

**PRACTICAL ASPECTS OF FRANCHISEE REPRESENTATION
ALTERNATIVE DISPUTE RESOLUTION: WHICH METHOD IS
BEST FOR YOUR CLIENT**

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This article explores three alternative methods of dispute resolution: mediation, arbitration, and litigation as applied in the area of franchise law.

The long-term and highly interdependent relationship between franchisors and franchisees is prone to a variety of disputes over the respective parties' rights and obligations. Among the conflicts that arise most commonly between franchisors and franchisees involve disputes over: operational performance, termination, non-renewal, transfer of a franchise, and claims of "encroachment" (charges that a new franchise unit has been permitted to open too close to an existing unit). The nature of the dispute and the extent of damages to be suffered play a significant role in determining which method best addresses a franchisee's needs. Each potential method of dispute resolution has strengths and weaknesses that affect both the franchisor and franchisee.²

**I. IN RECENT YEARS, BOTH LEGAL PRACTITIONERS AND JUDICIAL OFFICIALS
HAVE BEGUN TO RECOGNIZE THAT MEDIATION PLAYS AN IMPORTANT ROLE IN
THE DISPUTE RESOLUTION PROCESS.**

At least two-thirds of the federal trial courts now authorize one or more forms of alternative dispute resolution. The most common form of alternative dispute resolution authorized by the federal courts is mediation. At the present time, more than fifty federal trial courts authorize the use of mediation, with some relying on attorney mediators and magistrate judges.³

Mediation is the process by which the opposing parties come together and attempt to resolve their differences with the assistance of a neutral mediator. This process more closely resembles a negotiation session with an independent negotiator whose agenda is to arrange a

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² As a result of the relatively few Florida cases regarding the issues addressed herein, the author refers to authorities from various jurisdictions.

³ Stienstra, Donna, "ADR in the Federal Trial Courts," *FJC Directions* 4, 6 (December 1994).

compromise.

In the minds of many franchisees, mediation is lumped together with arbitration in the litany of mysterious sounding alternative dispute resolution methods. Although some believe that arbitration and mediation have much in common, the differences between the two are significantly more distinct than their similarities. Unlike mediation, arbitration, in its simplest form, is a judicial proceeding with a private judge and privately sponsored administrators of the proceeding.

In the area of franchise law, mediation is becoming increasingly more prevalent as many franchisees are executing contracts which include mediation provisions. Mediation, non-binding by definition⁴, offers an alternative to dispute resolution whereby both parties seek to resolve a dispute in a less adversarial manner - an essential element when the parties wish to continue their franchise relationship into the future.

A. Cost: The mediation process can be highly cost effective.

Disputing parties may avoid the substantial monetary costs and expense associated with formal adjudications by electing to mediate their disputes. They may simultaneously save valuable time and effort through the avoidance of protracted trial and post-trial proceedings. Although mediation requires some time investment by the parties, the return is evident if a resolution can be reached without having to pursue arbitration or litigation. Judges also benefit from successful mediation. They can use the time and resources they would otherwise have to expend on disputed matters to accomplish other objectives and to expedite the adjudication of those controversies that cannot be mediated between franchisors and franchisees.

One recent example of the cost-effectiveness of mediation involves a dispute between Pizza Hut and one of its franchisees that threatened to destroy a thirty-year old relationship. Through mediation, the parties resolved a three-year old conflict in a single day. Pizza Hut, a founding member of the National Franchise Mediation Program, is one of twenty-five major franchise companies to agree to attempt to mediate all disputes with their franchisees not resolved by direct negotiations. Other program members include Burger King, Dunkin' Donuts, 7-11 Convenience Stores, Jiffy Lube International, and McDonald's, to name a few. The Program has resolved cases ranging from under-reporting of sales to terminations.

B. Applicability to franchise cases: Franchise relationships are well-suited for the efficient and inexpensive solutions which are likely to result from mediation.

⁴ "Non-binding", as it applies to mediation, means that the mediator assists the disputing parties reach an agreement, but has no authority to impose that agreement on the parties. If either party feels the agreement is unjust, they may void the agreement and pursue with other methods of resolving the dispute. The non-binding aspect of mediation makes it much less risky for the parties than arbitration, but also less likely to produce a result.

This is especially true where the parties have typically invested substantial time, effort, and money in becoming business allies and developing a relationship long before they became adversaries. Successful mediation can be anticipated when the franchisee perceives the franchisor to be a valuable asset to the franchisee's business, and the franchisor views the franchisee as a valuable asset to the system.

An additional benefit to mediation is that it may be used effectively at any time to resolve disputes. Obviously, mediation is an option best explored by franchisees before the litigation process. Less optimally, mediation may be considered after the court case is filed, but before extensive discovery is commenced. At that point, the basic issues have been framed, and mediation may be viewed as a mechanism for avoiding the expense of discovery.

Mediation can even be effective if implemented following completion of discovery and prior to trial. At that point, substantially all of the strengths and weaknesses of each party's position are known, and a mediator may step in to help the franchisor and the franchisee reach an agreement based upon the evidence adduced. Finally, mediation can also be considered following receipt of a judgment and prior to appeal. Once again, a mediator can serve to save time, expense, and uncertainty for both sides by suggesting a solution to avoid the further expense and unpredictability of an appeal.

As a preemptive approach, some franchise agreements include multi-step clauses which carry built-in time tables as to when and how disputes are handled. These clauses may, for example, require negotiation as a first step and may permit either party to request mediation or arbitration if negotiation fails to achieve a resolution within thirty days. If another sixty days pass without resolution, the agreement may specify that the dispute will either go to arbitration or litigation.

C. Efficiency: Efficiency considerations must be weighed heavily by a franchisee when participating in the mediation process.

Parties who engage in mediation are never certain that the time and expense will result in a settlement or prove productive. One party can block a mediation by its refusal to negotiate and by its unwillingness to compromise. Therefore, mediation offers the best opportunity to succeed when both franchisor and franchisee have a genuine interest in settlement. Where there is no desire or perceived reason to settle on the part of one or both sides, mediation becomes problematic.

The most common problem existing with mediation is the lack of a decision maker on either side, with the authority and the courage to settle the case. Sometimes franchisors will send people who are authorized to settle the case, but who for internal politics or personal reasons, are ineffective at resolving disputes. Also, mediation can be unproductive if the representatives of the parties are those with a personal stake in the dispute, for example, the regional manager whose exercise of discretion resulted in the dispute. Because most franchisees are involved in small businesses, it is more difficult to get the franchisee to send someone without a direct personal role

in the dispute being mediated. It is important, therefore, for franchisee counsel to advise their clients to separate their emotional role in the dispute and to view the mediation process more dispassionately and objectively than they would otherwise be inclined to.

D. Discovery: In mediation, discovery is a voluntary process which a mediator has no power to enforce.

A mediator can suggest that parties make certain information available to each other, but a mediator cannot compel disclosure. Therefore, to the extent discovery is necessary before a party is willing to engage in settlement discussions, mediation does not provide an enforceable mechanism to require parties to exchange information with one another.

However, in place of discovery, mediation does provide an opportunity for the dissemination of information either through private meetings with the mediator or through joint sessions between the two parties. The private meetings are conducted solely with the mediator. Information transmitted to the mediator during these private meetings is kept confidential by the mediator, unless permission to disclose is otherwise given. Therefore, a party can safely disclose to the mediator information that it would not ordinarily disclose to the other side at an early stage in the negotiation process. This process allows the mediator to assess the information provided, maintain confidentiality, and possibly return with a proposed settlement to the dispute.

Joint sessions, on the other hand, provide for a voluntary discovery process between the parties. During joint sessions, both parties are encouraged to discuss the merits of their respective position. These disclosures, however, create risks, because whereas the disclosures themselves were made during settlement negotiations and may be confidential, the information revealed may be, at some later date, used to a party's detriment if the negotiations fail. One risk involved in disclosing information during this stage is that a party may use the mediation process as a means of informal discovery, without engaging in serious settlement negotiations. When one party has no intention of seeking a resolution, the mediation process can be undermined. Therefore, a franchisee engaged in mediation must be careful in assessing the risks of disclosing information during a joint session in order to accomplish a better settlement.

The kind of evidence and factual information an attorney will want to reveal during the mediation will, of course, depend on the nature of the dispute. As a litigation tactic, it may not be wise to reveal your "ace in the hole" or your "silver bullet." Further, it is important that nothing be revealed that will assist a non-party to the mediation with whom a client may have a future adversarial interest. This is of particular concern to franchisors who may have other franchisees in the system who are not content.

In deciding what information to disclose during settlement negotiations, one must keep in mind the potential admissibility of statements made by the parties as evidence, if mediation does not cure the dispute and litigation ensues. Since mediation is a form of settlement negotiations, Rule 408 of the Federal Rules of Evidence (or its applicable Florida counterpart, 90.408 of the Florida Evidence Code) applies and makes most of the parties' conduct and statements inadmissible as evidence. This Rule, provides:

Evidence of (1) furnishing or offering or promising to furnish, or (2) accepting or offering or promising to accept, a valuable consideration in compromising or attempting to compromise a claim which was disputed as to either validity or amount, is not admissible to prove liability for or invalidity of the claim or its amount. Evidence of conduct or statement made in compromise negotiations is likewise not admissible. *This rule does not require the exclusion of any evidence otherwise discoverable merely because it is presented in the course of compromise negotiations. This rule also does not require exclusion when the evidence is offered for another purpose, such as proving bias or prejudice of a witness, negating a contention of undue delay, or proving an effort to obstruct a criminal investigation or prosecution.*

Fed.R.Evid 408 [emphasis added]

In explaining the significance of this Rule, it is especially important to remind franchisees that the purpose of this rule is to make “evidence of settlement or attempted settlement of a disputed claim inadmissible when offered as an admission of liability or the amount of liability” and “to encourage settlements which would be discouraged if such evidence were admissible.”⁵ Notwithstanding the protection afforded by Rule 408, attorneys should also inform their clients that statements of fact made during settlement negotiations or the mediation process remain admissible.⁶

At any point throughout the process, the mediator may determine that no settlement is feasible, and thereby avoid the further expenditure of time and effort on settlement. In the event mediation fails, all other options remain open to the parties.

E. Applicability of the Federal Rules of Civil Procedure: The Federal Rules of Civil Procedure are applicable in court-ordered mediation proceedings.

Chapter 44 of the Florida Statutes sets forth the governing principles for court-ordered mediation in this state. Chapter 44 provides that “court-ordered mediation shall be conducted according to the rules of practice and procedure as adopted by the Supreme Court.”⁷ As for

⁵ Fed.R.Evid. 408, Advisory Committee Notes.

⁶ See *U.S. v. Shotwell Mfg. Co.*, C.A.Ill. 1961, 287 F.2d 667(8th Cir. 1961), *affirmed* 83 S.Ct. 448, 371 U.S. 341, 9 L.Ed.2d. 357, *rehearing denied* 83 S.Ct. 931, 372 U.S. 950, 9 L.Ed.2d 975.

⁷ Fla. Stat. 44.102 (1).

voluntary mediation, the parties can, by agreement, choose to follow the Rules of Civil Procedure (Federal or Florida). If the parties choose not to abide by the Rules, the mediator can provide applicable rules upon which the proceedings shall continue.

F. Policy Considerations: The opportunity to avoid the strains of litigation and escalation of expenses and hostility are benefits of mediation that strongly attracts franchisees to this method of dispute resolution.

Successful conciliation efforts can significantly enhance the psychological well-being of disputing parties. Mutually beneficial settlements avoid the anxiety, trauma, and uncertainty associated with contested litigation. Negotiated resolutions also permit litigants to participate directly in the formulation of the final results. Mutually developed solutions are generally preferable to results that are imposed upon interested parties through external judicial determinations. Some proponents of mediation believe that “if the parties make their own agreement they are more likely to abide by it, and it will have greater legitimacy than a solution imposed from without.”⁸

Many find mediation appealing because the process does not focus primarily upon which party is “right” or “wrong” or which side should “win” or “lose,” as do judicial proceedings. It instead considers what the participants need to satisfy their underlying interests. While litigation tends to be a “win-lose” endeavor, conciliation usually involves a “win-win” process.⁹ Parties are more satisfied with and are more likely to honor solutions they help to formulate, and this factor inures to the benefit of everyone concerned.

Recently, industry-wide ADR programs, such as the National Franchise Mediation Program, have created more encouragement for the use of mediation in disputes between parties, particularly between franchisors and franchisees. Under the program, the participating franchisor agrees to mediate any issue arising with a franchisee. The program lends administration to the mediation process in the sense that they provide a roster of expert mediators and mediation rules for the parties. However, once a dispute arises between the parties, the mediation process is generally party-managed. As a result, more than forty major companies (including restaurants and hotels, oil companies, and moving companies) have participated in the program, and it has resolved approximately 150 disputes since its inception in 1993.

In-house programs, such as an ombudsman or franchise liaison office, can also help to resolve disputes early on since the ombudsman or liaison officer essentially serves as a middleman when disputes arise. When a franchisee has a grievance, they can call the ombudsman or liaison

⁸ Menkel-Meadow, Carrie J. “For and Against Settlement: Uses and Abuses of the Mandatory Settlement Conference,” 33 *U.C.L.A. L. R.* 485, 502 (1985).

⁹ Folberg, J. & Taylor, A., *Mediation* (Jossey-Bass 1984).

officer. This staff member will then help to identify the source of the problem, gather relevant data about the dispute, present information to both the franchisee and management and determine how the problem can be resolved. The entire process is handled in-house, however, so the liaison or ombudsman must operate in an objective manner to gain credibility with franchisees even though they are usually funded and compensated by the franchisor. The Southland Corporation which franchises 7-Eleven Convenience stores, Subway Sandwiches & Salads, and McDonald's Corporation are examples of three franchise systems which have set up in-house mediation type programs.

II. ARBITRATION, TRADITIONALLY CONSIDERED AS THE PREFERABLE MEANS OF RESOLVING DISPUTES BECAUSE IT OFFERS PARTIES AN ECONOMICAL, RELIABLE AND EXPEDITIOUS SOLUTION, HAS PLAYED A SIGNIFICANT ROLE IN THE DEVELOPMENT OF FRANCHISE LAW.

Arbitration is a process of dispute resolution in which a neutral third party, known as the arbitrator, renders a decision after a hearing at which both parties in dispute have an opportunity to be heard. Franchise counsel will more than likely become familiar with arbitration, whether or not they ever select it for their client because, unlike other methods of dispute resolution, franchise agreements often require binding arbitration of disputes.¹⁰ Courts usually enforce these arbitration clauses,¹¹ although circumstances exist in which the arbitration provision has been held unenforceable.

A. Cost: The costs involved in arbitration can be as expensive as, or more expensive than, traditional litigation.

If the arbitration is to be conducted pursuant to and under the auspices of the American Arbitration Association, the claimant is required to file initial fees which can amount to several thousands of dollars, depending on the amount of the claim. Another expense that drives up the price of arbitration are the costs associated with private judges or panels of arbitrators. Arbitrator

¹⁰ Arbitration can also be non-binding, although most franchise agreements require that the arbitration be binding on both parties.

¹¹ In 1984, the Supreme Court, under Title IX of the United States Code, established the precedent for mandatory arbitration of franchise disputes pursuant to contractual arbitration clauses. *Southland Corp. v. Keating*, 465 U.S. 1, 104 S.Ct. 852 (1984). Title IX of United States Code, known as the Federal Arbitration Act, establishes federal policy favoring the resolution of disputes through arbitration in those instances where the parties have arranged for such resolution.

fees, especially when a panel is involved, can be the single most costly expense for the parties.¹² In addition, arbitration proceedings are often delayed because the arbitrators are usually practicing professionals in other fields who cannot dedicate their full time to the arbitration. These delays can be extended further when the arbitration is conducted by a panel of private judges, who meet infrequently due to scheduling difficulties.

Another factor that can raise the cost of arbitration is the fact that arbitration may occur in a series of short, incomplete segments and not in long, uninterrupted sessions. There exists constant starting and stopping of proceedings which can cause unanticipated expenses such as gearing up to start the arbitration again, preparing and transporting witnesses, getting witnesses ready to testify and trying to fit them into the choppy schedule, which amounts to more time expended by the attorney and more money spent by the client on attorneys' fees. The pace of the arbitration depends heavily upon the schedules of the arbitrators. In most arbitrations, there is no pressure or incentive pushing the arbitrators to diligent, prompt preparation of their award, reasoned or not. The scheduling and conducting of arbitration hearings is not regulated and there is no available relief to parties who complain about irregularities. Like judges, some arbitrators have been responsible for long delays in issuing awards, have asked for protracted extensions, and have delayed cases without asking the parties for an extension at all.¹³ In addition, as in any dispute resolution process, the disputants must consider their own schedules, expense and the diversion from other activities caused by arbitration, and should recognize that arbitration can be more time consuming for them than traditional court proceedings.

Another cost related issue that merits consideration is the division of costs involved in arbitration proceedings. Franchisee attorneys should address the division of costs and expenses incurred during the arbitration proceeding prior to the commencement of the proceedings. In some arbitration provisions, costs are spelled out with specificity. Those clauses include definitions for arbitrator fees, the AAA's administrative fee, the costs of stenographic records, and all other expenses of the arbitration (which could include such things as travel expenses of the parties, expert witness fees and other costs that would not normally be covered in a court's judgment).

Many arbitration clauses explicitly state that all costs will be divided evenly. However, in other cases, the arbitrator is given the discretion to assess all of the costs against one party or the other, or to allocate the costs between the parties, or to allow each party to bear his own. There are those agreements which require the arbitrator to assess the costs against the party who does not prevail. Attorneys' fees for the prevailing party are also often included in the arbitration clause

¹² For example, in a highly publicized CERCLA cleanup case, United States v. Stringfellow, a private judge presiding over the hearings billed out over \$1.2 million for his part time work over a period of eight years. "Rented Justice," *The Recorder*, Jul. 19, 1994, at 1.

¹³ Bureau of National Affairs, Daily Labor Reporter. June 4, 1987 "Text, Report of Special Committee on Professionalism of National Academy of Arbitrators Presented at NAA Annual Meeting, New Orleans," May 26-29, 1987 at E-3.

provisions relating to costs.

B. Applicability to franchise cases: Recently, franchise disputes have increasingly been resolved through arbitration.

The arbitration clause, if one exists within the franchise agreement, typically articulates the types of disputes which will be subject to arbitration. As a matter of law, an arbitration clause must have a definitive, certain and sufficient statement of the matters to be submitted to arbitration and must set forth the questions to be resolved in such a manner as to show clearly what disputes are to be arbitrated.¹⁴ No reasonable doubt can exist as to what was intended to be arbitrated, or arbitration will not be permitted.

Some franchise agreements, however, have arbitration contracts that provide for an extremely broad scope of arbitrability.¹⁵ An arbitration clause that calls for “all matters in dispute between the parties” to be arbitrated has been held sufficiently certain and comprehensive to support arbitration.¹⁶ However, franchise attorneys need to be wary of such “general” arbitration clauses. For example, the arbitration clause in some franchise agreements provide that “all disputes arising from or relating to this agreement shall be resolved by binding arbitration.” This general “catch-all” arbitration clause may actually exclude the arbitration of tort claims, as opposed to contract claims. This obviously becomes significant given the penchant of franchisees to seek tort remedies.¹⁷

In his book, *Business Arbitration - What You Need to Know*, Robert Coulson, a former president of the AAA, notes that the AAA generally recommends the following arbitration clause:

Any controversy or claim arising out of or relating to this contract, or the breach thereof, shall be settled by arbitration in accordance with the Commercial Arbitration Rules of the American Arbitration

¹⁴ See, e.g., *Marlene Indus. Corp. v. Carnac Textiles, Inc.*, 380 N.E.2d 239 (N.Y. 1978) and *Drake v. Stein*, 254 P.2d 613 (Cal. D.C.A. 1953).

¹⁵ If the arbitration clause is overly broad or vague, the courts, not the arbitration panel determines the scope of what is to be arbitrated, unless the parties employ language in their arbitration clause sufficient to give arbitrators the jurisdiction to determine this question See, e.g., *First Options of Chicago, Inc. v. Kaplan*, 115 S.Ct. 1920, ___ U.S. ___ (1995).

¹⁶ *Cracchiolo v. Carlucci*, 157 P.2d 352 (Ariz. 1945).

¹⁷ See, e.g., *Photovest Corp. v. Fotomat Corp.*, 606 F.2d 704 (7th Cir. 1979), *cert. denied*, 445 U.S. 917 (1980), in which an action based upon breach of contract and violation of antitrust law gave rise to punitive damages on the theory of an oppressive, intentional, tortious wrong.

Association, and judgment upon the award rendered may be entered in any court having jurisdiction thereof.¹⁸

However, as the franchise community has become more sophisticated, the arbitration provisions of franchise agreements have correspondingly evolved. Today, it is not uncommon for these provisions to be as much as a full page in length as franchise attorneys try to identify and address the issues which are overlooked by the AAA's suggested language. While Mr. Coulson goes on to note that "arbitration clauses are designed to meet the specific needs of the parties,"¹⁹ he gives little guidance as to what these specific needs may be and how they should be addressed.

Although no standard arbitration clause could effectively address every client's needs or every potential situation, franchise attorneys should make certain that the arbitration clauses their clients agree to (as part of the franchise agreement) at least cover: (1) the parties involved and the relationships they maintain; (2) the number of arbitrators to be selected; (3) the qualifications of the arbitrators; (4) the place of arbitration; (5) the timing of the arbitration, and how much time will be allotted; (6) the method of discovery; (7) the scope of arbitrable matters; (7) other procedural issues such as ancillary relief, limiting the power of arbitrators and circumscribing the awards they may render; (8) the possibility of class arbitrations; (9) costs; (10) confidentiality; (11) the statute of limitations upon which an arbitration may be commenced by a franchisee; and (12) appellate review.

C. Efficiency: Questions of efficiency often undermine the effectiveness of arbitration as an option to resolving disputes.

Even proponents of arbitration recognize its shortcomings in franchise disputes. One of the biggest shortcomings of arbitration is the relief attainable from the arbitrator. As a practical matter, injunctive relief is very difficult to obtain in arbitration. Rule 34 of the American Arbitration Association's Commercial Arbitration Rules authorizes an arbitrator to grant "interim relief" necessary to "safeguard the property that is the subject matter of the arbitration."²⁰ However, that authority is not nearly so broad as a court's authority to issue injunctive relief. Even if an arbitrator decided to issue preliminary injunctive relief, such an "award" has no teeth until it is enforced by court order, which again, is time consuming and no substitute for going to

¹⁸ Coulson, Robert., *Business Arbitration - What You Need to Know*, 17 (4th Ed. 1991). The AAA's Commercial Arbitration Rules contain virtually identical language in its "Standard Arbitration Clause." AAA Rules, at 5 (1993).

¹⁹ Coulson, at 17.

²⁰ The full text of Rule 34, Interim Measures, provides: "The arbitrator may issue such orders for interim relief as may be deemed necessary to safeguard the property that is the subject matter of the arbitration, without prejudice to the right of the parties or to the final determination of the dispute."

court in the first instance. One must keep in mind that arbitration awards are contractual in nature and need the force of law to be effective if a party refuses to obey them.²¹ Therefore, the requirement that interim relief “safeguard” property may, in practice, make interim relief in an AAA proceeding virtually unobtainable in many situations.

Another problem with arbitration is the inordinate delay between the institution of a demand for arbitration and the appointment of arbitrators. Some of the delay is institutional and results from the procedures of the dispute resolution provider relating to the selection of arbitrators (for example, the exchange of lists of potential arbitrators between the franchisor and franchisee and the procedure of accepting appointments). Some of the delay may result from the unresponsiveness of an opposing party and the arbitrator’s lack of authority or inability to coerce a response or effectively sanction a party’s non-compliance with procedure. This process can take months, and by that time, a franchisee truly in need of emergency relief will be out of luck. While the American Arbitration Association has “expedited” rules, these rules only apply to matters involving less than \$50,000 and are no substitute for the fact that a judicial litigant can, on a proper showing, usually get a judge assigned promptly with an early hearing date.²²

A third complaint that many participants in the arbitration process have pertains to the informality attending arbitration hearings, caused by the fact that the panel is not bound by any rules of procedure or evidence, and by the fact that arbitration awards are often unaccompanied by any underlying explanation or reasoned decision.

One of the frequently mentioned benefits of arbitration is that it provides a vehicle for the parties to resolve a dispute before someone who is skilled both in the process of arbitration and is knowledgeable in the field of franchise law. This is not universally true. What the provider believes is sufficient knowledge and what the parties expect can sometimes be quite different. While some arbitration providers offer arbitrators (often lawyers and business persons) who have some knowledge of franchise law, in the usual case, the special expertise of an arbitrator is not in franchise law nor in the types of issues in dispute before them. Many arbitrators have specific skills necessary to effectively arbitrate a dispute, but may still require being educated as to modern areas of franchise law.

D. Discovery: The Federal Arbitration Act provides no discovery mechanism.

Proponents of arbitration claim that discovery in arbitration is faster, less formal and less expensive. However, none of these characteristics would exist were it not for the fact that there is no inherent ability to conduct pre-hearing discovery in the arbitration arena. Many franchisees are particularly susceptible to the notion that taking part in arbitration will save them discovery

²¹ See 9 U.S.C.A. §2; see also *United Steel Workers v. Enterprises Corp.*, 363 U.S. 593, 597, 80 S.Ct. 1358, 4 L.Ed. 1424 (1968).

²² See, AAA Commercial Arbitration Rules 53-57.

expenses. However, few arbitration clauses within franchise agreements address discovery issues in any respect. Therefore, there are few rules and attempting to save money on discovery may in fact be a poor choice for franchisees when facing the potential cost of an unfavorable arbitration award based upon an uninformed arbitrator.

Few states offer state arbitration laws that deal with discovery issues (for example, California makes discovery mandatory in arbitrations of personal injury claims).²³ Florida is one of those few states that provides for some discovery in both court-ordered, nonbinding arbitration and voluntary, binding arbitration. For example, Florida Statute §44.103 (1) states that court-ordered, nonbinding arbitration “shall be conducted according to the rules of practice and procedure adopted by the Supreme Court.” Fla. Stat. § 44.103 (1). In addition, Florida Statute § 44.103, which deals with specific discovery issues states that,

at the request of any party to the arbitration, such arbitrator shall issue subpoenas for the attendance of witnesses and the production of books, records, documents, and other evidence and may apply to the court for orders compelling such attendance and production. Subpoenas shall be served and shall be enforceable in the manner provided by law.

Fla.Stat. § 44.103(4).²⁴ In addition, Rule 1.820 (c) of the Florida Rules of Civil Procedure, states that,

(c) Rules of Evidence. The hearing shall be conducted informally. Presentation of testimony shall be kept to a minimum, and matters shall be presented to the arbitrator(s) primarily through the statements and arguments of counsel.

Fla.R.Civ.P. 1.820 (c).

E. Applicability of the Federal Rules of Civil Procedure: Arbitrators are not always bound, as a matter of law, to follow the Federal Rules of Civil Procedure and may disregard them and substitute instead their own notions of justice and good conscience unless specifically set forth in the agreement.

²³ Cal. Civ. Proc. Code, §§1283.05 and 1283.1 (West 1982).

²⁴ Florida Statute §44.104, which deals with voluntary binding arbitration, follows similar evidentiary and procedural rules as those found in §44.103, (court-ordered, nonbinding arbitration), with the notable exception of §44.104(9) which states that “The Florida Evidence Code shall apply to all proceedings under this section.” Fla.Stat. §44.104(9). In contrast, there is no Florida law requiring that the Florida Evidence Code be applied to court-ordered, non-binding arbitration proceedings.

Procedural questions surrounding binding arbitration are heavily dependent upon the arbitration clause in the franchise agreement. On the other hand, in Florida, non-binding arbitration has set procedural rules that govern the proceedings.²⁵ Some arbitration clauses permit the arbitrator to grant discovery. If counsel for the parties agree, or if the arbitrator is permitted to and does so order, discovery may take place in a fashion that is similar to that available under federal and state civil procedure rules.²⁶ In addition, evidentiary rules are absent from most arbitrations and are provided for either in the arbitration clause or by agreement of the parties and the arbitrator.

The Center for Public Resources, or CPR, has established its own set of arbitration procedure rules known as the Rules for Non-Administered Arbitration of Business Disputes and Commentary. These Rules, originally published in 1989 and subsequently amended and re-issued, are based on the premise that once an arbitrator or panel is selected, the arbitrator and the parties are sufficiently capable of performing most of the functions generally performed by an administering organization. CPR advocates believe that the parties may be better able to control the conduct of the proceeding than any particular arbitration organization, therefore the Rules are crafted to favor non-administered or ad hoc administration. The main objective of the Rules is to conduct every arbitration proceeding expeditiously and economically. For example, they authorize the arbitrator to establish time limits for each phase of the proceeding and to penalize a party engaging in dilatory tactics.

F. Policy Considerations: Should all commercial disputes arising between contracting parties be privately resolved through arbitration or mediation?

Some disputes may involve questions of public rights or conduct that have traditionally been resolved by the courts. In cases such as these, courts are better suited in considering the private needs of the parties while also keeping in mind the larger policy implications of the areas disputed between the franchisor and franchisee. In a system where disputes are handled solely on

²⁵ See Rule 1.820, Florida Rules of Civil Procedure.

²⁶ For example, Rule 1.830(a)(2) of the Florida Rules of Civil Procedure, which governs the procedural rules of voluntary binding arbitration, states that “subject to these rules and section 44.104, Florida Statutes, the parties may, by written agreement before the hearing, establish the hearing procedures for voluntary binding arbitration. In the absence of such agreement, the court shall establish the hearing procedures.” Fla.R.Civ.P. 1.830(a)(2). In contrast, Rule 1.820(b)(1) of the Florida Rules of Civil Procedure, which sets forth the procedural rules for court-ordered, nonbinding arbitration, does not allow the arbitrator or the parties such broad discretion as to setting the procedural rules and states that “the chief judge of each judicial circuit shall set procedures for determining the time and place of the arbitration hearing and may establish other procedures for the expeditious and orderly operation of the arbitration hearing to the extent such procedures are not in conflict with any rules of the court.” Fla.R.Civ.P. 1.820 (b)(1).

a private basis, such as arbitration, resolution is the only desired end. If the parties are in agreement with the resolution, no further thought is necessary as to the issues involved in the dispute. However, the resolution of some disputes between franchisors and franchisees impacts upon the larger community. In a private dispute resolution, there is usually no benefit to the community of franchisees beyond the fact that the disputants are no longer at odds with one another.

Consider, for example, the consequences if a franchisee's claim for loss suffered because of a franchisor's failure to meet statutory disclosure obligations is handled strictly by an arbitrator. For the franchisor, private resolution is obviously preferred. The private resolution of the franchisee's claim does not expose the franchisor to the risk of additional claims by other franchisees who have received equally deficient treatment. As such, the franchisee community has been deprived of valuable information by the private resolution and of the knowledge that they may have cognizable claims against the franchisor. In addition, as a result of the arbitration of the parties' dispute, there is no public pronouncement of what constitutes acceptable conduct. Therefore, no one benefits other than the parties involved.

III. PRIMARILY BECAUSE OF THE HIGH COSTS INVOLVED AND ITS HEIGHTENED ADVERSARIAL NATURE, LITIGATION IS VIEWED BY MANY FRANCHISORS AND FRANCHISEES AS A VEHICLE OF LAST RESORT IN RESOLVING THEIR DISPUTES.

Litigation is often the most powerful weapon in the resolution of franchise disputes. Franchise disputes usually feature a small businessperson franchisee, doing battle with a larger, better financed franchisor.

A jury trial can be a powerful tool to help level the playing field against the franchisor. The discovery that accompanies litigation is also vital and almost always helpful to the franchisee in proving their case. Since results of litigation are public and have precedential impact, which can be of critical importance in franchising, one franchisee's rights may well be all franchisees' rights. Litigation provides access to preliminary relief such as injunctions, which frequently are of critical consequence in franchise disputes. The availability of other non-monetary relief, such as specific performance and declaratory judgments, and a greater likelihood of receiving punitive damages, when available, are also among the benefits of the traditional jury system of resolving disputes.

A. Cost: The costs associated with litigation has often times dissuaded franchisees from initiating a lawsuit.

While litigation has compelling features, it has many negatives that franchisee counsel should consider. Chief amongst them is cost. Litigation is expensive and often takes much longer to complete than alternative methods of resolving disputes. Plaintiffs, faced with the

reality of walking away from a loss in the courtroom with nothing to show for it, are extremely cautious of filing a lawsuit against franchisors. Most franchisors possess several in-house lawyers and general counsel, investigators, and support staff. There is virtually no limit to what a financially superior franchisor who wants to win may spend in a lawsuit, particularly if (as is often the case) the result of a lawsuit has system-wide implications.

B. **Applicability to franchise cases:** Franchisees often choose litigation as their means to resolve their disputes because of the types of relief obtainable through litigation.

Recent cases have seen franchisors recovering substantial judgments against franchisees for unpaid back royalties and trademark infringement. At the same time, franchisees have been successful in obtaining multi-million dollar, actual and punitive damage awards from franchisors. Substantial recoveries have been made against franchisors under common law for fraud and breach of implied covenant of good faith and fair dealing. Statutory damages are often recovered by franchisees under state deceptive trade practices acts, "little" federal trade commission acts and antitrust laws.

In addition, litigation has been an effective vehicle for obtaining injunctive relief. Traditionally, the grant of a preliminary injunction is an extreme remedy that should not be used unless clearly warranted.²⁷ Most franchise cases involving preliminary injunctions have arisen in one of three contexts: the franchisee's request for a preliminary injunction against termination of the franchise; the franchisor's request for a preliminary injunction against a terminated franchisee's use of the franchisor's trademarks; and the franchisor's request for a preliminary injunction against the franchisee's violation of a covenant not to compete.

Additionally, when litigating a franchise dispute, of notable importance in bringing a lawsuit and obtaining judicial relief is the decision as to where and what court to file the lawsuit. Often, the venue is chosen by the franchise agreement. Sometimes, franchise regulatory laws trump the forum selection clause. At times, the common law serves to trump the clause.²⁸ Franchisees may also be able to file an action in any of several jurisdictions, and the approach of those jurisdictions towards this issue may determine whether or not a helpful franchise statute or other state law is applied at all. Often the franchisee will be able to choose whether to file its claim in state or federal court. Many franchisee practitioners believe that state courts are often more generous with franchisees than federal courts. Of course, the availability of diversity jurisdiction provides the franchisor with the ability in many cases to remove state cases to federal court.

Choice of law and forum remain fertile ground for litigation, partly because conflicts

²⁷ *Fox Valley Harvestore, Inv. v. A.O. Smith Harvestore Products, Inc.*, 545 F.2d 1096 (7th Cir. 1976).

²⁸ See *Jacobson v. Mail Boxes Etc. U.S.A., Inc.*, 419 Mass. 572, 646 N.E.2d 741 (1995).

among the courts persist. The difference between the statutory protection offered to franchisees among the various states is profound and, therefore, so is the issue of what state's laws apply. In Arkansas, for instance, one court decided that even though both the franchisor's home state and the franchisee's home state had franchise laws regulating franchises located in those states, neither states' franchise law was available to protect the franchisee.²⁹

C. Efficiency: Litigation often provides for efficient resolution of disputes.

In terms of efficiency, litigation has definite benefits over ADR. Among them are the right to discovery, the presence of a jury, the precedential effect of a judicial decision and the potential for effective injunctive relief and other non-monetary relief.³⁰ Further, the use of rules to govern evidence and procedure also helps promote efficiency. Other benefits of litigation that assist in expediting a case are the presence of a record (thereby reducing the possibility that a witness will give conflicting testimony on separate occasions), and the availability of judicial review.

D. Discovery: Discovery in franchise litigation offers procedural safeguards for both parties and, often times, significant costs and burdens.

For a franchisee, discovery is often viewed as time-consuming and expensive, particularly due to depositions, interrogatories and document production. Thus, many franchisees opt for some other form of ADR in order to avoid discovery. However, what many franchisees do not understand is that some of these arbitration hearings or mediation proceedings play out in bizarre fashion whereby neither party knows of the other side's witnesses or what they will say; what documents the other side will introduce to rebut the plaintiff's case; what expert witnesses will be testifying and what they will say; and what evidence the client should have brought to the hearing to rebut the other party's evidence, but did not bring since it did not know just what the other side would be introducing. After all, there is a reason why the concept of trial has been formulated over a number of years, whereby neither party is surprised at the other party's evidence but, instead can come to court anticipating such evidence and be prepared to rebut it.

E. Applicability of the Federal Rules of Civil Procedure: Precedent from recent cases illustrates that established federal and state law continues to be viable in determining the outcome of franchise disputes.

In franchise litigation, the parties explicitly or implicitly focus on the contents of the written franchise agreement. From the franchisor's perspective, the franchise relationship is a commercial arrangement between business persons that is grounded in the writing. Thus,

²⁹ *JRT, Inc. v. TCBY Systems, Inc.*, Bus. Fran. Guide (CCH) ¶ 10,751 (E.D. Ark. 1994).

³⁰ See *Natl Bulk Carriers, Inc. v. Princess Mgmt. Co.*, 597 F.2d 819 (2d Cir. 1979) (franchise agreements often limit the availability of certain types of relief, including punitive damages and specific performance).

procedural and substantive rules under the Federal Rules applicable to common contract claims are equally applicable to franchise disputes. Areas such as the parol evidence rule, collateral estoppel, and res judicata are examples of applicable legal doctrine in this area and continue to grow in importance in franchise law. Although there may be some distinguishable characteristics involved in franchise contracts, and although the agreement may confer discretion on one or both parties, the parties' duties essentially spring from a consensual agreement that allocates risks and rewards. As such, franchise disputes resolved through litigation fall under the ambit of the Federal Rules of Civil Procedure.

F. Policy Considerations: In choosing litigation, a franchise attorney must be sure his client's claims can make it to trial.

While litigation has several compelling features, it also has some negative aspects that franchise counsel should consider. Before proceeding with a client's case, counsel must consider the enduring effect that litigation may have on the parties. As noted above, a franchise attorney must determine whether it is in their client's best interest, especially if they hope to continue in the franchise relationship in the future, to pursue the highly adversarial option of litigation or if other ADR techniques should be employed in order to maintain a more amicable relationship with the franchisor.

Another crucial aspect of litigation is dispositive motion practice. The franchisor's most powerful tool in many cases is the summary judgment motion. Such a motion presents the franchisor with the ability to argue to a judge that the franchise agreement means what it says, thus disposing of your client's entire case.

Perhaps the most difficult battle in franchise litigation is getting your case to a jury. Therefore, one important consideration in deciding whether to litigate or to pursue other available dispute resolution mechanisms is whether you are able to get your client's principal claims to trial. The current case reports in the CCH Business Franchise Guide or any other franchise case reporter, will show the frequency with which franchisees, despite superior representation, lose claims on summary judgment or other dispositive motions. Therefore, if you are not sure you know the area well enough to provide your client with the best chance to survive summary judgment, it may be in your client's best interest that you get expert assistance.