

PUBLICATION

Franchisee Scores with Florida Franchise Act Claim Against Hockey School Franchisor

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A franchise allows a business to utilize another's business model. A prospective franchisee assumes the franchise offered has a good track record of profitability; ease of duplication; detailed systems, processes and procedures; broad geographic appeal; relative ease of operation; and costs consistent with what is disclosed in the Franchise Disclosure Document (FDD).

The franchise agreement typically contains language that disclaims any promises of profitability to the franchisee, both generally and in the specific circumstances associated with the sales process for the franchise. However, such language may not necessarily protect a franchisor from claims by a Florida franchisee if the franchisee is not successful, and the franchisor has used financial performance representations that were strangers in the FDD.

The case of *Hockey Enterprises, Inc. v. Talafous*¹, concerns a hockey franchise gone awry. The franchisor and an affiliate, Total Hockey Worldwide and Total Hockey Products (collectively, "Total Hockey") entered into an agreement with Hockey Enterprises, Inc. (HEI) to franchise a business concept for operating hockey training facilities. HEI opened its franchise in Florida in December 2008 but, after experiencing an operating loss of more than \$250,000, was closed by February 2010. HEI filed a lawsuit against Total Hockey, as well as Total Hockey's two owners, Dean Talafous and Brian McKinney. HEI's lawsuit claimed fraud, negligent misrepresentation and violation of the Florida Franchise Act by Total Hockey, Talafous and McKinney (collectively, "Defendants").

In its lawsuit, HEI argued that despite disclaimers in the franchise agreement as to any guarantees of profitability, the defendants made promises of franchise profitability to HEI. HEI specifically relied on projection worksheets provided by the defendants, which included a total annual revenue estimate of \$437,000 and an annual profit estimate of \$139,600. HEI claimed that McKinney made representations that the projection worksheet was reflective of other Total Hockey training centers and that HEI's center would be able to meet those numbers. Nevertheless, the projection worksheets contained a disclaimer that it was merely a projection template and that it did not guarantee the results based on the worksheet. HEI also relied on internal emails stating that other Total Hockey facilities were likely closing and might file bankruptcy. HEI argued that because the defendants had provided these projection worksheets and had failed to disclose the financial conditions of these other facilities, the defendants made misrepresentations to HEI.

After discovery, McKinney, who was an engineer and part-owner of Total Hockey, filed a motion for summary judgment as to HEI's claims against him. McKinney claimed that HEI had no evidence that he had committed fraud, made negligent misrepresentations or committed a violation of the Florida Franchise Act. McKinney therefore argued that based on HEI's lack of evidence, its claims against him should be dismissed.

As an initial matter, the court found that, even though the lawsuit was pending in Minnesota, Florida law applied since the franchise agreement contained a choice of law provision. The court agreed that HEI did not provide sufficient evidence of fraud. Specifically, the court found that there was insufficient evidence to establish that Total Hockey was in trouble financially or that McKinney knew of this financial trouble when the franchise was sold to HEI. The court accordingly dismissed HEI's fraud claim against McKinney.

However, the court denied McKinney's motion for summary judgment on the other two claims. For the negligent misrepresentation claim, McKinney argued that the franchise agreement, including the integration/merger clause, disclaimed any guarantees or warranties of profitability. McKinney further pointed to a questionnaire HEI signed at the closing in which HEI indicated that no employee or other person speaking on behalf of Total Hockey had made any statement or promise concerning the total amount of revenue that HEI would receive or the costs involved in the franchise.

The court acknowledged that the provisions in the franchise agreement and the questionnaire filled out by HEI presented evidence that refuted the reasonableness of HEI's reliance on the alleged misrepresentations. Nevertheless, the court found that it was an issue of fact that should be decided by a jury and not decided on a motion for summary judgment. The court also found that the issue of whether McKinney made representations to HEI without knowledge as to their truth or falsity should be submitted to a jury. In particular, the court found that a reasonable jury could find that McKinney, as an engineer and part owner of Total Hockey, had a duty to tell HEI that he did not have sufficient information to comment on Total Hockey's financial status or, at least, that he had a duty not to make statements to HEI concerning probability of success.

HEI's claim for violations of the Florida Franchise Act (the "Act") survived McKinney's motion for summary judgment. The court found that the issues underlying this claim should also be submitted to a jury. First, the court found that although McKinney was not a party to the franchise agreement, he qualified as a "person" doing business in Florida and was subject to the Act.

Second, the court noted that the standard required for showing a violation of the Act was lower than the above-discussed standard for fraud. Unlike fraud, which requires intentional false statement, the Act only requires that the franchisee relied to his detriment on the franchisor's "intentional words or conduct" concerning the profitability of the franchise "which are not in accordance with the facts." Based on this lower standard, the court found that a reasonable jury could find that McKinney, as an engineer and part owner of Total Hockey, was in a position to make representations concerning the financial condition of Total Hockey to HEI. Accordingly, the court found that HEI's claim for violations under the Act should be submitted to a jury.

In summary, the court found that the issue of whether McKinney's representations rise to the level of negligent misrepresentation or a violation of the Florida Franchise Act should be submitted to a jury and should not be disposed of on summary judgment. Notably, the court admonished both parties to settle by this bold dicta:

It continues to be the Court's view that Plaintiff will have a difficult time prevailing in any significant way if this case proceeds to trial. Both parties bear some responsibility for this situation, and it is difficult for the Court to see how a trial would be in the interests of either party versus settlement of the case.

This case provides valuable lessons and cautions to any franchisor selling in Florida, particularly an early stage franchisor without a track record of successful franchise or company store operations. First, franchise agreement disclaimers of warranties or guarantees of profitability of the franchise are not sufficient to fend off claims by an unsuccessful franchisee based on negligent misrepresentation or violations under the Florida Franchise Act. Second, financial performance representations in the form of projections made to a potential franchisee as to profitability or costs of the franchise are a high-risk proposition. Finally, the principals of a franchisor may be held to answer personally for alleged misrepresentations as to the franchise if the franchisor has no basis in fact for the representations, even if they have no personal knowledge of the current status of the franchisor's finances or franchisee financial condition. The principals could wind up in the penalty box for someone else's infraction.

¹ No. 10-2943, 2012 U.S. Dist. LEXIS 3322 (D. Minn. Jan. 10, 2012).

