New York Law Journal

VOLUME 256—NO. 74 $4.00 WWW.NYLJ.COM MONDAY, OCTOBER 17, 2016 Serving the Bench and Bar Since 1888 An ALM Publication

FRANCHISING

Franchise Case Law Developments: ADA, Antitrust, Statutory Fraud Claim

By **David J. Kaufmann**

A number of judicial decisions were promulgated over the past year (two involving cases of first impression) clarifying and addressing: the rights and responsibilities of franchisees under the Americans with Disabilities Act; the antitrust implications of a franchisor heeding a franchisee's request that another franchise not be renewed; and how a New York Franchise Act statutory fraud claim must be addressed.

Let us examine each in detail.

ADA and Renovations

In what it described as an entirely "unsettled legal question," the U.S. District Court for the Southern District of New York, in *De La Rosa v. Lewis Foods of 42nd Street LLC*,[1] held that the plain language of the Americans with Disabilities Act (ADA)[2] leads to the conclusion that a current franchisee is not liable for its predecessor tenant's failure to make alterations of the franchise premises in accordance with the specifications of the ADA.

In *De La Rosa*, plaintiff—whom the court noted was a "frequent filer in this district"—complained that defendant's Times Square-based franchised McDonald's restaurant violated the ADA in that a prior tenant's alteration of the premises, which created a second-floor mezzanine accessible only via a stairway and not accessible to the disabled, rendered the current tenant (the franchisee) liable for ADA violations. Rejecting that contention, the court held:

> While the Court is sympathetic with De La Rosa's position—after all, at least for the purposes of evaluating this motion, De La Rosa is a victim of discrimination at the Times Square McDonald's—the Court is also constrained by text of the remedial scheme that Congress crafted [in the ADA]... [U]nder the statute that Congress passed, the broad requirement that a place of public accommodation must eliminate barriers to access irrespective of costs applies only when that entity played a role in the creation (or alteration without remediation) of the facility with the access barrier (or assumed the liability from an entity that did). In this case, the (current McDonald's franchisee) did not play a role in the non-compliant renovation of the McDonald's; accordingly, it cannot be held liable by virtue of its role as the current "operator" of the premises.[3]

> Can a franchisor, at the instigation of one of its franchisees, determine not to renew another franchisee's franchise without violating antitrust law prohibitions?

The court also rejected plaintiff De La Rosa's further contention that, since the McDonald's Franchise Agreement required the defendant franchisee to comply with all laws, that contractual provision alone engendered ADA liability. Held the court:

> If the Franchise Agreement provided that (the current franchisee) assumed the McDonald's USA, LLC's liability for any prior failures to comply with the ADA, and if McDonald's USA, LLC was the entity responsible for the renovation that is non-compliant, and if De La Rosa had standing to sue under the contract, then (the current franchisee) might be liable for the non-compliant alteration made by its predecessor. But language requiring [the current franchisee] to comply with federal laws and regulations moving forward does not render [the current franchisee] liable for a violation of the ADA that occurred at the time of the noncomplying renovation, well before its involvement at the premises... The Franchise Agreement does not confer liability for already-completed alterations that fail to comply with the ADA; accordingly, it does not provide a basis for De La Rosa's cause of action against (the current McDonald's franchisee).[4]

The court also observed that plaintiff De La Rosa's claim under the ADA would likely be barred by the statute of limitations in any event.

Antitrust

Can a franchisor, at the instigation of one of its franchisees, determine not to renew another franchisee's franchise without violating antitrust law prohibitions? Yes, held the U.S. Court of Appeals for the Second Circuit in *Planetarium Travel v. Altour International*.[5]

In *Planetarium*, Planetarium Travel was a franchisee of American Express Travel Related Services Company, Inc. (Amex) and alleged that another franchisee (Altour) induced Amex not to renew Planetarium's franchise agreement. Planetarium claimed that this conduct violated antitrust edicts as an illegal vertical restraint (that is, a restraint imposed by agreement between entities at different levels of distribution).

Observing that vertical restraints are generally subject to a "rule of reason" analysis (and are not per se illegal), the court held that plaintiff Planetarium failed to surmount the necessary rule of reason hurdles. Specifically, the court held that plaintiff Planetarium failed to allege any actual adverse effect on competition in the sale of first class and business class airline tickets. Nor, observed the court, did Planetari- » Page 7

DAVID J. KAUFMANN *is senior partner of Kaufmann Gildin & Robbins and wrote the New York Franchise Act while he was Special Deputy Attorney General of New York.*

«Continued from page 3»

um allege that Altour had sufficient market power to adversely affect competition.

Accordingly, the court held that the District Court correctly ruled that Planetarium did not plausibly allege a violation of antitrust laws and accordingly affirmed the lower court's decision.

Pleading Statutory Fraud

Answering a question not before addressed, the U.S. District Court for the District of Connecticut—construing a New York Franchise Act case—held that in order to state a claim of statutory fraud under Section 687 of the New York Franchise Act, a plaintiff must comply with the pleading requirements of Rule 9(b) of the Federal Rules of Civil Procedure (FRCP).

In *Family Wireless #1 LLC v. Automotive Technologies*,[6] 39 franchisees commenced an action against their common franchisor (a licensee of Verizon Wireless) alleging, inter alia, violations of the New York Franchise Act. Defendant moved to dismiss so much of plaintiff's Amended Complaint as alleged a violation of the New York Franchise Act's antifraud provisions (Section 687 of the Act) on the grounds that the pleading did not meet the "particularity" requirements of FRCP Rule 9(b).

The court observed that: "It has not been squarely decided by the Second Circuit...that the Franchise Act—and particularly those provisions under which the [plaintiffs] have sued—actually requires compliance with the Rule." However, in a ruling of first impression, the court concluded that Section 687 of the New York Franchise Act does, indeed, require compliance with FRCP Rule 9(b). The court reasoned that since "...Section 687 [of the act] prohibits "fraudulent" conduct, and a claim thereunder sounds in fraud...it is therefore necessary for the [plaintiffs] to comply with Rule 9(b) by stating clearly which FDDs [Franchise Disclosure Documents] were provided to each of them, and when they were provided in relation to the execution of the franchise agreements allegedly in reliance on the fraudulent FDDs."

Accordingly, defendant's motion to dismiss the New York Franchise Act fraud cause of action was granted—but it was granted without prejudice, affording plaintiffs the opportunity to replead their claim. The court sought to instruct plaintiffs what to do next: "...stat[e] clearly which FDDs were provided to each of them, and when they were provided in relation to the execution of the franchise agreements allegedly in reliance on the fraudulent FDDs."

1. 124 F.Supp.3d 290 (S.D.N.Y. 2015).
2. 42 U.S.C. §12183(a).
3. Id. at 298.
4. Id. at 299.
5. 622 Fed.Appx. 40 (2d Cir. 2015).
6. 2016 WL 183475 (No. 15-CV-1310) (D.Ct. Jan. 14, 2016) (not reported in F.Supp.3d).