ala. 2003); *Hoffnagle v. McDonald’s Corp.*, 522 N.W.2d 808 (Iowa 1994).

175. *See* *Butler v. McDonald’s Corp.*, 110 F. Supp. 2d 62 (D.R.I. 2000); *D.F. Zee’s, Inc.*, 31 F. Supp. 2d at 792; *Miller*, 945 P.2d at 1107.

reason not to get involved with any effort to prevent or investigate incidents of sex discrimination or harassment, since such action could tip the balance and lead a court to find that the franchisor exercised enough control over the franchisee to justify liability. The problem, of course, is that franchisors, by their nature, often operate across jurisdictional lines.

III. ARGUMENTS AGAINST HOLDING FRANCHISORS VICARIOUSLY LIABLE

A. Shoehorning Franchising into the Agency Model

Some commentators have strongly criticized the “perplexing” state of affairs that has resulted from cases such as those described above.¹⁷⁶ “If anything emerges from the case law, it is that there is no litmus test.”¹⁷⁷ Whether it is a case of “some courts . . . stretching general theories of liability”¹⁷⁸ to allow injured parties to collect from the deepest pockets¹⁷⁹ or that “courts have lagged behind the real world in their understanding of the franchise business concept,”¹⁸⁰ the result is that franchisors are left wondering to what extent they may be held liable for the acts of their franchisees.

At its core, the franchising model is based on the concept of uniformity.¹⁸¹ In general, most of the commentators addressing the issue have posited that the courts have failed to distinguish the type of control that traditionally has given rise to vicarious liability from the type of control that a franchisor must exercise to ensure that its franchise operations are uniform.¹⁸² One of the most important characteristics of a successful franchise system is that an outsider sees no difference between one location and another.¹⁸³ “This is what franchising is all about—finding a business model that works and then insisting that each franchise adhere religiously to the model.”¹⁸⁴

Without uniformity and consistency of operations, a franchise system would be little more than a very loose collection of small business owners.¹⁸⁵ Customers could no longer rest assured that the same quality of products or services would be offered at their favorite fast food restaurant, hotel, or gas

176. Randall K. Hanson, *The Franchising Dilemma Continues: Update on Franchisor Liability for Wrongful Acts by Local Franchisees*, 20 CAMPBELL L. REV. 91, 92 (1997).

177. Brimer & Bacon, *supra* note 123, at 194.

178. *Id.*

179. Gregory J. Ellis & Beth Anne Alcantar, *Franchisor Liability for the Criminal Acts of Others*, 18 FRANCHISE L.J. 11 (1998); Hanson, *supra* note 176, at 92; Shelley & Morton, *supra* note 12, at 121.

180. Shelley & Morton, *supra* note 12, at 120. Shelley describes the application of agency theory to franchising as “antiquated, silly, and absurd.” *Id.* at 119.

181. *Id.* at 121. This concept was discussed more fully *supra* Part II.

182. See Killion, *supra* note 12, at 164.

183. *Id.*

184. *Id.*

185. Shelley & Morton, *supra* note 12, at 121.

station when traveling away from home, or even when visiting different locations within the same city. In fact, they might not even recognize the restaurant, hotel, or gas station if each franchised location were permitted to control the appearance of its building and signage. Therefore, some form of franchisor control over system uniformity is absolutely vital to the franchising model's success.¹⁸⁶

When courts such as those in *D.F. Zees* and *Miller* are confronted with a franchise relationship in which the agreement commands strict compliance with detailed operational manuals, allows for frequent and unannounced franchisor inspections, prescribes the details of building design and site selection, requires attendance at franchisor-sponsored training events, mandates the use of highly visible and recognizable logos and trademarks, and allows the franchisor to terminate the franchising relationship, they see factors which convincingly indicate that the franchisor has retained sufficient control over the operations of its franchisee to justify the imposition of vicarious liability.¹⁸⁷ By the same token, however, such findings force franchisors to walk a "tightrope."¹⁸⁸ If their franchise systems are to be successful, franchisors must exercise control over their franchisees to ensure uniformity; however, franchisors now face the reality that exercising such control might make them liable for the franchisee's transgressions.¹⁸⁹

B. Some Recommendations from the Commentators

Commentators have suggested a number of recommendations aimed at ameliorating the "catch 22" that arises from cases such as *D.F. Zees* and *Miller*. Some of these suggestions are nominal at best. For instance, several commentators have recommended that franchisees be required to post signs that indicate that their location is independently owned and operated.¹⁹⁰ Moreover, these commentators recommend that franchise agreements should refer to the independent status of franchisees and expressly reject any inference of an agency

186. *Id.* at 120. Note also that the Lanham Act, 15 U.S.C. §§ 1051-1141n (2000), requires owners of trademarks, such as franchisors, to "maintain[] sufficient control of the licensee's use of the mark to assure the nature and quality of goods or services that the licensee distributes under the mark." Joseph Schumacher et al., *Retaining and Improving Brand Equity by Enforcing System Standards*, 24 FRANCHISE L.J. 10 (2004). If a franchisor "under-polices" its trademark, then it risks losing its federal registration. *Id.* However, "over-policing" the trademark can easily result in a finding of franchisor liability if a court finds that the franchisor was thereby asserting too much control over its franchisee. Ellis & Alcantar, *supra* note 179, at 12.

187. Killion notes, "Typical franchisor controls can look pervasive to judges, lawyers, and jurors who are not schooled in modern franchising." Killion, *supra* note 12, at 165.

188. Hanson, *supra* note 176, at 112.

189. *Id.*

190. *Id.*; Ellis & Alcantar, *supra* note 179, at 17; Shelley & Morton, *supra* note 12, at 127. Shelley urges that this information not only be included on signs but also on letterhead, contracts, and business cards. *Id.*

relationship between the franchisor and the franchisee.¹⁹¹

Jeffrey Brimer and Bryan Bacon suggest that franchisors should continue to assist their franchisees to prevent and reduce the occurrence of situations that might give rise to liability by providing training and advice and creating guidelines.¹⁹² They go on to state, “seemingly no amount of advice will push the franchisor into an agency relationship with its franchisee.”¹⁹³ Given the current state of the case law, however, a franchisor’s ability to rely on such a statement seems questionable at best.¹⁹⁴ It seems unlikely that courts such as the ones in *D.F. Zees* and *Miller* would be swayed by the posting of a sign indicating independent ownership¹⁹⁵ or a provision in the agreement expressly rejecting an agency relationship between the franchisor and its franchisee.¹⁹⁶

Another commentator, attorney William Killion, has recommended that the existing “right to control” test, as applied to franchisors, should be narrowed to focus only on whether the franchisor retained a right to control the actual instrumentality which led to a third person’s harm.¹⁹⁷ For example, in a case involving a franchisee who sexually harassed an employee, the court would focus not on whether the franchisor generally had the right to control its franchisee but rather on whether, and to what extent, the franchisor specifically had a right to control the franchisee’s employment policies and practices.¹⁹⁸ This revised approach focuses more acutely on whether the franchisor assumed a specific duty to the injured party and, subsequently, if that duty was breached.¹⁹⁹ In this way, the new test looks more like a negligence inquiry rather than one of vicarious

191. Ellis & Alcantar, *supra* note 179, at 17; Hanson, *supra* note 176, at 112. In addition, Shelley recommends that franchisors review the language of their operations manuals and franchise agreements and modify any provisions that might give rise to an inference that the franchisor is exercising, or has the right to exercise, day-to-day control over the franchisee. Shelley & Morton, *supra* note 12, at 127. Provisions which are not absolutely necessary to the franchisor’s goal of maintaining uniformity should be deleted altogether. *Id.*

192. Brimer & Bacon, *supra* note 123, at 194.

193. *Id.*

194. Brimer makes a strong argument that it should be against public policy for franchisors to be forced, out of fear of possible liability under the right to control test, to take an effectively hands off approach when it comes to assisting their franchisees to reduce the risk of harm to third parties. *Id.* While this point is well taken, it glosses over the fact that there is no bright line between mere advice, on the one hand, and guidelines and training regimes that might easily appear to some courts to be evidence of an agency relationship. See Killion, *supra* note 12, at 165.

195. See *Miller v. McDonald’s Corp.*, 945 P.2d 1107, 1112 (Or. Ct. App. 1997).

196. See *id.* at 1109; *Butler v. McDonald’s Corp.*, 110 F. Supp. 2d 62, 67 (D.R.I. 2000); *Miller v. D.F. Zee’s, Inc.*, 31 F. Supp. 2d 792, 807 (D. Or. 1998); but see *Kennedy v. Western Sizzlin Corp.*, 857 So. 2d 71, 78 (Ala. 2003).

197. Killion, *supra* note 12, at 166. This test has become popular especially in Texas. *Id.* (citing *Exxon Corp. v. Tidwell*, 867 S.W.2d 19 (Tex. 1993)).

198. See *id.*

199. *Id.*

liability.²⁰⁰

Underlying this new approach seems to be an assumption that it is unfair to hold franchisors liable for harm which they neither caused nor had a duty to prevent.²⁰¹ Arguably, however, vicarious liability never really seems “fair,” whether it is applied to a franchisor or any other principal, for it allows a court to pass liability to one who is technically without fault.²⁰² Yet our body of law has chosen to retain the concept.²⁰³ One strong justification for retaining franchisor vicarious liability lies in the concept of loss distribution.²⁰⁴ To the extent a franchisor is forced to pay for the transgressions of its franchisees, these costs will ultimately be spread out over the franchisor’s whole system.²⁰⁵ The cost, while potentially significant, has less of a chance of bankrupting any one party, and franchisor cost-sharing increases the chances that the injured party will recover.²⁰⁶ Moreover, retaining vicarious liability forces franchisors, who benefit monetarily from the activities of their franchisees, to share in some of the burdens when franchisees make poor business decisions.

Professor John L. Hanks has suggested yet another option—one that would discard existing theories of franchisor vicarious liability altogether in favor of a new system that imposes “guarantor status” on franchisors.²⁰⁷ Under this approach, “plaintiffs would not have a cause of action against a franchisor (assuming the franchisor has not itself been negligent) unless the franchisee was unavailable to be sued or unable to pay a judgment.”²⁰⁸ The most striking benefit for franchisors, of course, is that in most cases they would not be named as co-defendants in suits against their franchisees.²⁰⁹ As a result, Hanks argues, franchisors would enjoy substantially reduced litigation costs, while third parties injured by franchisees would benefit by still having a back-up source of payment in case the franchisee was insolvent.²¹⁰

There are two problems with this argument. First, it tends to reward

200. *See id.* The result, of course, is that it would be much more difficult for a party injured by a franchisee to assert a claim against the franchisor. Even if a particular franchisor exercised rather tight control over its franchisee (i.e., control sufficient to justify the finding of an agency relationship under the traditional test) in all areas but the franchisee’s employment practices, an employee seeking to recover from the franchisor in a sex discrimination suit would be unable to establish a *prima facie* case under the new test.

201. *See id.* at 165. Killion argues that franchisees, not franchisors, are in the best position to prevent harm from occurring to third parties and that franchisors simply do not have enough contact with their franchisees to control their behavior.

202. ATIYAH, *supra* note 82, at 13.

203. *See id.* at 19-20.

204. *Id.* at 22.

205. *See id.* at 26.

206. *Id.*

207. Hanks, *supra* note 49, at 8-9.

208. *Id.* at 9.

209. *Id.* at 32.

210. *Id.*

insolvent franchisees by paying their judgments, while it simultaneously punishes financially sound franchisees to the extent that it forces them to bear the full costs of judgments on their own. Second, it seems unlikely that franchisors would realize a dramatic reduction in litigation costs. Although a franchisor might not be officially named a co-defendant, it still would have a vested interest in the outcome of the litigation insofar as a judgment against the franchisee might end up later becoming the franchisor's liability if the franchisee proves to be insolvent.

C. Summary

Arguably, the current state of uncertainty in the case law sends a conflicting message to franchisors. Namely, they are forced to wonder whether the law requires them to take an active, hands-on approach to their relationships with franchisees, or whether such activity is in fact discouraged—a mixed message that is arguably unfair to franchisors. But is it necessary to dispose of franchisor vicarious liability altogether in order to bring some fairness back to the equation? In the next section, this Note suggests that adding an affirmative defense to the existing regime of franchisor vicarious liability would serve as an effective tool for encouraging franchisors to take an active role in addressing the problem of workplace sexual harassment and discrimination.

IV. THE CASE FOR FRANCHISOR VICARIOUS LIABILITY AND THE CREATION OF AN AFFIRMATIVE DEFENSE

A. Introduction

The Supreme Court has stated that “Title VII [was] designed to encourage the creation of antiharassment policies and effective grievance mechanisms.”²¹¹ Of these two aims, however, prevention is the primary focus under Title VII,²¹² as it should be since the costs of sex discrimination and harassment can be staggering. One study found that employers pay on average between \$25,000 to \$50,000 to settle sexual harassment claims.²¹³ In 2004, complaints to the EEOC resulted in the recovery of over \$100 million dollars for victims of sex discrimination.²¹⁴ Moreover, since the late 1990s, “settlements paid to sexual harassment victims have increased 600 percent”²¹⁵ Employers also face

211. *Burlington Indus., Inc. v. Ellerth*, 524 U.S. 742, 764 (1998).

212. *Faragher v. City of Boca Raton*, 524 U.S. 775, 805-06 (1998).

213. Danielle R. Birdeau et al., *Effects of Educational Strategies on College Students' Identification of Sexual Harassment*, 125 EDUCATION 496, 506 (2005). These figures do not take into account the possibility of occasional but dramatically higher individual judgments and settlements. See KATHLEEN NEVILLE, INTERNAL AFFAIRS: THE ABUSE OF POWER, SEXUAL HARASSMENT, AND HYPOCRISY IN THE WORKPLACE 199 (2000).

214. Equal Employment Opportunity Commission, Sex-Based Charges FY 1992—FY 2004, <http://www.eeoc.gov/stats/sex.html> (last visited July 25, 2006).

215. Birdeau et al., *supra* note 213, at 506.

additional costs relating to negative public perception and decreased investor confidence.²¹⁶ Additionally, the victims of sexual harassment and discrimination also pay dearly, as they often suffer serious physical and emotional symptoms and are sometimes even diagnosed with psychiatric disorders.²¹⁷ In turn, this often means increased costs for employers due to poorer work performance and decreased workplace morale.²¹⁸

B. Rationale in Support of Liability

Franchised businesses have a significant impact on the economy and employ vast numbers of workers.²¹⁹ As a result, franchisors are in a unique position to implement the mandates of Title VII. They have vast distribution channels and have been proven testing grounds for highly successful marketing and business techniques.²²⁰ If franchisor vicarious liability is discarded altogether, as many commentators have suggested it should be, there will be little, if any, incentive for franchisors to take a role in preventing sexual harassment and discrimination within their systems.

At the same time, retaining franchisor vicarious liability without some modification is unfair to franchisors, for no business entity can successfully operate within a legal system that sends mixed messages about what its obligations under the law are to be. In order to send a strong message to franchisors that they should take an active part in preventing sexual harassment and discrimination in the American workplace and that such action will be rewarded, this Note suggests the creation of an affirmative defense to franchisor vicarious liability.

C. The Affirmative Defense

Whether or not one supports franchisor vicarious liability, the fact remains that all of the current factor sensitive approaches serve as disincentives for franchisors to become involved in the implementation of Title VII. The more a franchisor gets involved in the employment practices of its franchisees, the more likely it will be found to have control over such areas.²²¹ There is no “quick fix”

216. NEVILLE, *supra* note 213, at 189-90. Such costs can take the form of negative perceptions by both customers and investors. *Id.*

217. SHARYN ANN LENHART, CLINICAL ASPECTS OF SEXUAL HARASSMENT AND GENDER DISCRIMINATION 135 (2004). Physical symptoms range from gastrointestinal disorders and fatigue to back pain and muscle spasms. *Id.* Psychologically, many victims report not only anxiety and feelings of guilt and shame but are also diagnosed with sleep, stress, and depressive disorders. *Id.*; see also NEVILLE, *supra* note 213, at 202-07.

218. LENHART, *supra* note 217, at 131. It follows that employers probably also experience higher costs for funding employee health insurance plans when victims seek medical and psychological treatment as a result of workplace harassment and discrimination.

219. ECONOMIC IMPACT, *supra* note 1, at 10.

220. See BOROIAN & BOROIAN, *supra* note 7, at 66-67.

221. See, e.g., *Miller v. McDonald's Corp.*, 945 P.2d 1107, 1110 (Or. Ct. App. 1997).

to the problem of sexual harassment and discrimination,²²² but franchisors can play a vital role in implementing a comprehensive solution to the problem. For this reason, the affirmative defense would relieve franchisors from liability for sexual harassment and discrimination claims if they met a series of bright-line factors.

1. *Creation of a System-wide Non-discrimination Policy.*—Franchisors have proven themselves to be highly successful business innovators.²²³ They develop comprehensive business systems which allow franchisees to realize the dream of small business ownership without “the attendant growing pains” of starting a business from the ground up.²²⁴ It follows, then, that a franchisor is in a unique position to design and implement a highly effective non-discrimination policy which would be tailored to the uniform needs of the franchisees within its system. Such a policy should be a written statement of the particular franchise system’s stance against workplace sexual harassment and discrimination²²⁵ and should be uniformly adopted by the franchisor and all of its franchisees. The policy should clearly describe what constitutes sexual harassment and discrimination, how an employee should make a report, and what actions the franchisee and franchisor will take to investigate and correct the problem.²²⁶

2. *Training for Franchisees and Their Supervising Employees.*—A policy statement alone likely would be insufficient to combat the problem, but at least one study has found that adding a training component can be an effective way to prevent sexual harassment and discrimination from occurring in the first place.²²⁷ Most franchisors already require their franchisees to attend some form of training prior to operating a franchised location,²²⁸ and sexual harassment and discrimination training would be a natural addition. In effect, this approach would save franchisees the expense of single-handedly creating and implementing their own training programs by allowing them to pool their resources, much like they already do with marketing expenses. That said, however, the creation of a comprehensive sexual harassment and discrimination policy and the implementation of a training regime alone are likely not enough. For instance, one study suggests that subordinates are more likely to report when there is an alternative reporting channel “outside of the normal chain of

222. NEVILLE, *supra* note 213, at 160.

223. See DICKE, *supra* note 2, at 1.

224. BOROIAN & BOROIAN, *supra* note 7, at 17.

225. NEVILLE, *supra* note 213, at 219; see also Equal Employment Opportunity Commission, Model EEO Programs Must Have an Effective Anti-Harassment Program, <http://www.eeoc.gov/federal/harass/index.html> (last visited July 25, 2006).

226. *Id.*

227. See, e.g., Birdeau et al., *supra* note 213, at 504, 508.

228. Even after the franchisee has started his or her franchise location, franchisors often provide ongoing support and training. For instance, McDonald’s operates “Hamburger University” in Oakbrook, Illinois, for the purpose of training both its own as well as its franchisees’ employees. See McDonald’s Corp., Hamburger University Homepage, http://www.mcdonalds.com/corp/career/hamburger_university.html (last visited July 25, 2006).

command.”²²⁹

3. *Creation of an Alternative Reporting and Investigative Channel.*—In order to address the problem, franchisors and franchisees need to know that it exists.²³⁰ However, employees are less likely to report harassment or discrimination if they do not feel safe telling their direct supervisor.²³¹ In the franchising context, this would be especially true where the franchisee himself or herself was responsible for the discrimination or harassment. In such a situation, franchisors are especially well suited to serve as an alternative reporting and investigation channel. The affirmative defense would require that franchisors create some form of centralized call center to handle incoming complaints from employees who felt unsafe reporting directly to their franchisee. Moreover, the call center would initiate a franchisor-led investigation of such complaints.

4. *Clear Notice to all Employees Within the Franchisor’s System.*—Every employee in the franchise system must be aware of the uniform policy and of the existence of the alternative reporting and investigative channel.²³² This would be accomplished by requiring that information be posted in every location which both clearly describes the non-discrimination policy and informs employees of the call center maintained by the franchisor. Such a poster should be similar to those which inform employees of minimum wage requirements.

5. *Financial Responsibility and Insurance Requirements.*—Finally, in most cases, a franchisee’s general liability insurance policy will not cover claims for sexual harassment and discrimination.²³³ For this reason, a franchisor should require in the franchise agreement that its franchisees maintain adequate “employment practices liability insurance,” which is specifically designed to cover employee claims of sexual harassment.²³⁴ To ensure that franchisees maintain adequate coverage, franchisors should periodically request proof of insurance from the franchisee. Moreover, the franchise agreement should contain a provision that allows the franchisor to terminate the relationship if a franchisee is unwilling or unable to maintain an adequate policy.

D. Implementing the Affirmative Defense

On occasion, the Supreme Court has shown a willingness to expand the meaning of Title VII. For instance, in the landmark case of *Meritor Savings*

229. Juanita M. Firestone & Richard J. Harris, *Perceptions of Effectiveness of Responses to Sexual Harassment in the US Military, 1988 and 1995*, 10 GENDER, WORK & ORG. 42, 58-59 (2003).

230. NEVILLE, *supra* note 213, at 94.

231. See Firestone & Harris, *supra* note 229, at 58.

232. Birdeau et al., *supra* note 213, at 506.

233. Ed. E. Duncan, *Insurance Coverage for Sexual Harassment in the Workplace*, 51-2 PRAC. LAW 51, 63 (2005).

234. *Id.* at 60. Such policies might also include coverage for claims made by applicants for employment or other third parties, such as customers. *Id.*

Bank v. Vinson,²³⁵ the Court recognized for the first time that sexual harassment which creates a hostile work environment is an actionable form of sex discrimination, even though the language of Title VII does not explicitly refer to sexual harassment.²³⁶ Subsequently, in the companion cases of *Burlington Industries, Inc. v. Ellerth*²³⁷ and *Faragher v. City of Boca Raton*,²³⁸ the Court held that employers are subject to vicarious liability when a supervisor creates a hostile work environment through sexual harassment of a subordinate employee.²³⁹ At the same time, however, the Court created an affirmative defense²⁴⁰ for employers, which allows them to avoid such vicarious liability when the following conditions are met: (1) no tangible employment action²⁴¹ against the employee has occurred; (2) the employer “exercised reasonable care to prevent and correct promptly any sexually harassing behavior;”²⁴² and (3) the “employee unreasonably failed to take advantage of any preventative or corrective opportunities provided by the employer or to avoid harm otherwise.”²⁴³

Likewise, the affirmative defense proposed here would allow franchisors to avoid vicarious liability for sex discrimination and harassment claims made by employees against franchisees. Much like the *Ellerth/Faragher* defense, it would “recognize the [franchisor’s] affirmative obligation to prevent violations and give credit . . . to [franchisors] who make reasonable efforts to discharge their duty.”²⁴⁴ One obvious problem with relying on the judicial creation of an affirmative defense, however, is that franchisors would not be on notice, and thus they would not begin implementing the preventative practices recommended above until the Supreme Court had the opportunity to hear a case involving this matter.

Perhaps, then, there is a better approach. This Note suggests that there are at least two. First, Congress could amend Title VII to explicitly include

235. 477 U.S. 57 (1986).

236. *Id.* at 66-67. The Court noted that this had long been the position of the EEOC and various courts of appeal. *Id.*

237. 524 U.S. 742 (1998).

238. 524 U.S. 775 (1998).

239. *Ellerth*, 524 U.S. at 765.

240. This Note does not propose an extension of the *Ellerth/Faragher* defense to franchisors. Rather, the *Ellerth/Faragher* defense is mentioned because it serves as an example of the Supreme Court’s willingness to shield employers from sexual harassment liability when certain conditions are met.

241. A tangible employment action includes, for instance, being terminated, demoted, or denied a raise or promotion. *Ellerth*, 524 U.S. at 761. If a tangible employment action occurs, then the *Ellerth/Faragher* affirmative defense is not available to the employer. *Faragher*, 524 U.S. at 808. The franchisor affirmative defense proposed here would differ from *Ellerth/Faragher* in that it would be available to franchisors even when a tangible employment action occurred.

242. *Ellerth*, 524 U.S. at 765.

243. *Id.*

244. *Faragher*, 524 U.S. at 806.

franchisors within the definition of the term employer.²⁴⁵ Under this approach, Congress would also create a statutory affirmative defense similar to the one suggested above in Part IV.C. In the alternative, the EEOC, which already creates regulations and guidance documents for the implementation of Title VII, could take on the role of creating the affirmative defense.²⁴⁶

Action by Congress or the EEOC has two primary benefits. First, it would allow for a comprehensive study of the issue. Arguably, there are many questions which remain to be answered. For instance, should all franchisors be subject to vicarious liability and the affirmative defense, or should franchisors with only a few locations be exempt? And, are there other elements that should be included in the affirmative defense? Second, and perhaps more importantly, it would give franchisors prospective notice of the affirmative defense and allow them to begin taking an active role in addressing the problem of workplace sexual harassment and discrimination sooner rather than later.

CONCLUSION

Franchising has revolutionized the way the United States does business.²⁴⁷ As a group, franchised businesses now employ significant numbers of workers and generate considerable economic activity. Unfortunately, the problem of sexual harassment and discrimination has also become an increasingly recognized phenomenon in the modern American workplace. This Note advocates that franchisors stand in a unique position to bring about yet another business revolution by taking an active role in the sexual harassment and discrimination policies of their franchisees.

Under the approach advocated here, franchisor vicarious liability would be retained as it recognizes that franchisors often exercise sufficient control over their franchisees to justify holding them responsible when their franchisees discriminate on the basis of sex. By the same token, the creation of an affirmative defense would allow franchisors to use their unique positions of control to influence the sexual harassment and discrimination policies and practices of their franchisees without fearing that such action will ultimately increase their chances of being held liable. Giving responsible and active franchisors a shield from liability represents a positive step towards shielding the nation's workers from workplace sexual harassment and discrimination.

245. Title VII's definition of the term employer is found at 42 U.S.C. § 2000e(b) (2000).

246. *See, e.g.*, 42 U.S.C. 2000e-4(g)(5), which states that the EEOC is empowered "to make such technical studies as are appropriate to effectuate the purposes and policies of this subchapter and to make the results of such studies available to the public."

247. McDonald's Corp. stands as a vivid example. The company, which started a mere fifty years ago as a hamburger stand, now has more than 30,000 locations and is the world's largest owner of real estate. McDonald's Investor Fact Sheet, http://www.mcdonalds.com/corp/invest/pub/2006_fact_sheet.html (last visited July 25, 2006); BOROIAN & BOROIAN, *supra* note 7, at 27.