Armstrong Teasdale | **Client Alert**

June 14, 2010

Awuah v. Coverall North America:
Is The Franchising Model At Risk?

A federal court in Massachusetts made national headlines when it compared franchising with a "modified Ponzi scheme." Recent developments (including a subsequent judicial decision and jury verdict) in the case, *Awuah, et al. v. Coverall North America, Inc.*, have shed further light on the potentially problematic ruling.

Interpreting the Massachusetts Independent Contractor Act (M.G.L. c. 149 § 148B), the court initially found that a franchisor (Coverall) of a janitorial business incorrectly classified its Massachusetts franchisees as independent contractors instead of employees. It ruled that Coverall was unable to establish each of the elements of the Act's three-prong test and prove that:

    (1) The contractor is free from control and direction in connection with the performance of a service.

    (2) The contractor performs a service that is outside the usual course of the employer's business.

    (3) The contractor is customarily engaged in an independently established trade or profession.

In reviewing the relationship between Coverall and its franchisees, the court focused on the second prong of the test. Determining that Coverall did not produce sufficient evidence to show that the contractors (its franchisees) were performing a service outside of Coverall's usual course of business, the court found that franchising is not a "business" in itself. Instead, the court reasoned that Coverall and its franchisees were in the same business - that of selling janitorial cleaning services to ultimate end users. As a result, the court permitted the franchisee's employment-based claims to proceed to trial.

After the trial began, the court dismissed all claims relating to the plaintiffs' assertion that they should be classified as employees. The court based its ruling on the plaintiffs' failure to present proof that they suffered any damages as a result of the alleged misclassification. Plaintiffs' remaining claims of fraud, negligent misrepresentation, breach of contract, and violation of state deceptive practice acts then proceeded to trial, where the jury found against the plaintiffs and in favor of Coverall.

Although the end result was a positive one for Coverall, the court's initial ruling puts at risk many of the fundamental assumptions governing the franchise relationship. Of particular concern is that the court rejected Coverall's argument that "franchising," i.e. the development of a system using a trademark, licensing a system, and training franchisees how to operate a business according to the system, is a business that is separate and distinct from the business of franchisees. Many states have tests similar to the one in Massachusetts to distinguish an independent contractor relationship from the employer-employee relationship.

Franchisors concerned about the possibility of being deemed "employers" should learn from *Awuah* and carefully review their franchise documents for provisions that may put their status as an independent contractor at risk. Armstrong Teasdale's attorneys can assist franchisors in reviewing and analyzing their franchise documents to identify potential areas of concern. If you would like to discuss the potential application of the *Awuah* decision and reasoning to your franchise, please contact one of the following members of the Franchising, Antitrust, and Distribution practice group:

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