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After Gig Battle, Franchises Are Next Front in Worker Status War

By Erin Mulvaney

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- ABC test could upend franchises, industry warns
- California Supreme Court says 'open question' remains

The franchise industry is mounting an attack on California's rigid worker classification standard, hoping to follow in the footsteps of app-based gig companies that managed to secure a carveout to save their business models.

The test clashes with franchising and puts it at risk, the International Franchise Association has said in an ongoing lawsuit challenging Assembly Bill 5, the law that makes it harder to classify workers as independent contractors instead of employees. Uber Technologies Inc. and Lyft Inc. scored a major victory last November at the ballot box to avoid the law's reach, after their attempts to block the law through litigation didn't gain traction.

The International Franchise Association, along with franchise groups that represent companies including Dunkin' and Supercuts, are banking on a different outcome in court, arguing that the state's "ABC test" shouldn't apply to franchises because federal law governs their businesses. It's an "open question" that the California Supreme Court punted earlier this month in a worker misclassification case against Jan-Pro Franchising International, and could come up again in the decades-old litigation.

"It's a threat to franchising as we know it today," said Justin Klein, an attorney with Marks & Klein who represents franchises across the country. He said whether a franchiser is an employer of individual franchise owners should be a fact-based question and not encompass every type of work agreement. "If the law applies as written, it would be hard for any of them to want to do business in California."

Rising in Other States

Courts in other states are also grappling with the question, teeing up the franchise sector as the next battleground for worker classification litigation, attorneys said.

For example, 7-Eleven Inc. franchisees in Massachusetts are asking the U.S. Court of Appeals for the First Circuit to rule that the state's ABC test applies to franchise relationships. The test is used in other states, including New Jersey and Connecticut.

"There is no doubt that there is still significant uncertainty," said Matthew Haller, the International Franchise Association's senior vice president of government relations and public affairs. "Beyond that, I would just say that this is one of the big reasons we filed our lawsuit last year, to provide certainty about the franchise model's applicability to the ABC test."

The distinction between employees and contractors is key, as only employees are entitled to benefits such as minimum wage, overtime, health care, and workers' compensation.

To classify workers as contractors under the ABC test, companies must show a worker has freedom from control over how to perform the services they provide; that the services are outside the business' normal variety of work; and that the worker is engaged in an independently established role.

Spokespeople for 7-Eleven, Supercuts, and Dunkin Donuts didn't immediately respond to requests for comment on the effect stricter worker classification tests would have on their businesses.

7-Eleven Wins in Court

In Massachusetts, five individual 7-Eleven franchisees hope the First Circuit will overturn a federal judge's ruling that the ABC test doesn't apply to the franchise industry.

U.S. District Judge Nathaniel Gorton, a George H.W. Bush appointee, said there was an "inherent conflict" between the franchise model, a U.S. Federal Trade Commission franchise rule, and the state's ABC test.

The court also said that finding in favor of the individual store owners would "eviscerate the franchise business model."

The franchisees' attorney, Shannon Liss-Riordan of Lichten & Liss-Riordan, said "the sky has not fallen in Massachusetts for franchisers, even though the ABC test has been in effect in its current form since 2004." Liss-Riordan also represents workers in California classification cases.

Liss-Riordan said franchise groups have been making the argument unsuccessfully for years in Massachusetts and Connecticut that the test shouldn't apply to their business model because of federal laws. Judges in those states applied the test to janitorial franchises, including Jani-Kingand Coverall, saying their franchise owners were employees, she said. Coverall stopped operating in Massachusetts after a court ruling in favor of workers.

The U.S. Labor Department also succeeded in bringing a case against Jani-King in the Tenth Circuit, which held that franchisers can be employers of their franchisees under the Fair Labor Standards Act. That federal law relies on a less strict worker classification test with multiple factors.

The National Employment Law Project has argued that misclassification cases against the franchise industry highlight the dangers of that model for low-income workers.

The advocacy group argued that Jan-Pro International, the company at the heart of the recent California high court ruling, "has created a structure that allows it to charge its employees to work as cleaners for Jan-Pro clients, while also avoiding all labor costs that other employers incur, including payroll taxes and insurance premiums." They said this model forces workers into vulnerable and sub-par working conditions.

'Collateral Damage'

Klein, one of the attorneys representing the International Franchise Association in California, said ABC tests could stifle growth in the economy and reduce opportunities for small-business owners.

Even though California's ABC test has been in place since April 2018, the franchise association hasn't cited new litigation that's been filed against franchisers. Courts have used the test in ongoing litigation. Some of those cases resulted in rulings in favor of the franchiser, or were vacated and remanded for consideration on whether the ABC test applied.

"The ABC test is chaotic," said Jonathan Solish, an attorney with Bryan Cave Leighton Paisner, who represents employers. "A franchiser is always in the same business as the franchisee. It doesn't make them an employer."

He represented franchisers in several cases across the country. In California, he said, "We don't know why we have to be collateral damage with Lyft and Uber."

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