



June 29, 2011

Hon. Linda Dorcena Forry, House Chair
Joint Committee on Community Development and Small Business
State House, Room 26
Boston, MA 02133

RE: House Bill 3513

Dear Chairwoman Dorcena Forry,

On behalf of the International Franchise Association (IFA), I would like to thank you for the opportunity to offer testimony in support of House Bill 3515, *An Act Relative to Clarifying Franchises*.

As the largest and oldest franchising trade group, the IFA's mission is to safeguard the business environment for franchising worldwide. The IFA represents over 90 different industries, including more than 11,000 franchisee, 1,100 franchisor, and 575 supplier members nationwide. According to a study conducted by PwC, there are over 825,000 franchised establishments in the U.S. that are responsible for creating nearly 18 million direct and indirect American jobs and generating \$2.1 trillion in economic output. This accounts for approximately 12% of the nation's private jobs and 10% of the GDP. In the Commonwealth of Massachusetts, there are over 13,500 franchise establishments employing over 149,000 individuals and generating \$15 billion in economic output annually.

In an effort to ensure that all companies are properly adhering to Massachusetts' labor laws, the state uses a three-pronged "ABC Test" to assess whether an employment relationship exists between business entities. The ABC Test evaluates whether the individual is free from control and direction; whether the individual's service is performed outside the usual course of business of the entity for which the service is performed; and whether the individual can conduct the business independently of the other entity. Massachusetts' statute assumes an employment relationship unless all three prongs of the test are met.

The problem from a franchising perspective – and the reason for this legislation – is that, while a rational person would think otherwise, an argument can be made that a franchise system fails all three prongs of Massachusetts' ABC Test. While prong (a) requires the individual to be free from control, both under the parties' agreement and in fact, under federal law, a franchisor *must* maintain certain controls over the use of its brand, marks and system, or risk losing trademark rights. In many cases, these are the very things that make a franchise system appealing to a prospective franchisee. Prong (b), on the other hand, requires the individual to offer a service outside the *usual course of business* of the franchisor. While Doctor's Associates Inc, the franchisor of Subway, for example, is engaged in the business of selling a business model that allows local small business owners to successfully sell sandwiches, some may also argue that Doctor's Associates in, in fact, in the business of selling sandwiches – the same business as their franchisees. To complicate matters, within many franchise systems, such as McDonald's, there may be a blend of both corporately owned and franchised outlets, which significantly blurs the line as to what is each company's "usual course of business." Finally,

with respect to prong (c), which evaluates the individual's ability to conduct their business separately from the other entity, the termination of a franchise relationship in many instances would effectively mean the termination of that individual's ability to continue conducting the same business. For example, were a Burger King franchisee to be terminated, they would no longer be able to use Burger King's trademarks, its operating system, or its trade dress. Furthermore, post-termination non-competition covenants are ubiquitous in franchise agreements, meaning a franchisee cannot continue in the same line of business when its franchise agreement ends. In these respects, a franchisee is necessarily dependent on its franchisor for the continuation of the services it provides.

Despite being a well-established business model in Massachusetts, with homegrown companies such as Dunkin Donuts, Friendly's, and Fantastic Sams using franchising as a means to expand their brands all across the country, the ABC Test simply does not account for the symbiotic relationship that is at the heart of franchising. This incongruence between Massachusetts General Law and the day-to-day practices of franchise systems in the state creates an uncertainty amongst the franchising community.

To be clear, this legislation does not absolve employers from adhering to Massachusetts law. Franchisees will still be responsible for all appropriate obligations to their employees, just as any franchisors located in Massachusetts will be responsible for their respective employees. This legislation only makes clear that the relationship between the franchisor and franchisee is not one of employer and employee.

Becoming a franchisee is an entrepreneurial choice. It is a decision *not* to be someone's employee, but rather to be one's own boss (and the boss of those whom the franchisee may choose to employ). Treating franchisees as employees likely will have one of two consequences, neither of which is good for the franchisee. If held to be the "employer" of its franchisee, some franchisors will seek to impose the resulting costs on the franchisee, since they are properly the costs of operating the *franchisee's* business. A franchisee that already is paying such costs for his or her own benefit will thus face double the costs he or she otherwise would. Other franchisors will simply stop selling franchises in a jurisdiction that finds them to be "employers," go elsewhere, and thereby reduce the opportunities for those entrepreneurs left behind. Either result fails to promote the objectives of the state's regulation of employment, workers compensation insurance, and unemployment insurance.

Extending "employment" regulations to the franchisor/franchisee relationship punishes those who want to be entrepreneurs. Franchisees and other small-business owners are the engines of the American economy. Regulations that force franchisees to be treated as "employees" while they act as their own boss will serve only to deprive the economy of the entrepreneurial drive and talent of franchisees, and thereby hinder economic growth.

Thank you in advance for your consideration of this testimony. If I can provide any additional information that would aid in the Committee's consideration of this legislation, please do not hesitate to contact me.

Sincerely,



Judith Thorman

Senior Vice-President, Government Affairs and Public Policy