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For more information on Dickinson Wright's Franchise and Distribution practice, visit http://www.dickinson-wright.com/practice-areas/franchise-and-distribution. Dickinson Wright is a full service firm with over 300 lawyers and officers in offices in Toronto (Canada), Arizona, Michigan, Nevada, Ohio, Tennessee and Washington DC.

ONTARIO PASSES NEW LEGISLATION GOVERNING TIPS AND GRATUITIES

by Kathy Le

Ontario restaurants, bars and other businesses with employees who receive some of their pay through tips and gratuities will face new laws governing how these tips are collected and distributed to employees beginning this summer. The regulations have yet to be developed, but the new laws will take effect on June 10, 2016.

Under Bill 12, *An Act to Amend the Employment Standards Act, 2000 With Respect to Tips and Other Gratuities* (Bill 12) (passed in December 2015) an employer will be prohibited from withholding, deducting, or collecting tips or other gratuities from an employee unless authorized to do so under the *Employment Standards Act, 2000* (ESA). Bill 12 defines "**tip or other gratuity**" as:

1. a payment voluntarily made to or left for an employee by a customer such that a reasonable person would likely infer that the customer intended that the payment would be kept by the employee or employees;

2. a payment voluntarily made to an employer by a customer such that a reasonable person would likely infer that the customer intended that the payment would be redistributed to an employee or employees;

3. a service charge or similar charge imposed by an employer such that a reasonable person would likely infer that the customer intended that the payment would be redistributed to an employee or employees; and

4. such other payments as may be prescribed.

In other words, if a customer makes a voluntary payment that a reasonable person would likely infer was intended for employees, then the payment will constitute a "tip or other gratuity" under Ontario law, regardless of whether payment is made by the customer to the employee, to the employer, or as part of a service charge levied by the employer.

The method of payment also does not impact whether a payment constitutes a "tip or other gratuity." A voluntary payment made by credit card will constitute a "tip or other gratuity" if a reasonable person would likely infer that the payment was intended for employees. The exemption for charges relating to the method of payment will likely apply only to credit card service charges, and only if such charges are prescribed by regulation.

One exception or authorization is "pooling", under which an employer may withhold, deduct, or collect tips or other gratuities if it redistributes such tips or other gratuities to some or all of its employees. Even this exception, however, has limitations on the employees that can share pooled tips and other gratuities. For instance, an employer, or a director or shareholder of an employer, is prohibited from sharing in tips or other gratuities unless such person regularly performs, to a substantial degree, the same work performed by the employees who share in the redistribution, or employees of a different employer in the same industry who commonly receive or share in tips or other gratuities. In addition, for an employer to share in the pooled tips and gratuities, the employer must also be a sole proprietor or a partner in a partnership.

Other exceptions include authorization through Ontario or federal legislation or by a court order.

Enforcement

If an employer violates any of the prohibitions, the amount withheld, deducted or collected becomes a debt owing to the employee and is enforceable under the ESA as if it were wages owing to the employee.

Collective Agreements

If an employer is party to a collective agreement that is in effect as of June 10, 2016 and includes provisions addressing the treatment of employee tips or other gratuities that conflicts with Bill 12, the provisions of the collective agreement prevail until a new or renewed collective agreement comes into effect. If the collective agreement is made or renewed on or after June 10, 2016, Bill 12 will prevail over the provisions of the collective agreement.

Going Forward

As we continue to monitor this development, employers should review their existing tips and gratuities policies, including any applicable collective agreement provisions.

ONTARIO EMPLOYMENT STANDARDS AUDIT MANUAL NOW AVAILABLE

by Kimberly Asnani

In Ontario, statutory employment standards are established by the *Employment Standards Act, 2000* (ESA) and enforced by the Ministry of Labour (Ministry) through its Employment Standards Program. The Ministry also:

1. provides information and education to employers and employees to aid in compliance;
2. investigates possible violations; and
3. resolves complaints.

Most employees and employers in Ontario are governed by the ESA, with certain exceptions including, among other things, employees and employers in sectors that fall under federal jurisdiction (e.g. airlines, banks, radio etc.). The Ministry has a Special Rule Tool that can be used to determine if a particular industry is governed by the ESA. If an employer's industry is governed by the ESA, then it is important to ensure that such employer is in compliance with the ESA, as the consequences of failing to do so may be harsh.

In some cases, Employment Standard Officers may require an employer, on notice, to conduct a self-audit of their records, practices, or both, to determine whether they are in compliance with the ESA and its regulations. An employer is required to report all self-audit findings to such Employment Standard Officer. A self-audit puts an employer in the position of being an inspector and may ultimately result in the employer having to disclose incriminating evidence to the government.

Franchise clients interested in learning more about the ESA's self-audit provisions should download "The Ontario Employment Standards Act Self-Audit Manual" (Manual), prepared by employment lawyers from Dickinson Wright's Toronto office. The Manual serves as guide to the self-audit process for both Canadian and American employers. The Manual also provides clear information about how to best ensure that an employer company is in compliance with its employer obligations under the ESA and avoid any surprises during the self-audit. For example, the Manual provides practice tips for employers with respect to keeping employee records and summarizes the rules relating to wages, deductions from wages, workable hours, eating periods and breaks, vacation, overtime, minimum wage, and termination.

To receive an electronic copy of the Manual, please contact us.

DUNKIN' DONUTS QUEBEC CASE NOW FINAL

by Ned Levitt

The Quebec Court of Appeal's April 15, 2015 decision is now the last word in a landmark case brought by 21 Dunkin' Donuts Quebec franchisees against their franchisor, Dunkin' Brands Canada Ltd. On March 17, 2016, the Supreme Court of Canada dismissed, without reasons, the franchisor's application for leave to appeal the Quebec Court of Appeal decision. The Court of Appeal had affirmed the lower court's decision, which found for the franchisees and allowed them to terminate their leases and franchise agreements, annulled their releases and awarded them a total of $16,407,143 in damages. The Court of Appeal did, however, allow the franchisor's cross claims for $899,528 and $249,316 and reduced the global damages against the franchisor to $10,908,513.

While it can be argued that this case was decided on some atypical wording in the Dunkin' Donuts franchise agreements, the Court's extremely strong language regarding the implied obligations of franchisors in how they manage their systems, fend off competitors and deal with their franchisees, stands. Such language will no doubt be brought up in future Quebec franchise cases and may, one day, become part of the test regarding franchisor conduct. If that happens in Quebec, or even if it does not happen there, it may happen in the common law provinces in Canada based upon the Quebec Court's analysis.

For more on this case, please refer to our earlier article Dunkin' Donut .

ARE SHAREHOLDERS OF A CORPORATE FRANCHISEE CONSIDERED "FRANCHISEES" UNDER ONTARIO'S FRANCHISE LEGISLATION?

by Andrae Marrocco

The answer is that it depends. The Ontario Superior Court of Justice considered the matter in *2313103 Ontario Inc. et al v JM Food Services Ltd. et al.* in the context of whether the shareholders of the corporate franchisee can invoke the statutory rights afforded to franchisees under the *Arthur Wishart Act (Franchise Disclosure)*, 2000 (Ontario) ("**Act**").

The Court ruled that unless the shareholders of the corporate franchisee can produce evidence to justify that they were treated as one entity for the purposes of franchise obligations, or that the franchise was "granted" to them, then they have no direct rights and remedies, and are restricted to those found in corporate legislation (ie as shareholders of a corporate entity).

The brief facts of the case are as follows: Three individuals (the aggrieved parties) incorporated 2313103 Ontario Inc. (together the "**Plaintiffs**"). The corporate Plaintiff and JM Food Services Ltd. ("**Defendant**" and franchisor), as shareholders, equally invested in F.S. Food Services Ontario Inc. ("**FS**") to act as master franchisee of the Defendant and to operate the Defendant's pizza stores in Ontario.

The Defendant's pizza stores did not fare well, and FS shortly thereafter was unable to continue. The three individuals abandoned their operational roles with FS and the Plaintiffs sought, among other things, rescission of the master franchise agreement between FS and the Defendant. The Defendant argued the Plaintiffs lacked standing on the basis that none of the Plaintiffs were "franchisees" (within the meaning of the Act) under the master franchise agreement and that FS was the franchisee.

The Court refused to recognize the Plaintiffs' claim based on a number of findings:

1. the master franchise (the agreement and other documents) was clearly granted to FS as the franchisee;
2. there was no evidence proffered showing that the Plaintiffs had taken on any obligations under the master franchise agreement (ie such as guaranteeing any of the ongoing obligations of FS); and
3. the Plaintiffs failed to demonstrate that the franchise was granted to any one of them in the sense of a sale or disposition, and there was no basis to argue multiple instances of such grant.

Ultimately, the Court found that the Plaintiffs were not "franchisees" within the meaning of the Act. Any claim by the Plaintiffs ought to have been brought as a derivative action under corporate legislation. It was inappropriate to characterize the Plaintiffs as "franchisees" under the Act by virtue of their equity ownership in FS. Such characterization would be akin to creating a new class of "franchisee's associate" under the Act.

Although decided on the circumstances, the above case demonstrates the need to draft a franchise agreement in a manner that makes it clear whether the shareholders of a corporate franchisee are intended to be "franchisees" (and thereby have recourse to the rights under franchise legislation). Additionally, it appears from the reasoning of the case, that if shareholders (of a corporate franchisee) are taking on responsibility and obligations under the agreement, then this will militate in favour of such shareholders potentially being franchisees for the purposes of the Act. Clear drafting can go a long way to protecting franchisors from that presumption.

CHANGE TO MICHIGAN LAW PROVIDES SOME PROTECTION FOR FRANCHISORS

by Paul Fransway

Joint Employer Liability

One of the recent concerns for both franchisors and franchisees in the US has been the uncertainty created by regulatory efforts to have franchisors held liable as a "joint employer" of the employees of their franchisees. Most prominent of these efforts has been the National Labor Relations Board's ("**NLRB**") actions asserting that McDonald's is a joint employer of its franchisees' employees. This concern has arisen because of the change in the 40-year old standard applied by the NLRB for determining when a joint employer relationship exists, including the possibility that a finding of joint employer status can occur even if there is "indirect" control by the franchisor, and even if this possible indirect control is not exercised. Considering that a standardized consumer experience is the primary goal of franchised systems, and that indirect controls are common in franchise operations, the risks to the franchise model are obvious.

The Michigan Legislature Steps In

Michigan has taken steps to limit franchisor exposure by amending its statutes to provide that a franchisee is the sole employer of the workers paid by the franchisee or to whom a franchisee provides a benefit plan unless the franchise agreement provides to the contrary. The amendments to the Michigan Franchise Investment Law (MFIL) were part of six bills passed and signed into law to clarify the status of franchise employees. The bills also modified the definition of the term "employer" in the Michigan Employment Security Act, the Workforce Opportunity Wage Act, the Michigan Occupational Safety & Health Act, and the Payment of Wages and Fringe Benefits Act. These amendments include a provision in the Michigan Worker's Disability Compensation Act excluding joint employer status unless "(t)he franchisee and franchisor share in the determination of or codetermine the matters governing the essential terms and conditions of the employee's employment" and ". . . both directly and immediately control matters relating to the employment relationship, such as hiring, firing, discipline, supervision, and direction." The amendments to the MFIL and the Worker's Compensation Act were effective on March 22, 2016. The effective date for the other statutory changes is May 23, 2016.

Things to do now:

1. Michigan franchisors should consider amending their franchise agreements to clearly provide that the franchisee is the sole employer of the workers that the franchisee pays or to whom they provide benefits to the maximum extent permitted under Michigan law.

2. All franchisors should review their franchise agreements and consider removing any provisions that are unnecessary or that may result in a finding of indirect control over franchisee employees. This is particularly important with respect to the employment relationship or the day to day activities of the franchise employees.

3. Franchisors should also review their operations manuals and documents that they provide to franchisees to remove any "mandatory" compliance language for issues that are not essential to the business model. Franchisors should also avoid directing franchisees or franchise employees or engaging in any course of dealing that could support a finding that the franchisor has "indirect" control over the franchisee's employees.

4. Franchisors should consult legal counsel familiar with the intersection of employment law and franchise operations to assist with document review and protective measures in order to limit liability.

HOW ENFORCEABLE ARE YOUR NON-COMPETITION COVENANTS IN CANADA?

by Andrae Marrocco

Most franchise agreements include a non-competition covenant preventing a franchisee from competing with the franchisor during the term, and in many cases after the term of the agreement. Ontario courts have generally enforced non-competition covenants, acknowledging the potential harm to a franchisor's goodwill, and the integrity of the franchisor's system, in circumstances where non-competition covenants that are reasonable in scope and time are not enforced.

Interestingly, the case of *MEDIchair LP v DME Medequip Inc.* provides an example of circumstances under which an Ontario court will not enforce a non-competition covenant. The Ontario Court of Appeal refused to enforce the non-competition covenant on the grounds that the franchisor had no intention of opening another franchise store in the protected geographic area. The court cautioned that non-competition covenants can serve only to protect "the legitimate interest of the franchisor" and cannot extend beyond that. The typical approach and considerations were not warranted in circumstances where the franchisor did not intend to operate in the relevant region post-termination – and thereby essentially concluding that the franchisor has no legitimate interest to protect.