



Vol. 13 No. 2 | Spring 2010

#### THE FRANCHISE LAWYER

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#### Forum on Franchising

American Bar Association 321 N. Clark Street Chicago, IL 60654 312-988-5666

#### **Message from the Chair**

Fortunately for all of us, the founders of the ABA Forum on Franchising recognized long ago the importance of institutionalizing the process of recruitment, training and promotion of leaders. Indeed, the mark of a great organization is one that identifies, cultivates and promotes good people. *Read more...* 

#### **2010 Nominating Committee Selected**

Ronald K. Gardner, Chair of the Forum, is pleased to announce the appointment of the 2010 Nominating Committee. The committee, which is headed by the Immediate Past Chair, is responsible for recommending candidates to fill open positions on the Governing Committee. *Read more...* 

#### 33rd Annual Forum on Franchising

Please join us for the 33rd Annual Forum on Franchising from October 13 – 15, 2010, at the Hotel Del Coronado in San Diego, CA. The "Del" was the site of the Billy Wilder classic film *Some Like it Hot*, has hosted presidents and dignitaries since its opening in 1888, and boasts one of the best beaches in a state known for its beaches. *Read more...* 

#### A Tribute to Janet Reyes

Shortly after the Forum on Franchising meeting this past October, Janet Reyes succumbed to cancer which she fought valiantly after being diagnosed in the Spring of 2009. Janet was an exceptional franchise paralegal, a consummate professional who went out of her way to make sure that the attorneys she worked with shined. *Read more...* 

#### Ready For Trial, Your Honor

In a word, winning at trial requires preparation. Weeks before trial you know every document, transcript and point of law, and you have outlined every examination and argument. You know the case better than your client does and certainly more than your opponent ever will. If these things are not true, then you are not ready for trial. *Read more...* 

#### New Federal Gift Card Regulations to Become Effective on August 22, 2010

On March 23, 2010, pursuant to the Credit CARD Act, the Board of Governors of the Federal Reserve issued Gift Card Regulations which become effective on August 22, 2010. This article will help franchisors and franchisees with gift card programs prepare for the new law. *Read more...* 

### Proposed Arbitration Fairness Act Of 2009 Friend or Foe in Franchising?

In February 2009, Representative Henry Johnson (D) of Georgia introduced legislation known as the "Arbitration Fairness Act of 2009 to remedy what he and many others perceive as failings of the Federal

Arbitration Act. If passed, it would ban the enforceability of pre-dispute arbitration agreements in franchise, as well as employment and consumer, disputes. *Read more...* 

#### **Books from the Forum on Franchising**

**Annual Franchise and Distribution Law Developments 2009** 

Joel R. Buckberg and Jon P. Christiansen

International Franchise Sales Laws - 2009 Supplement

Andrew P. Loewinger and Michael K. Lindsey, Editors

Financial Performance Representations: The New and Updated Earnings Claims

Stuart Hershman and Joyce G. Mazero

**Fundamentals of Franchising, Third Edition** 

Rupert M. Barkoff and Andrew C. Selden, Editors

**Antitrust Handbook for Franchise and Distribution Practitioners** 

Co-published with the ABA Section of Antitrust Law

**Back to Top** 

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Vol. 13 No. 2 | Spring 2010

#### **INSIDE THIS EDITION**

Message from the Chair

2010 Nominating Committee Selected

33rd Annual Forum on Franchising

A Tribute to Janet Reyes

Ready For Trial, Your Honor

New Federal Gift Card Regulations to Become Effective on August 22, 2010

Proposed Arbitration Fairness Act Of 2009

Friend or Foe in Franchising?

Books from the Forum on Franchising

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The single biggest way to impact an organization is to focus on leadership development. There is almost no limit to the potential of an organization that

recruits good people, raises them up as leaders and continually develops them.

—John C Maxwell, The 17th Irrefutable Laws of Teamwork (2001, 185)

As professionals, most of whom are engaged daily in the politics of law firms and/or corporations, it is my suspicion that the vast majority of us are called upon at different times to lead in our work, communities or places of worship. I also suspect that those of us who have been called to lead understand the truth of the above-quoted maxim—the mark of a great organization is one that identifies, cultivates and promotes good people.

Fortunately for all of us, the founders of the Forum recognized long ago the importance of institutionalizing the process of recruitment, training and promotion of leaders.

Elsewhere in this newsletter you will find the official announcement of the appointment of this year's Nominating Committee. Under our By-laws, the Nominating Committee is chaired by the Immediate Past Chair of the Forum, and is "comprised of at least three members of the Forum who are not candidates for any Forum office, at least one of whom is neither a past nor present officer or member at large of the Governing Committee." Further, Section 6.1 of our By-laws requires me, in my role as Chair of the Forum to "consider appropriate representation of types of organizations, practice areas, geographic areas, minorities and women, so that the Nominating Committee may reflect the diversity of members of the Forum." Guided by these principles, I am pleased that a well-qualified and diverse Nominating Committee has been selected.

As you will see in the more formal announcement, joining our Immediate Past Chair Jack Dunham on our Nominating Committee this year are Past Chair Susan Grueneberg, along with Alex Brito of Zarco, Einhorn, Salkowski & Brito, Stuart Hershman of DLA Piper and Mark Kirsch of Plave Koch. These five people are diverse in many ways, including perhaps most importantly, diverse in their viewpoints. It is these five people on whom we all rely to use their best efforts and wisdom in selecting our next generation of leaders. I am extraordinarily confident that their discussions will lead us in the right direction.

Notably, nominations this year have taken on a new significance. Besides being charged with nominating my successor, this year's Nominating Committee will be charged with nominating successors to the three members of the Governing Committee whose terms will be expiring in 2011 (Kerry Bundy, Kathy Kotel, and Leslie Smith), as well as filling two of the three vacancies that have been created by the adoption of the

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Amendment to the By-laws that we passed in Toronto. (As you may recall, the Forum voted to expand the Governing Committee from 9 At-Large members to 12 At-Large members. The implementation of that change calls for an addition of two new members in the current nominating cycle for 2011, and a third new member in the nominating cycle for 2012.) Of course this change not only means a lot of work for the Nominating Committee itself, but will also require additional thought and input from you, our members.

The Nominating Committee announcement, which will also be sent via the List Serv and otherwise, also includes our formal call for nominations. Between now and June 4, I urge you to give some thought to those individuals in our Forum community that you believe possess the qualities necessary to lead this great organization into the future. We are particularly interested in members who have demonstrated a strong commitment to the organization, through writing, speaking, and successful fulfillment of other leadership opportunities, as well as being interested in those people who coordinate and lead "behind the scenes." If you know of any such person, it is our strong hope and expectation that you will share their names and qualifications with us so that we might consider them in the pool of potential nominees for this year's upcoming Governing Committee class.

Once the Nominating Committee concludes its work, a nominated class of individuals will be announced sometime in June for your consideration. We then will, as we always do, hold an election to approve or disapprove that slate of candidates at our annual meeting in October.

And speaking of our annual meeting, do you have it on your calendar yet? Our brochures are in process, and you can be certain that you will see them in the next few weeks. Having had a "sneak peek" at the programs and speakers that Deb Coldwell and Kathy Kotel have put together for us, I can hardly wait to get to the Hotel Del Coronado in San Diego for this year's Forum! It promises to be one of the best ever.

To make this year a more viable alternative for new young members, the Forum has also adopted a \$500 discount in registration for lawyers who are under the age of 36 and will be attending the Forum for their first or second time. After lots and lots of thought and discussion, the Governing Committee has taken this dramatic step to make it much easier for firms and companies to bring their young lawyers to the Forum. Like nominations, our future membership also relies on our ability to pass on what we do so well to the next generation. We are hoping that this significant financial commitment on behalf of the Forum will entice you, and your colleagues, to seek out and bring with you to San Diego an exciting new generation of lawyers who will be proud to be part of this prestigious organization.

I look forward to seeing you in San Diego October 13-15. In the meantime, get those nominations ready—we need your help!

#### **Back to Top**

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Vol. 13 No. 2 | Spring 2010

#### **INSIDE THIS EDITION**

Message from the Chair

2010 Nominating Committee Selected

33rd Annual Forum on Franchising

A Tribute to Janet Reyes

Ready For Trial, Your Honor

New Federal Gift Card Regulations to Become Effective on August 22, 2010

Proposed Arbitration Fairness Act Of 2009 Friend or Foe in Franchising?

Books from the Forum on Franchising

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#### **2010 Nominating Committee**

In accordance with the Forum's By-Laws, the annual Governing Committee election process begins with the appointment of a Nominating Committee by the Forum Chair. The committee, which is headed by the Immediate Past Chair, is responsible for recommending candidates to fill open positions on the Governing Committee.

Ronald K. Gardner, Chair of the Forum, is pleased to announce the appointment of the following members to the 2010 Nominating Committee:

#### Edward Wood Dunham, Chair

Wiggin & Dana LLP edunham@wiggin.com

#### Alejandro Brito

Zarco Einhorn Salkowski & Brito, P.A. abrito@zarcolaw.com

#### Susan Grueneberg

Snell & Wilmer LLP sgrueneberg@swlaw.com

#### Stuart Hershman

**DLA Piper** 

Stuart.hershman@dlapiper.com

#### Mark A. Kirsch

Plave Koch PLC

mkirsch@plavekoch.com

This year's Nominating committee will recommend candidates for three Member-at-Large positions on the Governing committee beginning August 2011, when Kerry Bundy, Kathy Kotel and Leslie Smith complete their terms. The Committee will also nominate candidates to fill two new at-large positions, as well a current Governing Committee member to succeed Mr. Gardner as the next Chair of the Forum. Finally, the Committee may also be required to nominate someone to fill the remaining term of the GC member who is selected as the next Forum Chair, depending on the length of time remaining on the Chair-designate's current term at the time of the election.

An election to fill these positions will take place at the Forum's Annual Business Meeting, which will be held in

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conjunction with the 33rd Annual Forum on Franchising. This meeting will take place on Thursday or Friday, October 14 or 15, 2010, in Coronado, California. Forum members wishing to recommend candidates to fill these positions should convey their comments in writing to Jack Dunham **no later June 4, 2010**.

#### **Back to Top**

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American Bar Association • Forum on Franchising

Vol. 13 No. 2 | Spring 2010

#### **INSIDE THIS EDITION**

Message from the Chair

2010 Nominating Committee Selected

33rd Annual Forum on Franchising

A Tribute to Janet Reyes

Ready For Trial, Your Honor

New Federal Gift Card

Regulations to

Become Effective on August

22, 2010

Proposed Arbitration Fairness
Act Of 2009

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The program schedule is loaded with educational and entertaining offerings.

- During the plenary session *Strategic and Tactical Decision-Making: What Do Your Peers Think of Your Decisions?*, compare your decisions with those of your peers and our panel of experts.
- On Wednesday, plan to attend our half day intensive workshop on social media to learn everything
  you ever wanted to know about social media for your practice, your clients, or your franchise
  system. Or attend the always popular *Fundamentals of Franchising* intensive.
- On Thursday and Friday, choose from our many engaging workshops including Advanced
  Disclosure Issues: Pushing the Envelope, Bet the System Litigation, Gift Cards and Loyalty
  Programs, Litigating Unlawful FPR's, Protecting the Franchise Brand in the Age of Social Media,
  The Fundamentals of an M & A Transaction in a Franchise System, two new Fundamentals 201
  Series programs, and more.
- On Friday morning, we will hear a recap of the most important franchise cases and decisions from the past year in one of the Forum's signature events, *Annual Developments*.

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#### Forum on Franchising

American Bar Association 321 N. Clark Street Chicago, IL 60654 312-988-5666 For entertainment and networking, there will be many unique events to help you enjoy the gorgeous October weather in Southern California. First, we will meet Wednesday evening for the Welcome Reception on the Del Sundeck and can watch the sunset from a one of a kind vantage point. On Thursday night, we will enjoy an All-American barbecue on the beach complete with burgers, 'dogs, fire pits and Jimmy Buffet-style music. On Friday night, there will be a ticketed event at the San Diego Zoo to experience the new Elephant Exhibit and dine at the Sabertooth Grill. Saturday morning, we will end our stay at the Del with our community service project, a coastal habitat clean-up event at the mouth of the San Diego River on Ocean Beach.

Please mark your calendars now for October 13th–15th to attend great workshops, network with old and new friends, and enjoy a hotel designated as a National Historic Landmark.

Please look for more details about the Annual Meeting in May 2010 here.

We look forward to seeing you there!

#### **Deb Coldwell and Kathy Kotel**

Co-chairs of the 33rd Annual Forum Meeting

**Back to Top** 

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# Forum on Franchising Flanchising Flanchising Franchising Flanchising Franchising Flanchising Flanchisi

American Bar Association • Forum on Franchising

Vol. 13 No. 2 | Spring 2010

#### **INSIDE THIS EDITION**

Message from the Chair

2010 Nominating Committee Selected

33rd Annual Forum on Franchising

A Tribute to Janet Reyes

Ready For Trial, Your Honor

New Federal Gift Card Regulations to Become Effective on August 22, 2010

Proposed Arbitration Fairness Act Of 2009 Friend or Foe in Franchising?

Books from the Forum on Franchising

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## A Tribute to Janet Reyes, 1953-2009

Shortly after the Forum on Franchising meeting this past October, Janet Reyes succumbed to cancer which she fought valiantly after being diagnosed in the Spring of 2009. Janet was an exceptional franchise paralegal, with accolades from John Baer who had the wisdom to hire her in 2000 while with the firm, Sonnenschein, Nath & Rosenthal

LLP. Janet also worked closely with Shelley Spandorf who proceeded to invite Janet to join her when Davis Wright Tremaine expanded their franchise practice. The attorneys who Janet worked with all delighted in the attention and care she showed to clients who Janet quickly befriended. Perhaps Janet's greatest professional talent was her ability to connect with clients and co-workers at the human level. Foremost, Janet was a people person yet a consummate professional who went out of her way to make sure that the attorneys she worked with shined.

Before Janet joined Sonnenschein as a Senior Paralegal in the firm's franchise and distribution practice group, Janet was with McDonald's Corporation for eight years, and before that, she was with VMS Realty Partners, a real estate syndicator/developer, for six years. While at McDonald's, Janet worked closely with the company's Chief Franchising Officer on McDonald's national franchise rewrite program. Janet was selected as a charter member of a total quality management team to evaluate and improve McDonald's Franchising Department. She also received two McDonald's awards, The McDonald's Way award, and Senior Management recognition certificate.

During her six years at VMS Realty Partners, Janet assisted in-house and outside legal counsel in numerous real estate transactions, managing and closing complex real estate and financial transactions ranging from \$50-\$100 million per project. Janet was humble about all of these things including her determination to further her education in the evenings, with the completion of Roosevelt University's Lawyer's Assistant Program (with honors) and, in 1998, received her Bachelor's degree in Business Administration/ Management with highest honors from Lewis University, graduating with a perfect 4.0.

As a leader in franchise administration, Janet enthusiastically joined Joan Painter as co-chair of the Franchise Administrators Network which provides resources and support to franchise paralegals. Joan and Janet instantly became friends and only later discovered that they shared the same birthday after setting up FaceBook accounts. Janet was the first franchise paralegal to be invited to speak at the annual meeting of the ABA Forum on Franchising which she did in October, 2008. She was especially proud of this, but one would never know as she was so humble about her professional accomplishments. Janet was a teacher to many franchise paralegals, always willing to share her knowledge and experience with others by arriving annually with updates and contacts for the group. She always spoke well of others, was focused and enjoyed every minute which was demonstrated by a warm smile and time to chat.

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She knew far more about franchise law and franchise relationships and her skills extended beyond the technical laws regulating franchise sales disclosure and registration. She was on a first name basis with all of the state franchise examiners who universally respected her for her practical wisdom and calm demeanor and welcomed being assigned to Janet's files, for "every exchange with Janet was enjoyable."

In addition to being an ardent supporter of the ABA Franchise Forum, Janet was a dedicated member of the Chicago chapter of the Franchise Business Network, through which many of the leading franchising professionals in the Chicago area got to know Janet and quickly came to admire her. She served as a role model for others aspiring to be an active participant in the franchise community—she knew how to do it and how to do it right, always with a sense of humor.

Accolades of Janet from attorneys that she worked with include statements such as "working with Janet meant never having to worry about missing a deadline, or being on top of the latest developments regarding filing requirements. She made the paper-intensive registration process easy and always had good ideas about how to improve it. Apart from being the ultimate franchise paralegal, Janet was also an absolute delight to work with. She brightened up the gloomiest day with a big smile and a never-ending stream of witty e-mails. She is missed by all of those who had the pleasure of working with her. Those who didn't can be doubly sad for not having had that experience" and "Janet quite simply was the best paralegal I have ever worked with."

There is no doubt that Janet's professional accomplishments took second to her role as an amazing single mother to her children. The love for her children Jenny and Jascha was always top priority. She coached soccer teams and supported and encouraged their passions. She valued family dinners and conversations around the kitchen table. Janet's home was also very important to her. From the steward of the street storm drain to block party organizer she enjoyed her neighborhood.

Janet also enjoyed travel. She loved the beaches of Southwest Florida; she was passionate about looking for sharks teeth on the beach during the early morning hours of the low tide. In 2007, she had a most memorable trip to Egypt often reminding herself that she had really been there. Her travel journeys continued on a motorcycle and often times in a convertible with her significant other, Gene. She loved being in the great outdoors whether it be at a backyard fire pit, long walks, taking in a sunrise on Chicago's lakefront or Miami Beach, etc. But her greatest traveling pleasure was enjoying the sunsets from the beach in Southwest Florida. Janet was as comfortable relaxing in shorts and tank top as she was fashionably prepared and elegantly dressed for a night on the town, a play, or concert. In each of these settings Janet loved to snap pictures with her camera. She had "the eye." Her pictures were of professional quality. The large digital camera would pop out during almost any event or occasion. These photos are a great testimony of the wonderful times we all had together.

Janet leaves her daughter, Jenny (Sean) Neilly, her son Jascha Reyes, her beloved significant other, Gene Sapinski as well as her grandmother, sister, nieces and her loyal dog Fritz. She was a treasure: our colleague and friend, and we will greatly miss her.

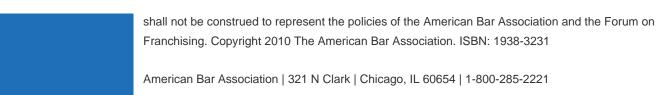
#### Joan Painter

Franchise Ventures, LLC

#### **Back to Top**

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Message from the Chair

2010 Nominating Committee Selected

33rd Annual Forum on Franchising

A Tribute to Janet Reyes

Ready For Trial, Your Honor

New Federal Gift Card Regulations to Become Effective on August 22, 2010

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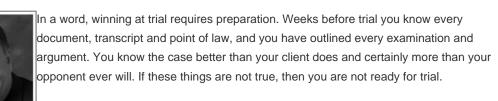
Associate Editors

#### Ready For Trial, Your Honor

Editor's Note. We asked two experienced trial lawyers, one from each side of the franchisor/ franchisee aisle, but who happen to have offices located in the same zip code in Chicago, to ruminate on their approaches to being ready for trial. We hope you find the result to be useful and illuminating.

#### Carmen D. Caruso

The Law Office of Carmen D. Caruso, P.C.



Visualizing the trial began when your Forum friend introduced your new client, who explained a business problem and sought solutions. You listened carefully. Then you

explained that the only way—repeat, the only way—to win in negotiations is to demonstrate your capacity and willpower to win at trial.

Knowing your client is the first essential step. Will your client wear the white hat? Keep in mind that this case is a close call. If it were one-sided, it would have been settled or decided by motions.

As Lincoln used to say, where is the rub? What evidence will sway the decider(s)? How much of the opposing case must I concede? Where do we draw the line? What's our fallback? How many different ways can the other side try to surprise us?

Grand questions of strategy are important. Talk the case through with other lawyers as well as with your clients, and then do it again. These discussions are essential. Your gut feeling that persuaded you to take the case ought to stay solid, but your tactics and strategy must constantly evolve. Who testifies and in what order? Which witness introduces what evidence? These decisions are always reviewable. The fittest survive because they adapt.

Intellectual preparation is not sufficient, for true persuasion must combine logic and emotion. Going to trial is like playing an accordion. Your case is filled with a universe of information, just as the accordion must first be filled with air. Now you place your fingers on the keys and squeeze. Like music, your case must emerge as organized sound.

I like the music analogy. Music we enjoy sticks with us, changes our mood, and influences our behavior. I want my trial to have rhythm and flow, from opening statement (an overture), the presentation of evidence (the lyrics), a dominant theme (the chorus), and of course my closing argument as the grand finale. I want the

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jury to be humming my case on their way home and when they wake up the next day.

Different cases make different music. Cross-examining the defendant in a plaintiff's fraud case might start softly, and then, the big bang. If that same defendant is relying on exculpatory contract language, its witnesses on their direct exams might sound quite folksy, with a chorus built around the no reliance clause.

Your music is your trial theme. Pick it carefully. If you are representing a franchisee or a dealer, don't overplay the violins of sympathy. Chances are, every client made some mistakes. If nothing else, maybe they were too trusting. Outwardly at trial, you seek your opponent's condemnation. Quietly, you are also seeking redemption and possibly forgiveness for your clients.

Now add the visuals. You pick your exhibits wisely from a million documents, from the FDD and the franchise agreement, and all those emails, to the numbers in financial statements. You know your melody, so now you know when to present your evidence in exactly the right sequence.

The importance of visual evidence cannot be overstated. We create charts and summaries to argue from. We pick our colors carefully, edit and re-edit because less is more. We aspire like Spielberg to achieve maximum impact from every visual image, synchronized to our stirring soundtrack. We engage our clients in this process because they know their brand and we want harmony between our exhibits, our client, and our winning theme at trial.

But again, if the paper trail was so darn clear, the case would never have reached trial. Witnesses will have the opportunity to explain the contract language or the smoking gun email with their spoken words at trial. The jury will consider everything including the additional images created by facial expressions and body language.

Victory comes from the music. Done right, cross-examination and closing argument, the highlights of every trial, are especially musical. With a week to go you, take a night off and visit the opera. Your case on trial is the evening's performance. Start singing the case to yourself and your team. Bring your client in on Sunday when the office is quiet and do a ruthless cross-examination, but in a teaching way. Make sure your client likes the music.

Rehearse your questions endlessly, to cover every possible answer, every twist and turn the case might take. Give a hundred different versions of your closing, one for every possible mood in the courtroom at the close of evidence. Do as much preparation as you can out loud, on your feet, and then keep it going in your mind, every waking moment.

Get a good night's sleep. When you enter the courtroom, and you hear the music, you will know that you are ready for trial.

#### Norman M. Leon

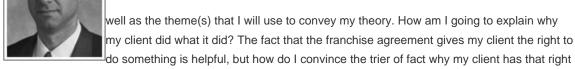
**DLP Piper US LLP** 

"Neither genius nor talent, neither tact nor cunning, can equip an advocate to try a cause as it is the duty of advocates to try causes, without a foundation well laid by thorough and complete preparation."

Byron K. Elliott and William F. Elliott, The Work of the Advocate, at 3 (1888)



It goes without saying that preparation is the key to a successful trial. If you have not completed your preparation, then, as Carmen correctly notes, you are not ready for trial. Once I have studied the documents and interviewed the key players, I work on formulating a theory that accounts for both the strengths and weaknesses of my case, as



and why that right needs to be enforced. In formulating my themes, I try to look at them through my opponent's eyes. I also try to test them against what I believe will be my audience's belief system. The trier of fact—whether it be an arbitrator, a judge, or a jury—will, at some level, want to do "the right thing." It will also want to feel that what you are saying is consistent with its view of the world. It is therefore not enough for your themes to be consistent with the facts and the law. They must, if possible, be consistent with common life experiences and they must appeal to the trier of fact's sense of fairness. For these reasons, I run my theme(s) past just about anyone who will listen, constantly making refinements, as these themes will be the foundation of my arguments and examinations.

When I begin preparing my arguments and examinations, I work on my closing argument first. Doing this helps me refocus on the elements of the claims, what facts needs to be proved (or disproved), what documents are essential to the presentation of my case, and what testimony I would like to have at my fingertips to prove (or disprove) some aspect of the case. It also helps me hone in on what facts are "unimportant" or inconsistent with my theme(s). This not only assists my preparation of a simple, cohesive closing, but helps me avoid over-reaching or over-selling early on in the case.

Once I have outlined my closing, I work on my examinations, determining how much I can establish through my most likeable witnesses, how much I can limit my use of those witnesses who wake me up in the middle of the night, and how much I need to get out of my cross-examinations. When my outlines are complete, I try to run through the examinations as if I were the witness—*i.e.*, if I were on direct, how would I like my testimony to come off, and if I were being crossed, what could I say to be as difficult as humanly possible. Working on directs in this manner allows me to listen to the story as I would want it to come out, and helps me focus on testimony that might be unnecessarily complicated or simply unnecessary. It also helps me recognize where I am likely to have evidentiary issues. Working on crosses in this way helps me anticipate how and where that moment that I dreamed about might go wrong, and allows me to focus my crosses on what I can realistically hope to achieve. Once I feel prepared, I spend as much time as I can preparing my witnesses for both direct and cross (recognizing that this will be an ongoing process as what needs to be said evolves over the course of the hearing or trial).

The last thing I do is work on my opening statement, remembering that nothing should be taken for granted and that, in a relatively short period of time, I need to convey my theme(s), personalize my client, and explain why my client did the right thing. I rehearse my opening repeatedly until it feels natural and I am comfortable with both the words and the delivery. I then try my opening out on my best and most critical mock jury—my wife (who is also a lawyer). If my wife understands and agrees with the actions my client took, my opening is where I want it to be. If I can't convince her that I'm right, I have little chance of convincing a judge, an arbitrator or a group of strangers. Finally, if circumstances permit, I try to find some time in the courtroom where I will be trying the case (I might show up an hour before a motion calendar begins) and practice at least the beginning of my opening.

In a perfect world, I have reached this point of preparation several days before trial begins. In the real world, I usually reach this point late in the day on the day before trial. If I'm actually done early, I like to go into the office in the morning the day before a hearing or trial, go through my checklist of everything I need to bring with me, make sure that my trial notebook is ready, go through my opening once or twice, and take the rest of the day off so that I can pretend to relax. A nice dinner of something that is guaranteed not to cause stomach problems followed by either a football game or a good, mindless action movie on TV is the perfect evening. A trip to the gym in the morning to release any excess energy completes my preparation.

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Vol. 13 No. 2 | Spring 2010

#### **INSIDE THIS EDITION**

Message from the Chair

2010 Nominating Committee Selected

33rd Annual Forum on Franchising

A Tribute to Janet Reyes

Ready For Trial, Your Honor

New Federal Gift Card Regulations to Become Effective on August 22, 2010

Proposed Arbitration Fairness Act Of 2009

Friend or Foe in Franchising?

Books from the Forum on Franchising

#### THE FRANCHISE LAWYER

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Associate Editors



#### New Federal Gift Card Regulations to Become Effective on August 22, 2010

Craig J. Knobbe Nathan J. Cook Ballard Spahr LLP



On May 22, 2009, the Credit Card Accountability Responsibility and Disclosure Act of 2009 ("Credit CARD Act") was signed into law by President Obama. The Credit CARD Act amends the Electronic Fund Transfer Act ("EFT Act") by adding federal regulations applicable to "gift certificates," "store gift cards," and "general-use prepaid cards" (collectively, "Gift Cards"). Specifically, a person is prohibited from imposing expiration dates or dormancy, inactivity or service charges which do not comply with the conditions of the new federal gift card regulations. To implement the new federal gift card

regulations, the Board of Governors of the Federal Reserve System ("Board") announced on March 23, 2010, following a notice and comment period, an amendment to Regulation E and the official staff commentary to Regulation E ("Gift Card Regulations"). Pursuant to the Credit CARD Act, the Gift Card Regulations become effective on August 22, 2010. This article will highlight the important provisions of the Gift Card Regulations to help franchisors and franchisees with gift card programs prepare for the new law.

#### Effect of Gift Card Regulations on State Gift Card Laws

One of the Credit CARD Act amendments to the EFT Act provides that the EFT Act will not preempt state laws which provide greater protection than the Gift Card Regulations. As such, the new federal minimum standard under the Gift Card Regulations for expiration dates and dormancy, inactivity and service charges will be the only regulations in the approximately ten states without gift card regulations. For the remainder of the states, the impact of the Gift Card Regulations will depend on the extent the state law focuses on the required disclosures, the fees that can be charged in a given month and the amount of inactivity required before service fees can be charged.

#### Gift Card Definitions

Under the Gift Card Regulations, a "store gift card" is a card, code or other device issued to a consumer in a specified amount that can be increased or reloaded by the consumer and which can be redeemed for goods and services at a single merchant or an affiliated group of merchants. An "affiliated group of merchants" is two or more affiliated merchants or persons related by common ownership or corporate control which share the same name, mark or logo. For example, the term includes franchisees that are subject to a common set of corporate policies or practices pursuant to their franchise agreements. Unless excluded under the Gift Card Regulations, closed-loop cards are generally considered to be "gift certificates" or "store gift cards."

A "general-use prepaid card" is essentially the same as a "store gift card," except that it can be redeemed for

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goods and services at multiple unaffiliated merchants or used at ATMs. Unless excluded under the Gift Card Regulations, open-loop cards are generally considered to be "general-use prepaid cards." One common example of general-use prepaid cards are "open-loop" cards issued by banks which can be used at any retailer that accepts that card brand (i.e. Visa or MasterCard).

A "gift certificate" is basically a "store gift card," except that a gift certificate's value cannot be increased or reloaded.

#### Dormancy, Inactivity and Service Fee Restrictions and Related Disclosure Requirements

Under the Gift Card Regulations, it is unlawful to impose dormancy, inactivity or service fees on Gift Cards unless three conditions are satisfied. First, there must not be activity on the card or certificate during the one year period before the fee is imposed. As such, if a fee is imposed after a one year period with no activity and the consumer uses the card or certificate the following month, another fee cannot be imposed until another year of inactivity passes. For purposes of this condition, the term "activity" relates to any action by the consumer to use the funds on the card or certificate (i.e. increasing, decreasing or otherwise using the funds). Second, only one dormancy, inactivity or service fee can be imposed in any given calendar month. For example, if such a fee is imposed on February 24th, the next such fee could not be imposed until March 1st at the earliest. Finally, dormancy, inactivity and service fees must be disclosed "clearly and conspicuously" on the card or certificate *and* the issuer or vendor must provide such disclosures to the consumer prior to purchase.

The Gift Card Regulations contain a complex array of disclosure requirements applicable to various settings depending on, for example, whether a consumer purchases an instrument such as a card, code, or device in person or whether a Gift Card is purchased over the telephone. Certain disclosures are required on the face of a card and others can be made on packaging, electronically or orally. Additionally, certain disclosures made on accompanying contract documents do not comply with the clear and conspicuous disclosure requirements.

For purposes of the Gift Card Regulations, "dormancy fees" and "inactivity fees" are fees for the non-use of or inactivity on a Gift Card. "Service fees" are periodic fees for holding or use of a Gift Card and include monthly maintenance fees, transaction fees, reload fees or balance inquiry fees (it does not matter if the fee is waived or only assessed after a certain period of time). Although the Board is clear that "service fees" will be interpreted broadly, service fees do not include certain one time fees such as issuance fees or cash-out fees.

The following is summary of certain important disclosure requirements:

- Dormancy, inactivity and service fees must be visible to the consumer without the need to remove
  packaging or other materials at the time of sale. The amount of such fees, how often fees may be
  assessed, and the fact that fees may be assessed for inactivity must be disclosed prior to purchase,
  regardless of whether a Gift Card is purchased in person, via the internet or by phone.
- A toll-free phone number and web address, if one is maintained, where consumers may obtain fee information or a replacement Gift Card must be disclosed.
- Information regarding whether funds underlying a Gift Card may expire must be disclosed on the Gift Card.
- Electronic disclosures cannot be given through a hyperlink or in a manner where the purchaser can easily bypass the disclosure.
- In situations where oral disclosures are allowed, written or electronic disclosures must still be given on or with the Gift Card.

An issue that has caused confusion regarding disclosures on loyalty, award, and promotions cards, which are generally excluded from coverage under the Gift Card Regulations, is the fact that the substantive restrictions regarding the timing of service fees and expiration dates do not apply; but the terms of any service fees—to the extent such fees exist—must be disclosed in equal prominence and in close proximity to the card

expiration date.

#### **Expiration Date Restrictions**

Gift cards may not be sold or issued unless the expiration date of the underlying funds is at least five years after the date of issuance (for a gift certificate) or five years after the date funds were last loaded (for a store gift card or general use prepaid card). In certain instances, the expiration date for the underlying funds can be different from the printed expiration date on the card (i.e. a consumer could load additional funds on a card with a printed expiration date that is less than five years after the date such funds are loaded). Concerned about the possibility of consumer confusion regarding differences between the expiration date for the Gift Card and the expiration date for the underlying funds, the Board adopted an approach to ensure that consumers will have an adequate period of time to spend Gift Card funds. The Board's approach provides that policies and procedures must be in place to give consumers a reasonable opportunity to purchase a Gift Card with at least five years remaining until the Gift Card expiration date. In the official staff commentary, the Board explains that consumers are deemed to have a reasonable opportunity to purchase a Gift Card with at least five years remaining until the Gift Card expiration date if (i) policies and procedures are in place to prevent the sale of a Gift Card that does not have an expiration date at least five years after the date the Gift Card was sold or initially issued to a consumer; or (ii) a Gift Card is available to consumers to purchase five years and six months before the Gift Card expiration date.

#### **Exclusions**

The Gift Card Regulations exclude certain card products, including an electronic promise, plastic card, or payment code or device that falls into one of the following six categories:

- 1. Cards usable solely for telephone services;
- 2. Reloadable cards not marketed or labeled as a Gift Card;
- 3. Loyalty, award, or promotional gift cards;
- 4. Cards not marketed to the general public;
- 5. Cards issued in paper form only; and
- 6. Cards redeemable solely for admission to events or venues.

For those who wish to claim an exclusion, a careful and thorough review of the Gift Card Regulations is necessary to ensure that appropriate steps are taken to fall within the desired exclusion.

#### Applicability and Potential Impact on Franchisors and Franchisees

The Gift Card Regulations apply to issuers and sellers of Gift Cards. Since franchisors typically establish and control a franchise system's gift card program and franchisees sell Gift Cards to consumers, the Gift Card Regulations likely apply to both franchisors and franchisees. The following is a list of items franchisors and franchisees should consider and be aware of in advance of August 22, 2010 when the Gift Card Regulations become effective:

• Franchisors should carefully evaluate the differences between the Gift Card Regulations and the myriad of state regulations governing Gift Cards because many state regulations provide greater protection to consumers. For instance, many state laws require issuers of unused gift cards (or cards with unused balances) to transfer, or escheat, to the state where the cardholder resides or the issuer is incorporated, any remaining funds after a certain period of time. Although time periods vary, funds typically must be transferred to the state either three or five years following the sale or the last use of the card. Unfortunately, the preemption language in the Gift Card Regulations does not clearly address this issue. Thus, it can be argued that issuers are obligated to transfer unspent funds to certain states after three years while simultaneously maintaining adequate funds to cover the five year expiration period required by the Gift Card Regulations. Because state escheat laws vary, the Board believed that it was not feasible or prudent to make a preemption determination that applied generally to all states. Upon request for a preemption determination with respect to a particular state's

escheat law, the Board will apply the general preemption standards discussed previously to determine whether such a law is inconsistent with the Gift Card Regulations. In such a scenario, the Board's analysis would be published for notice and comment, and, if the Board determined that the state law is preempted, the final determination would be published in the commentary. Franchisors should be prepared to address this potential issue.

- Franchisors should start thinking about additional policies and procedures that may be required for its
  gift card program, and determine whether franchisees will need additional training to ensure
  compliance with the Gift Card Regulations. For example, franchisors should anticipate establishing
  sales and marketing procedures to ensure that cards will not be sold with a stated expiration date that
  does not comply with the Gift Card Regulations.
- Franchisors and franchisees should consider what the actual gift card will look like after the new disclosures are added. Much of the limited space on a standard Gift Card is already occupied by items such as the magnetic strip, a Visa, MasterCard or other logo, state-specific consumer protection disclosures, and the card number. The Gift Card Regulations include many specific requirements on what must be included on the gift card, and how such information can be displayed. As such, franchisors should consult the regulations to get a head start on preparing new Gift Cards which comply with the new regulations.
- If a franchisee sells reloadable cards that are not intended to be marketed as Gift Cards, the franchisee must be careful about how the cards are displayed to the customer to obviate the likelihood of any confusion regarding whether the cards are Gift Cards. For example, such cards should be presented in a display which does not include Gift Cards. Franchisees should also be prepared to answer questions from customers about the new disclosures under the Gift Card Regulations. It is important that franchisees review their Gift Card inventories and take steps to ensure that Gift Cards sold to customers comply with the Gift Card Regulations. Finally, franchisees should anticipate receiving new policies and procedures from franchisors about the Gift Card Regulations and could consider using the new regulations as an opportunity to talk to the franchisor about best practices for selling and marketing Gift Cards to customers.
- The Gift Card Regulations are available online <u>here</u>.

#### Conclusion

The Gift Card Regulations establish a "federal floor" with respect to expiration dates and dormancy, inactivity and service fees. Since state laws that provide greater protection are not preempted by the new federal regulations, establishing and operating a legally compliant gift card program will continue to be a challenging task.

#### **Back to Top**

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Vol. 13 No. 2 | Spring 2010

#### **INSIDE THIS EDITION**

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In February 2009, Representative Henry Johnson (D) of Georgia introduced legislation known as the "Arbitration Fairness Act of 2009" ("AFA") to remedy what he and many others perceive as failings of the Federal Arbitration Act, 9 U.S.C. § 1 et seq. ("FAA"). See H.R. 1020. If passed, the AFA would ban the enforceability of pre-dispute arbitration agreements in franchise, as well as employment and consumer, disputes. See H.R. 1020. In April 2009, Senator Russ Feingold (D) of Wisconsin introduced a similar bill in the Senate, S. 931. The bills were assigned to the Judiciary Committee of the respective houses of Congress and are currently in committee.

The FAA, when passed in 1925, was intended to apply to disputes between commercial entities of generally similar sophistication and bargaining power. However, the AFA proposes a finding that Supreme Court decisions have changed the meaning of the Act so that "it now extends to disputes between parties of greatly disparate economic power." See HB 1020 Congressional Findings at § 2 (1) - (2). See, e.g., 14 Penn Plaza LLC v. Pyett, 129 S. Ct. 1456 (2009) (U.S. Supreme Court held mandatory arbitration provisions in collective bargaining agreements requiring employees to arbitrate age discrimination claims are enforceable).

The AFA would result in amendments to the FAA, including the addition of a new Section as follows: "(b) No pre-dispute arbitration agreement shall be valid or enforceable if it requires arbitration of ... (1) an employment, consumer, or franchise dispute. . . . " See H.R. 1020 at § 2(4)(b)(1). (Emphasis added.) A "predispute arbitration agreement" would mean "any agreement to arbitrate disputes that had not yet arisen at the time of the making of the agreement." See H.R. 1020 at § 1(6). A "franchise dispute" would be defined in the AFA as "... a dispute between a franchisor and a franchisee arising out of or relating to contract or agreement by which:

- 1. a franchisee is granted the right to engage in the business of offering, selling, or distributing goods or services under a marketing plan or system prescribed in substantial part by a franchisor;
- 2. the operation of the franchisee's business pursuant to such plan or system is substantially associated with the franchisor's trademark, service mark, trade name, logotype, advertising or other commercial symbol designating the franchisor or its affiliate; and
- 3. the franchisee is required to pay, directly or indirectly, a franchise fee." See H.R. 1020 at § 1(5).

Sound familiar? This definition is clearly borrowed from The FTC Franchise Rule (Amended), 16 C. F. R. § 436.1.

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The AFA would ban all mandatory arbitration clauses in franchise and ancillary agreements, effectively requiring most disputes between franchisors and franchisees be disposed of in court. Federal law would govern the applicability of the AFA to specific disputes. Thus, any challenge to the validity and enforceability of an agreement to arbitrate would be shifted from the arbitrator to the court. See H.R. 1020 at § 2 (c). Although the AFA is billed as not applying retroactively because it applies only to disputes arising after its effective date, the AFA would apply to all franchise disputes regardless of when the contract at issue was signed. See H.R. 1020 at § (5).

The franchise community should take notice because the proposed amendments are not only gaining momentum in Congress, but have also been endorsed by the North American Securities Administrators Association ("NASAA"), the voluntary association of state securities regulators that oversee franchising on the state level. NASAA has included the passage of the Arbitration Fairness Act as a key component of its <a href="Legislative Agenda">Legislative Agenda</a> for the 111th Congress.

The International Franchise Association ("IFA") naturally opposes the inclusion of franchising in the proposed amendments to the FAA. IFA President, David French, maintains that franchise disputes should not be put in the same category as employment and consumer disputes because "[f]ranchise contracts are business to business agreements, not business to consumer agreements." See Girard, "Mandatory Franchise Dispute Arbitration Under Assault".

As of 2009, IFA research indicated that approximately 45 percent of franchise agreements contain an arbitration clause. *Id.* (blog post by David French, June 2, 2009). With such a substantial number of franchise agreements containing arbitration clauses, proponents of the AFA argue that the franchise relationship requires the same protections afforded to consumers in other transactions. Although the franchise landscape has evolved, resulting in more sophisticated multi-unit franchise operators, the lion's share of franchisees are still mom and pops investing their retirement funds and leveraging most of their personal assets to start their own business. These individuals lack the sophistication and bargaining power originally contemplated by the FAA.

Franchisors have invited new protections by employing more oppressive and fundamentally unfair franchise agreements and then refusing to negotiate reasonable changes. Most franchise agreements have reached the "take it or leave" status of credit card agreements and other contracts of adhesion. See Nagrampa v. Mailcoups, Inc., 469 F.3d 1257, 1281-1286 (9th Cir. 2006). Granted, the regulatory scheme of franchise disclosure does not always make it easy for a franchisor to negotiate the franchise agreement and remain in compliance. The franchise community, however, has always proved adaptable in the face of change.

Proponents of the AFA further claim that arbitrations lack transparency because the decisions are not made public and an arbitrator's decision is not presently subject to substantive review by the courts. See 9 U.S.C. § 11. The grounds for review of an arbitration award governed by the FAA are limited solely to corruption, fraud, forms of misconduct, or an inadequate or incomplete award. 9 U.S.C. § 10. Moreover, in *Hall Street Ass., Inc. v. Mattel, Inc.*, 552 U.S. 576 (2008), the United States Supreme Court held that the grounds for review as specified in the FAA may not be expanded by agreement of the parties. The result may be different, however, in arbitrations conducted under state law. See, e.g., Cable Connection, Inc. v. DIRECTV, Inc., 190 P.3d 586, 599 (Cal. 2008). The FAA further leaves little challenge to arbitrability. See Southland Corp. v. Keating, 465 U.S. 1 (1984); Doctor's Assoc., Inc. v. Casarotto, 513 U.S. 681 (1996).

Arbitration clauses alone in franchise agreements have not precipitated legislators' concerns. Rather, a laundry list of traditional protections granted *every citizen* are being eliminated or otherwise eroded by many of today's franchise agreements—*i.e.*, the right to a jury, consequential and punitive damages, class action status, and contractually reduced limitations of claims.

The sponsors of the AFA, as well as consumer advocates, assert that most consumers and employees have

little or no meaningful option whether to submit their claims to arbitration. They further suggest that private arbitration companies are sometimes under significant pressure to devise systems that favor repeat customers who decide what arbitration service provider to use. See HB 1020 Congressional Findings at § 2 (3), (4). Because there is no meaningful judicial review of arbitrators' decisions and arbitration proceedings are private, critics claim that the development of public law is being thwarted. See HB 1020 Congressional Findings at § 2(5).

As a result of these concerns—the AFA was introduced, which is precisely what happens when we in the industry do not self-regulate. Uncle Sam will make the rules and will not necessarily endeavor to understand the nuances of the relationship.

As presently drafted however, there would be unintended consequences to international transactions and trans-global contracts. The American Bar Association ("ABA"), at its August 2009 annual meeting, moved quickly to take an official position with respect to the use of arbitration in international disputes. In ABA Resolution 114, the ABA proclaimed its opposition to federal or state legislation or regulations that would reduce or discourage the use of international commercial arbitration to resolve disputes involving international business transactions or that would be inconsistent with established international commercial arbitration standards and practice. The ABA also opposes federal or state legislation or regulations that would invalidate pre-dispute agreements to arbitrate international commercial disputes. See ABA Resolution 114.

Some say the AFA, if passed, will lead to the extinction of arbitration, especially since the recent end of consumer debt collection arbitrations. In July 2009, the National Arbitration Forum ("NAF"), the Country's largest administrator of credit card and consumer collections arbitrations, under a settlement with the Minnesota Attorney General, stopped accepting, processing, and administering new consumer arbitrations involving consumer debt, including credit cards, consumer loans, telecommunications, utilities, health care, and consumer leases. On the heels of the NAF settlement in Minnesota, and likely prompted by it, the American Arbitration Association ("AAA") voluntarily ceased administering consumer debt collection arbitrations the same month until major reforms to the process are made to ensure consumer protection. The AAA publicly supports Senator Feingold's revised bill. See Commentary on ADR and Public Policy, "The Chapter 4 Solution," February 10, 2009.

If passed, there can be no doubt that the AFA will materially alter the landscape for resolving franchise disputes. It will lead to increased uncertainty of forum and applicable law. Franchisors may well be forced to litigate in multiple venues. Conflicts over which state's law applies will become more commonplace. Even if franchisors include provisions specifying forum selection and governing law, those provisions may be held unenforceable under some state franchise laws.

At the time a dispute arises, both sides will have to agree to proceed in arbitration or otherwise fall back to traditional litigation. Discovery is certainly much more expansive as well as expensive in court. The time from start to finish in court is generally significantly longer than in arbitration. This paradigm shift will likely give franchisees more leverage to convince franchisors to reach a reasonable settlement or face the uncertainties of a jury trial. See, e.g. *Too Tall, Inc. v. Sara Lee Bakery Group, Inc., Bus.* Franchise Guide (CCH) ¶14,229 (D.N.Mex.,2009), (Sara Lee's motion to strike the distributor's jury demand denied in the face of bilateral jury trial waiver in the agreement).

Franchisors will likely take a more positive view of mediation as an effective outlet to open communications with their franchisees and explore creative solutions to tense situations in the spirit of collegiality.

In our view, instead of focusing on legislative workarounds, the concerns raised in the proposed legislation can and should be addressed by the franchise bar through more evenhanded drafting.

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Vol. 13 No. 2 | Spring 2010

#### **INSIDE THIS EDITION**

Message from the Chair

2010 Nominating Committee Selected

33rd Annual Forum on Franchising

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Ready For Trial, Your Honor

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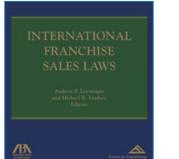
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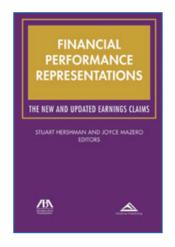
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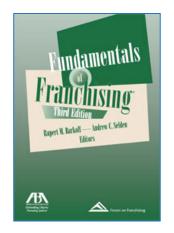
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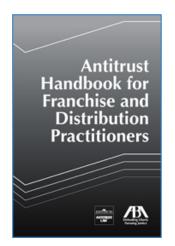
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#### **Back to Top**

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