



2023 LEGAL SYMPOSIUM

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Pros and Pitfalls of Legal Collaboration between Franchisees and Franchisors

Collaboration Between Franchisor and Franchisee Counsel in Franchising

- Collaboration between franchisor and franchisee counsel (or unrepresented franchisees) is common in franchising
 - Assists with the development of the brand
 - Cutting-edge initiatives tested
 - Experience gained in other markets
 - Leveraging bargaining power
 - Common goals/interests
 - Efficiency and cost savings



Collaboration Between Franchisor and Franchisee Counsel in Franchising

The on-going and often amicable relationship between franchisors and franchisees can also create the potential for ethical risks.



Establishing (and Avoiding) the A-C Relationship

- Express – engagement letter
- Implied – rendering legal advice and reliance
- Note-- Presumption that confidential information conveyed to attorney



Unintentional Representation

- Franchise system necessitates direct communication between counsel
- Overarching interest in maintaining brand standards
- TIPS:
 - Distinguish between franchisees legal questions v. business advice
 - Be clear regarding boundaries, while preserving the relationship



Ethical Duties Owed to Nonclients

- Model Rule 4.3
 - Must not state or imply that the lawyer is disinterested when dealing with nonclient and must make reasonable efforts to correct a misunderstanding if nonclient misunderstands lawyer's role in the matter.
 - *Unrepresented Franchisees
- Model Rule 4.1
 - Must not knowingly make a false statement of material fact or law to a third person or fail to disclose a material fact to a third person when disclosure is necessary to avoid assisting a criminal or fraudulent act by a client.
- Model Rule 8.4(c)
 - It is professional misconduct for an attorney to engage in conduct involving dishonesty, fraud, deceit, or misrepresentation.



Scenario

A franchisee has located a buyer for its franchise location and they parties are negotiating an asset purchase agreement. As counsel for franchisor, you send Seller the transfer documentation and the franchise agreement that the buyer will be required to sign.

Buyer's counsel adds additional indemnification provisions to the asset purchase agreement. The Seller reaches out to you to ask you to explain the new terms.



Scenario

New franchisee contacts counsel for franchisor. Franchisee has discovered that in its particular state, it needs a specific license to perform certain optional approved services allowed by the system.

Franchisor's counsel is aware of the license required, where to find the necessary application, and the information needed to apply. The licensing process can be time consuming and expensive, but franchisor's counsel is aware of some ways to expedite the process.



IN SUM/TLDR:

Collaboration between franchisor and franchisee counsel is a crucial and unavoidable component of a successful franchise relationship.

Franchisor counsel should take extra precaution in communications with unrepresented franchisees, as they may be more prone to rely on the advice of the attorney. Such reliance could create an unintentional attorney-client relationship and trigger the attorney's ethical obligations beyond those already owed to third parties under the Model Rules.



Collaboration with Counsel: When?

- Both transactional and litigation events can involve collaboration
 - Pursuing new supplier relationships
 - Testing Pilot Programs
 - Developing into new markets
 - Brand Protection Initiatives/IP Protection
 - Co-Plaintiffs or Co-Defendants in Litigation
 - Can be multiple franchisees or franchisee/franchisor



Dual/Joint Representation: Common Structures

- Both parties' counsel co-represent both clients
- Counsel for one client tenders representation to another party
- The parties jointly hire third-party counsel



Dual/Joint Representation

Pros	Cons
<ul style="list-style-type: none">• United front and ensure cooperation	<ul style="list-style-type: none">• Duty of loyalty owed to all clients
<ul style="list-style-type: none">• Efficiency – joint pleadings, discovery, etc.	<ul style="list-style-type: none">• Interests diverge – claims, settlement, appeal
<ul style="list-style-type: none">• Cost-savings	<ul style="list-style-type: none">• No A-C privilege between jointly represented clients/Revealing confidential information
<ul style="list-style-type: none">• Expertise and long-term contractual relationship	<ul style="list-style-type: none">• Conflicts of interest & voluntary or mandatory withdrawal
	<ul style="list-style-type: none">• Duties owed to former clients (Model Rule 1.9)
	<ul style="list-style-type: none">• Joint employer standard



Maintaining Ethical Duties to Client When Collaborating with Counsel

- Model Rule 1.3 - Duty of Loyalty and Zealous Advocacy
 - A lawyer shall act with reasonable diligence and promptness in representing a client.
 - Comment 1: A lawyer must also act with commitment and dedication to the interests of the client and with zeal in advocacy upon the client's behalf.
- Model Rule 1.6 – Maintaining Confidentiality
 - Except in limited circumstances, attorneys are obligated to maintain confidential information related to client representations and to pursue their clients' interests despite any obstruction or inconvenience



Maintaining Ethical Duties to Client When Collaborating with Counsel: Identifying and Remediating Conflicts of Interest

- Duty of Loyalty Includes Duty to Avoid Conflicts of Interest
- Model Rule 1.7: Concurrent Conflict of Interest
 - Directly adverse or significant risk representation of one or more clients will be materially limited by responsibilities to another client



Maintaining Ethical Duties to Client When Collaborating with Counsel: Identifying and Remediating Conflicts of Interest

At the beginning of the collaborative engagement, counsel for both parties should:

- make it clear to both its client and the other party who each lawyer represents;
- explore the benefits of a collaborative legal strategy with both clients, which may include revealing confidential information to the collaborating attorney;
- consider the potential for conflicts of interests, or instances where the parties' interests might diverge as the matter progresses;
- explain the limits or scope of the collaborative representation and the fee structure; and
- obtain both clients' informed and written consent for the attorneys to collaborate.



Maintaining Ethical Duties to Client When Collaborating with Counsel: Identifying and Remediating Conflicts of Interest

When Conflicts of Interest Arise During Dual Representation

The Model Rules warn that “[u]nforeseeable developments . . . might create conflicts in the midst of a representation” and impair the lawyer’s ability to comply with the duties of loyalty, confidentiality, and independent judgment owed to each client. Model Rule 1.7 Comment 5; Rule 2.1.

The duty of loyalty obligates attorneys to disclose a conflict of interest if one arises and obtain the client’s informed consent before continuing to represent the client. Model Rule 1.7, 1.7 Comment 2.



Remedying Conflicts of Interest

- Model Rule 1.7 Comment 5, 2.1.
 - “If such an occurrence would impair the lawyer’s ability to comply with the duties of loyalty, confidentiality, and independent judgment owed to each client, counsel is ethically obligated to inform the clients immediately and cease concurrent representation.”
- Model Rule 1.7 Comment 4; *See* Model Rule 1.9 Comments 5 and 29.
 - Generally, if a conflict of interest arises “[w]here more than one client is involved, whether the lawyer may continue to represent any of the clients is determined both by the lawyer’s ability to comply with duties owed to the former client and by the lawyer’s ability to represent adequately the remaining client or clients, given the lawyer’s duties to the former client.” Model Rule 1.7 Comment 4; *See* Model Rule 1.9 Comments 5 and 29.”



Confidentiality in Joint Representation Situations

- Counsel must not disclose its client's confidential information without first obtaining the client's consent. Model Rule 1.6.
- Except in limited circumstances, attorneys are obligated to maintain confidential information related to client representations and to pursue their clients' interests despite any obstruction or inconvenience. Model Rule 1.3, 1.6, 1.3 Comment 1.
- There is always a presumption that confidential information has been revealed when two clients are represented concurrently, and but that presumption does not extend to confidential information the lawyer received prior to the inception of the joint representation.
- Practical and long-term considerations regarding revealing certain confidential information may make joint representation less desirable



Best Practices in Joint Representation

- Evaluate likelihood of conflicts prior to engagement
- Obtain informed consent
- Consider issues such as timing and control of litigation up front to avoid them impacting the parties at an inopportune time.
- Establish and document joint defense/common interest privilege early
- If the parties view themselves as competitors (i.e., two or more franchisees), representation may be improper even if the parties have aligned legal interests.
- Make clear who the attorney represents
- Consider the level of risk associated with joint employer issues that is presented by the specific scope of the joint representation.



Dual/Joint Representation

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<ul style="list-style-type: none">• Cost-savings	<ul style="list-style-type: none">• No A-C privilege between jointly represented clients/Revealing confidential information
<ul style="list-style-type: none">• Expertise and long-term contractual relationship	<ul style="list-style-type: none">• Conflicts of interest & voluntary or mandatory withdrawal
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	<ul style="list-style-type: none">• Joint employer standard



Joint Employer Considerations in Deciding Whether to Commence with Joint Representation

- Franchisors should carefully consider which types of litigation it controls or joins on behalf of its franchisees, and how often.
- While the franchisor certainly has an interest in the reputation of the brand, consistency, and uniformity, it must also balance those interests with overstepping into franchisees' employment relationships.



Joint Employer Hypo #1

Franchisor runs a national training facility, where employees of the Franchisee attended a training program. Franchisor's employees travel to New Mexico to assist with the first Franchisee stores' openings in Albuquerque; Franchisor's employees and attorneys offered advice and guidance to the Franchisee over the telephone; and Franchisor distributes manuals prepared by its employees and reviewed by its attorneys detailing operational guidelines.



Joint Employer Hypo #2

Franchisor mandates Franchisee use certain POS and payroll systems. Franchisee implements the required POS and payroll systems with various modifications regarding wage & hour questions for employees to answer at the time they clock out at the end of the day.



Joint Employer Hypo #3

Franchisor has a detailed “Guiding Principles” and “Code of Conduct,” created by their employees and attorneys, that they require all franchisees and franchisee employees to follow. In addition, the Franchisor, through their employees and attorneys, assisted in the construction of a website portal used by applicants for employment with Franchisees. Finally, the Franchisor’s attorney prepared a statement regarding unionization that was made available to all Franchisees to use in their onboarding packet.



IN SUM

Attorneys owe to their clients a duty of loyalty and zealous advocacy, in which they are obligated to act in the client's best interest, maintain confidentiality, and avoid any conflicts of interest. To uphold these duties when working with nonparty counsel, the attorney should always make clear who the attorney represents, explain the limits and scope of the collaborative representation, and obtain the clients' informed consent when appropriate.

Litigation and dispute resolution situations present heightened ethical questions. Clients may seek dual or joint representation in the franchise context when their interests are aligned for the cost and efficiency benefits. However, these situations are ripe for conflicts of interest if the interests of franchisor and franchisee diverge, such as in disputes relating to litigation strategy or settlement offers. Dual representation also presents the possibility that a court will view franchisor and franchisee as joint employers, thus opening the door to potential future liability.

Counsel for both franchisors and franchisees should navigate the relationship carefully, while keeping their ethical duties top of mind. Transparency and boundary-setting is essential for collaborative counselling to benefit both parties and for counsel to maintain its ethical obligations to its clients and non-clients.



Questions?

We Would Love to Keep in Touch!

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