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News and Views for Your Hospitality and Franchise Business

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New CPSC Crib Standards Will Affect Places of Public Accommodation

On December 15, the Consumer Product Safety Commission (CPSC) approved a final rule establishing new safety standards for full-size and non-full-size cribs. For manufacturers and distributors of such products, the new rules will take effect within six months of publication in the Federal Register. Child care centers, family child care homes and places of public accommodation would be prohibited from using non-complying cribs within 18 months of publication. CPSC staff estimates that there are approximately 43,303 firms providing public accommodation that could be affected by the regulation. Although the agency received numerous comments from child care centers concerning potential difficulties in meeting the new crib standards within the originally proposed six-month deadline, CPSC did not receive any comments from hotels or similar places of public accommodation indicating the need for additional time to obtain complying cribs for such establishments. The rule was published in the Federal Register on December 28, 2010. The final rule can be found at http://edocket.access.gpo.gov/2010/pdf/2010-32178.pdf.

FDA Mulls Enforcement Strategy for National Menu Labeling

John H. Kinney, 202.508.3431, jkinney@bakerdonelson.com
Alisa L. Chestler, 202.508.3475, achestler@bakerdonelson.com

As we previously advised in a prior edition of *Hospitalitas* ("Congress Considers National Menu Nutrition Disclosure Standard for Chain Restaurants," 2009, Vol. 2), Section 4205 of the Patient Protection and Affordable Care Act (the Act) authorized the U.S. Food and Drug Administration (FDA) to establish and enforce national menu labeling standards applicable to certain chain restaurants and similar retail food establishments with 20 or more locations. Failure to comply with the new

continued on page 2

Revived Threat Bites Hotels

Benjamin West Janke, 504.566.8607, bjanke@bakerdonelson.com

After more than 50 years of dormancy, cases of bed bugs are on the rise at an alarming rate. The hysteria has caught the attention of the Centers for Disease Control and Prevention (CDC) and the Environmental Protection Agency (EPA), which recently released a Joint Statement on Bed Bug Control in the United States.[1]

continued on page 3

Greetings from *Hospitalitas*

Hospitalitas is the Baker Donelson newsletter for our clients and friends in the hospitality industry – hotels, restaurants and their suppliers. It is published several times a year when we believe we can deliver first class, useful information for your business. Please send us your feedback and ideas for topics you would like to know more about. True to our Southern heritage of hospitality, we'll work hard to make each visit with us something special and worth repeating.

In this issue:

New CPSC Crib Standards Will Affect Places of Public Accommodation 1

FDA Mulls Enforcement Strategy for National Menu Labeling 1

Revived Threat Bites Hotels 1

Could Internet Advertising Drag a Texas Franchisee into a Pennsylvania Court? 6

The Debut of LEED for Retail and LEED for Volume 8

Oregon Affirms Commitment to Franchisee as Employee Ruling 10

FDA Mulls Enforcement Strategy for National Menu Labeling, *continued*

requirements would render a food misbranded under the Federal Food, Drug and Cosmetic Act (FFDCA), which could result in civil and criminal penalties.

Specifically, the Act requires that calories and nutrition information be disclosed to consumers on standard menu items, food on display and self-service food. Section 4205 also requires vending machine operators who own or operate 20 or more machines to disclose calories for articles of food. The legislation allows restaurants and retail food establishments with less than 20 locations and vending machine operators with less than 20 machines to opt-in to the regulatory regime by registering with the FDA.[1]

Purpose of the Legislation

The legislation is the result of a political compromise reached between the national restaurant industry and public health and consumer groups on standardizing the way calories and nutrition information is disclosed on menu boards. In the wake of federal court decisions upholding the authority of state and local governments to regulate menu labeling, industry groups feared exposure to multiple and potentially conflicting labeling requirements by different states and municipalities. To that end, Section 4205 preempts state and local menu labeling that is not identical to the national menu labeling standards authorized by the Act.[2]

Key Requirements of Section 4205

Under Section 4205, chain retail food establishments must meet the following requirements: (1) disclose the number of calories in each standard menu item on menus and menu boards; (2) make additional written nutrition information available to consumers upon request; (3) provide a statement on menus and menu boards about the availability of the additional nutrition information and (4) provide calorie information (per serving or per food item) for most self-service items and food on display on a sign adjacent to each food item. These requirements took effect on the date of enactment of the Act (March 23, 2010) but the FDA has stayed enforcement until it has decided on a final enforcement strategy.[3]

The FDA is also expected to issue no later than March 23, 2011 proposed regulations concerning a narrow set of issues specifically identified in the legislation, such as the standardization of recipes and methods of preparation, reasonable variation in serving size, ingredients, and formulation of menu items, space on menus and menu boards, inadvertent human error, the training of food service workers and "other factors" the FDA determines to be useful to the industry in meeting the calorie and nutrition labeling requirements.

Concerns about FDA Enforcement Strategy

There is tremendous uncertainty among industry groups concerning the way the FDA plans to enforce Section 4205. The problem is in part caused by the way Congress drafted the statute. In delegating authority to the FDA, Congress usually requires the agency to conduct a formal rulemaking process subject to public notice and comment period. However, because Section 4205 took effect on March 23, 2010, the FDA may enforce these requirements prior to completing a formal rulemaking process. For the time being, the FDA has agreed to stay enforcement of these provisions until it has finalized what is in essence a pre-rulemaking guidance document to guide interim FDA enforcement. The FDA continues to solicit input on the document, including "the appropriate time period for enforcement after the issuance of final guidance."

If the FDA decides to enforce Section 4205 in a guidance document before completing a formal rulemaking, regulated restaurants may be forced to first comply with an agency guidance document for an as yet unknown time period. The FDA could then instruct restaurants to change mid-course and comply with a revised set of rules produced after a lengthy formal rulemaking process to be completed at some point in the future. Because such an enforcement strategy will lead to added compliance costs and potential confusion in the compliance, inspection and enforcement process, industry trade groups have told the FDA that issues being addressed in the guidance document and the rulemaking process should be covered simultaneously in one consolidated rulemaking procedure. Convincing the FDA to initiate a formal rulemaking relating to all aspects of Section 4205 is a top industry priority. In comments submitted to the FDA on September 7, the National Council of Chain Restaurants and the National Restaurant Association told the FDA that "attempting to require implementation based on general statutory language and guidance followed by a second implementation in accordance

continued on page 3

FDA Mulls Enforcement Strategy for National Menu Labeling, *continued*

with the final regulation would be contrary to law, confusing to our customers, and an undue burden on the industry."

The Road Ahead

It is too early to predict the regulatory compliance and enforcement strategy on which the FDA finally decides. Industry stakeholders will remain heavily involved in shaping the strategy and will not be shy about reaching out to key allies on Capitol Hill in ensuring that the FDA adopts an open and transparent notice and comment process so that industry is fully aware of all of its obligations under the law prior to FDA enforcement. In the interim, regulated restaurant operators should work with suppliers to make sure they are fully aware that once the menu labeling standards become fully enforceable, any alterations in the nutritional values of their products will have a big impact on menu labeling. Stay in contact with your counsel on the timing of the upcoming compliance materials.

Mr. Kinney is a senior advisor and Ms. Chestler is an attorney in our Washington, D.C., office.

1. The FDA issued a notice in the *Federal Register* on July 23 informing restaurants with less than 20 locations and vending machine operators with less than 20 machines of the FDA registration process in the event they choose to opt-in to the national menu labeling regime. Vol. 75 Fed. Reg. 43182 (July 23, 2010)
2. On August 25, the FDA issued a draft guidance document notifying state and local governments of the legal impact of Section 4205 on their menu and vending machine labeling laws. Vol. 75 Fed. Reg. 52427 (August 25, 2010)
3. FDA Press Release, "FDA releases guidance on federal menu labeling requirements: Agency requests public comment on implementation of new provisions," August 24, 2010. The vending machine operator nutrition labeling requirements of Section 4205 also took effect on the date of enactment, and the FDA stay applies to these requirements as well.

Revived Threat Bites Hotels, *continued*

Bed bugs have infested hotels across the country. They are natural hitchhikers who latch on to travelers and their luggage and make new homes wherever people sleep. The resurgence is linked to a number of causes, including an increased resistance to pesticides; increased domestic and international travel; the banning of pesticides proven to be effective against them, such as DDT, in favor of less environmentally impactful chemicals; and ineffective pest management programs.

Bed bugs are small, flat insects belonging to the Cimicidae family that are reddish-brown, wingless and about the size of a watermelon seed. Bed bugs feed on blood, but they can go several months without food. They create habitats near where people sleep and hide practically anywhere such as box springs, clothing and curtains; they travel with ease in folds of luggage, overnight bags and clothes.

Bed bug bites are similar to mosquito bites, but unlike mosquitoes or other pests, bed bugs are not known to transmit disease. They inject an anesthetic and anticoagulant so that the person does not feel the bite, but the bite may take as long as two weeks to manifest. People may suffer allergic reactions to bed bug bites, inflammation or secondary infections to the skin; but the primary symptom from the bite is itching. For most people, bites require no treatment. Discomfort is treated with antiseptic lotion or antibiotic cream, or in more significant inflammation and irritation, corticosteroids and oral antihistamines.[2]

Psychologically, however, affected claimants often argue that bed bugs present a greater threat of maladies such as insomnia and anxiety. While bed bugs do not present the same health hazard as many other disease carrying pests, they are the current sensational news story. Regardless of the truth that these pests are relatively innocuous, the stigma of being bitten over 100 times in a night without knowing about it is strong.

Hotel operators have seen a spike in litigation related to bed bug bites and infestations. Most state laws provide for

some sort of implied warranty of habitability between the hotel and its guests, and claimants have founded their causes of action against hotels for a breach of this warranty or general negligence.[3] Some states are enacting bed bug legislation to clarify the duty of the landowner, to prevent and solve bed bug issues and to penalize those who breach that duty.[4]

For the most part, the general damage awards have been relatively minimal

continued on page 4

Revived Threat Bites Hotels, *continued*

and range from $4,000 to $24,500.[5] The small damage awards may limit the number of individual claims against hoteliers, as the value of the claim may not be high enough for an attorney to take the case. Nevertheless, the potential for much higher damage amounts related to emotional distress and mental anguish, and the perceived fear of adverse publicity in this era of unverified consumer outrage using public forums like Trip Advisor, provides an incentive to continue aggressive pursuit of the cases.

Hotel operators should not treat bed bug infestations lightly, as some courts have assessed significant punitive damages in bed bug cases when the hotel demonstrates little or no willingness to solve the problem. For example, guests at a Chicago hotel who suffered bed bug bites were given only $5,000 in compensatory damages but another $372,000 in punitive damages for the hotel's "willful and wanton conduct."[6]

Hotels with effective pest control programs for other insects that respond to such programs remain vulnerable to bed bug infestations simply because each new guest represents a risk of contamination that cannot be avoided. There is little that can be done to prevent bed bugs. Unlike many other pests, bed bugs are not attracted to bait traps because they feed on blood. An infestation of many other pests and vermin can be avoided by maintaining a clean environment, but sanitation has little to do with bed bugs. Hotels can take some limited measures to prevent bed bugs such as reducing the number of hiding places, limiting fabric surfaces where appropriate (for example, luggage racks), vacuuming and sealing cracks and crevices. Otherwise, proactive measures to prevent bed bugs are few.

The greater threat on the horizon is potential for expensive and time-consuming class action litigation. A multi-unit operator's failure to institute a comprehensive plan to prevent and manage bed bug infestations at a corporate level could result in significant exposure for a class action defendant.

Most franchised hotel chains allocate responsibility for pest control to the local operator, much like security. In the franchise context, this approach manifests in operations manual language that alerts the franchisee to this responsibility. More specific language runs the risk of crossing the threshold into "control" that will offer claimants the chance to take the franchisor, as well as the operator-franchisee, to trial.[7] But at the same time, franchisors can generally protect the franchise by setting out standards governing their franchisees' operations and reserving their right to inspect, monitor or evaluate the franchisees' compliance with such standards.[8] Context remains important to delineating between franchisor and franchisee responsibilities. Given the public image crisis that has the potential to affect all locations when the blunder of a single franchisee is cast into the spotlight,[9] franchisors will wish to address the issue of "control" with the utmost care.

Likewise, in the management arena, owners will likely rely on the professional manager to deal with a bed bug issue aggressively and quickly. The fragility of operating budgets can be readily exacerbated by rooms out of service for pest eradication, particularly if a few rooms of infestation are not quickly addressed, so a larger section of the hotel is affected by the eradication process once it has begun.

Note: Actual size of adult insect is approximately 3/16" in length.

While hotel operators have little choice but to approach bed bug problems with a more reactive approach, they can be proactive about mitigating the damages and limiting or avoiding liability. First, hotel operators should instruct and train housekeepers to look for and spot bed bugs as a part of the daily routine. Having a checklist for each day's or checkout inspection is a good idea, as it both reinforces the housekeeping staff's instructions and serves as evidence of a hotel's diligence in limiting the risk. Second, hotels should have an integrated pest management system in place that takes into account the life cycles of bed bugs and other pests and their interaction with the environment. This includes using appropriate pesticides according to the manufacturer's directions, which among other things prevents the likeli-

continued on page 5

Revived Threat Bites Hotels, *continued*

hood that bed bugs will develop a resistance to such pesticides. The EPA has a list of over 200 EPA-registered bed bug products[10] and offers a search tool to help identify the appropriate product.[11] Other environmentally friendly solutions are also available, such as using extreme heat treatments or deep freezing. Third, hotels should have a written plan for dealing with bed bugs and should execute the plan immediately following the first report. Finally, hotels should have a licensed pest management company respond in the event of a bed bug report as anecdotal evidence shows that home grown solutions are inconsistent and ineffective.

As travel for business and leisure is improving, prudent operators will prepare for this new threat to returning demand. A comprehensive plan to respond to bed bug reports and to take effective, responsive and protective measures demonstrates the level of care demanded by the law and the well-informed traveling public.

Mr. Janke is an attorney in our New Orleans office.

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1. http://www.cdc.gov/nceh/egs/publications/Bed_Bugs_CDC-EPA_Statement.htm
2. http://www.biteremedy.com/BedBug-Bites.html
3. Similar landlord and tenant laws provide the foundation for a cause of action against landlords in a lease context, where it can be more challenging for the landlord to solve the bed bug problem when he does not have complete control of the premises as a hotel owner does.
4. *See* New Jersey Assembly Bill No. 3203 (2008), available at http://www.njleg.state.nj.us/2008/Bills/A3500/3203_I1.HTM.
5. *See generally Stuerhoff v. Cort Business Services Corporation*, 2009 WL 4906548 (M.D. La. 2009). *See also Matthias v. Accor Economy Lodging, Inc.; Motel 6 Operating LP*, 2003 WL 25147946 (N.D.Ill.2003) ($5,000 in general damages); *Wyatt, Pro Ami, Slaton v. Heritage Christian Academy; Heritage Assembly*, 2003 WL 25693187 (Ala. Dist. Ct. 2003) ($9,800 settlement award for four-year-old who suffered ant bites at a day care facility); *Elgandy v. Boyd Mississippi, Inc.*, 2003 WL 24571854 (Unknown State Miss. Dist. Ct. 2003) ($4,000 awarded where plaintiff suffered an allergic reaction to insect bites she received in her room at the defendant resort where she was a guest); *Huynh v. J.C. Penney Co.*, Inc., 2008 WL 4145883 (N.J. Dist. Ct. 2008)), JVR No. 492575) ($49,000 award for two plaintiffs who suffered insect bites after sleeping on a bed purchased at the defendants' store).
6. The hotel in this case had the opportunity to spray every room for only $500, but it declined to do so. When the hotel discovered bed bugs the following year, the hotel asked the pest control company to spray just the affected room. Later, the hotel's manager discovered bed bugs in other rooms after investigating refunds being given by desk clerks and reports from guests that there were ticks in the rooms. The judgment was affirmed on appeal by Judge Richard Posner in *Mathias v. Accor Economy Lodging*, Inc., 347 F.3d 672 (2003). Judge Posner reasoned that the quantum of punitive damages was appropriate to achieve deterrence: "The award of punitive damages in this case thus serves the additional purpose of limiting the defendant's ability to profit from its fraud by escaping detection and (private) prosecution. If a tortfeasor is 'caught' only half the time he commits torts, then when he is caught he should be punished twice as heavily in order to make up for the times he gets away." *Id.* at 677. *See also* Steven Shavell, *On the Proper Magnitude of Punitive Damages:* Mathias v. Accor Economy Lodging, Inc., 120 HARV. L. REV. 1223 (2007).
7. Exhibiting too much "control" may render a franchisor liable for claims against the franchisee under three theories: (1) the "joint employer" theory; (2) the "agency" theory or (3) the "apparent or ostensible employer" theory. Consider the case of *Myers v. Garfield & Johnson Enterprises, Inc.*, 679 F.Supp.2d 598 (E.D. Pa. Jan. 14, 2010), a case in which a franchise employee sued the tax preparation services franchise, franchise supervisors and the franchisor for sexual harassment. The employee cited various actions by the franchisor in adopting a system-wide code of conduct and training of its franchisees' employees to establish liability for the franchisor. Regarding the "joint employer" theory, whereby the franchisee and franchisor are both considered the "joint employer" of the employee, the court considered three factors: (1) the authority to hire and fire employees, promulgate work rules and assignments and set conditions of employment, including compensation, benefits and hours; (2) day-to-day supervision of employees, including employee discipline and (3) control of employee records, including payroll, insurance, taxes and the like. *Myers*, 679 F.Supp.2d at 607. Similarly, in support of the "agency" theory, the *Myers* court looked to the franchisor's degree of "control" over the franchisee's day-to-day decisions. *Myers*, 679 F.Supp.2d at 611. Regarding the "apparent or ostensible employer" theory, the court looked to statements made by the principal (the franchisor) to the employee. *Myers*, 679 F.Supp.2d at 613.
8. *See generally Schlotsky's, Inc. v. Hyde*, 538 S.E.2d 561, 563 (Ga. App. Aug. 25, 2000).
9. *See* Jessica Dickler, *Franchise Nightmare, the "Rat Effect,"* at http://money.cnn.com/2007/03/19/smbusiness/franchisee_problems/index.htm
10. http://cfpub.epa.gov/oppref/bedbug/search_results.cfm?mattress=1&ProductName=&ingSearch=null&company=null&Registration=&Submit=Search
11. http://cfpub.epa.gov/oppref/bedbug/

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Could Internet Advertising Drag a Texas Franchisee into a Pennsylvania Court?

Jillian M. Suwanski, 615.726.5558, jsuwanski@bakerdonelson.com

A Pennsylvania Federal Court recently refused to dismiss a case filed by a hotel guest and his wife against franchisor Hampton Inns, its Texas franchisee Allen Stacy Hotel, Ltd., its parent Hilton Hotels Corporation and hotel manager Gateway Hospitality Group, Inc., rejecting arguments that the court lacked personal jurisdiction over Hampton and the Texas hotel owner.[1] The opinion marks one court's foray into harmonizing an old line of hotel reservation system cases with modern reservation practices and internet marketing activity for the purpose of considering whether a guest can sue a distant hotel in the guest's home district. This unconventional case represents the court's willingness to extend the reach of Pennsylvania jurisdiction beyond traditional "minimum contacts" limits (which contemplate a voluntary physical presence or transactions delivering goods or services in-state) to transactions originated through ecommerce activity that brought the Pennsylvania guests to the Texas hotel. In a twist of traditional agency concepts, in which the injured party usually seeks to hold the franchisee to be the franchisor's agent as the basis of liability for the franchisor, this case seeks to obtain jurisdiction over and find both franchisor and franchisee liable because the franchisor is the franchisee's agent.

In *Orazi v. Hilton Hotels Corporation, et al.,* Pennsylvania residents Dante Orazi and his wife Eileen (plaintiffs) sued the franchisor, franchisee, reservation system owner and hotel management company[2] for negligence and loss of consortium due to injuries suffered by Mr. Orazi after a "slip, trip and fall" in the bathroom of the Allen, Texas, Hampton Inn.[3] Although the accident occurred in Texas, plaintiffs argued that Hampton and the hotel owner are subject to the jurisdiction of and venue in the Pennsylvania federal court because plaintiffs had booked their Texas hotel room online through the www.hamptoninn.com booking engine from their home in Pennsylvania.

Throughout the opinion, the court seemed to lean towards granting the franchisor's and hotel owner's Motion to Dismiss, as the court found at every step that plaintiffs did not meet their burden of proving the minimum contacts with the Pennsylvania forum. However, the court threw a curveball at the end when it ordered jurisdictional discovery so that plaintiffs could have the opportunity to discover and then allege the proper facts. The court mapped a route for plaintiffs to show them exactly what facts they need to prove in an amended complaint for the court can exercise jurisdiction over the hotel owner and franchisor.

In their Motion to Dismiss, the franchisor and hotel owner first argued that neither possesses the requisite minimum contacts with Pennsylvania to be subject to the court's jurisdiction in this case. The court analyzed in great detail why plaintiffs had not met their burden of establishing jurisdiction over these two defendants. To establish personal jurisdiction, the court must find either general jurisdiction, in which contacts are unrelated to the cause of action but are "continuous and systematic," or specific jurisdiction, in which a claim is "related to or arises out of the defendant's contacts with the forum" and are significant enough for "the defendant to have reasonably anticipate[d] being hauled into court" in that jurisdiction.[4] Hampton's presence through numerous franchised hotels in this judicial district was deemed irrelevant by the court.[5]

For Hampton, the court characterized plaintiffs' attempts at establishing personal jurisdiction as "weak" and "conclusory."[6] Plaintiffs listed the following facts as the basis for their claim of jurisdiction over Hampton: (1) reservation of the room by Mr. Orazi using the Hampton website while in Pennsylvania; (2) a Philadelphia Hampton Inn's listing of the Allen, Texas hotel in its in-room directory and (3) other Philadelphia Hampton Inns' participation in promotional efforts in the city. The court stated that the in-room directory and promotional efforts of other Hampton Inns were independent actions of the owners of those hotels and did not prove that Hampton controlled or had any relationship with such hotels beyond sharing a brand identity. Even if Hampton did control that advertising, the contacts would be insufficient because plaintiffs did not show that the advertising was specifically targeted to Pennsylvania residents. Also, the website is owned by Hilton and its use could not be imputed to Hampton to constitute a contact because plaintiffs alleged no agency relationship between Hampton and Hilton.

The court pointed plaintiffs toward the need to allege an agency relationship between Hampton and Hilton, and the need to allege that Hampton targets Pennsylvania residents in its marketing for the brand and that such advertising is extensive.

For the Texas hotel owner, the court also found that

continued on page 7

Could Internet Advertising Drag a Texas Franchisee into a Pennsylvania Court?, *continued*

plaintiffs did not show the requisite minimum contacts with Pennsylvania. Plaintiffs presented no evidence of direct contacts, but relied solely on the argument that Hilton's contacts could be imputed to the owner. Plaintiffs alleged that Hilton is an agent of the owner because Hilton had the authority to accept reservations on the owner's behalf. Relying on a line of New York case law, the court held that a forum-state reservation service that takes and confirms reservations on behalf of the hotel acts as the hotel's agent. However, because plaintiffs did not show that Hilton could confirm reservations for the Texas hotel, the court could not find agency. The court seemed to nudge plaintiffs to provide evidence that Hilton can confirm reservations on the hotel owner's behalf.

The court also found that the other services provided to the hotel owner by Hilton were those of a traditional franchise relationship, which is not, by itself, sufficient to form minimum contacts with the jurisdiction of a hotel guest. Basing apparent authority or alter ego theory on the franchise relationship alone does not constitute due process for either party, the court stated. Unless plaintiffs can prove that the relationship goes beyond that of a traditional franchise relationship, plaintiffs could not use apparent authority or alter ego theory to prove jurisdiction over the hotel owner. Plaintiffs could still use the reservation system as its basis for agency though.

The court then explained that even if plaintiffs prove Hilton was an agent of the hotel owner, plaintiffs must also prove either (i) general jurisdiction over Hilton to the extent that Hilton's contacts with Pennsylvania directly benefit the hotel owner or (ii) specific jurisdiction of Hilton with respect to this cause of action. To prove general jurisdiction, plaintiffs must demonstrate that the Pennsylvania-targeted advertising was geared toward attracting Pennsylvanians to stay at the Texas hotel and that Hilton's interactive website was targeted at Pennsylvania residents and crucial to Hilton's or the hotel owner's business in Pennsylvania. This may prove difficult for plaintiffs to demonstrate. Specific jurisdiction, however, is an easier standard, and plaintiffs must prove only that the online reservation contract entered into between Mr. Orazi and Hilton was sufficiently related to plaintiffs' tort claims (already proven, according to the court) and that Hilton purposefully directed its activities at the forum state. The court suggested that plaintiffs provide evidence of the number of transactions entered into in Pennsylvania on the Hilton website, and that this may be enough to prove specific jurisdiction.

Although it repeatedly stated that plaintiffs did not meet their burden, the court ultimately found that plaintiffs had "alleged sufficient facts to suggest with 'reasonable particularity the possible existence of the requisite contacts between [the defendants] and the forum state.'"[7] In ordering the parties to conduct jurisdictional discovery, the court noted that it wanted to see evidence of the Pennsylvania contacts of Hampton, Hilton and the hotel owner and the relationship of the parties. The court went on to explain:

> [D]iscovery is particularly important here where each of the Defendants is a corporation and much of the information that plaintiffs require to evaluate the nature of the relationships among the defendants and the extent of their contacts with this forum, such as the franchise agreement, other contracts and transactional data, is publicly inaccessible and controlled by defendants.[8]

Thus, it appears that this court will give plaintiffs every opportunity to prove jurisdiction. If plaintiffs can provide the facts the court would like to see – marketing and web-based interaction targeted directly to Pennsylvania residents, agency between Hampton and Hilton and a reservation confirmation service performed by Hilton – then Hampton and possibly the hotel owner will be forced to litigate this case in Pennsylvania. Franchisors and franchisees should both be cognizant of the ramifications of this potential result as franchisors are increasingly targeting individuals with personalized internet marketing offers based on initial interest about the brand's products or services. If contacts are sufficient for the franchisor and if agency can be proven for the franchisee, then both parties could be forced to litigate in the jurisdictions where their guests reside, instead of the franchisee's home turf.

The ramifications become even more interesting if a court decides to exercise jurisdiction over the franchisor and not the franchisee. Since the franchisor typically will operate in more than one state and market to customers broadly by means of ecommerce platforms, plaintiffs may have an easier time proving the necessary minimum contacts for

continued on page 8

Could Internet Advertising Drag a Texas Franchisee into a Pennsylvania Court?, *continued*

the franchisor than they will for its franchisees. If a court exercises jurisdiction over a franchisor and not a franchisee in a premises liability or contract claim brought by the franchisee's customer, then defense counsel will raise the issue of whether the franchisee is a necessary and indispensable party required to be joined under Federal Rule of Civil Procedure 19. In premises liability cases like *Orazi*, where the franchisor is the operator of the facility, logic dictates that the franchisee should be a necessary and indispensable party, although no reported case confirms this notion. If a necessary party cannot be joined because of lack of personal jurisdiction in a situation where another court could exercise jurisdiction over all parties, then venue may need to be transferred to that other court anyway, and the *Orazi* court's expeditionary search for jurisdiction could be for naught. In other types of cases, however, the "necessary and indispensable party" analysis may lead to a different result. The parties' arguments and the court's decisions in the upcoming stages of the *Orazi* case should provide helpful instruction on these important procedural issues in franchise cases.

Ms. Suwanski is an attorney in our Nashville office.

1. *Orazi v. Hilton, et al.*, 2010 U.S. Dist. LEXIS 123472 (E.D. Pa. November 19, 2010). The Motion to Dismiss at issue also alleges improper venue as a basis for dismissal, but this article focuses on jurisdiction only. The court found that venue in the court is improper under 28 U.S.C. § 1391(a)(2) because the acts where the injury occurred took place in Texas, but deferred ruling on venue under §§ 1391(a)(1) and (a)(3) until personal jurisdiction can be determined.
2. Hilton did not join in the Motion to Dismiss and conceded jurisdiction since it is authorized to do business in Pennsylvania. After filing the Motion, the parties stipulated to the dismissal of Gateway. Thus, the court only analyzed its jurisdiction over Hampton and the Texas franchisee.
3. *Id.* at *2.
4. *Id.* at *7 (citations omitted).
5. *Id.* at *12.
6. *Id.* at *11.
7. *Id.* at *35.
8. *Id.* at *36.

The Debut of LEED for Retail and LEED for Volume

Trevor Jones, 205.244.3864, tjones@bakerdonelson.com

On November 18, 2010, the LEED (Leadership in Energy and Environmental Design) for Retail Rating System and LEED for Volume Program were unveiled by the United States Green Building Council (USGBC). LEED for Retail promises to make LEED certification more accessible and realistic for retailers and hoteliers in general, while LEED for Volume should streamline the certification process for those retailers and hoteliers desiring to certify multiple sites at the same time.

The demand for greener buildings, and particularly LEED certified buildings, by both governmental authorities and consumers continues to grow. However, until recently, only a handful of retailers and hoteliers had achieved LEED certification, primarily for two reasons. First, previous LEED certification systems did not account for the necessity of increased energy usage by retailers and hoteliers, and the lack of flexibility inherent in the LEED systems meant that only a few of even the greenest of retailers and hoteliers could obtain LEED certification. Second, LEED certification for just one site is a rigorous process that is both expensive and time consuming, and thus certifying a number of sites presents daunting challenges. However, with the debut of the LEED for Retail Rating System and LEED for Volume Program, the LEED certification process for retailers and hoteliers—especially those desiring to certify in bulk—just got easier.

The LEED for Retail Rating System and the LEED for Volume Program, which have been in pilot phase since 2007, were unveiled at the USGBC Greenbuild International Conference and Expo in Chicago. The pilot included over 80 project teams, including Chipotle Mexican Grill, Marriott Hotels, Starwood Hotels, McDonalds, Office Depot and Bank of America, most of which achieved certification during the process.

All retailers and hoteliers seeking LEED certification will now be required to build in accordance with LEED for Retail, which actually consists of two separate tracks—LEED for Retail: New Construction and Major Renovation, and LEED for Retail: Commercial Interiors. The New Construction and Major Renovation track addresses specifics for the construction of a new retail or hotel project or a major renovation of a new retail or hotel project. The Commercial Interiors track addresses the specifics of tenant spaces primarily where a retailer or hotelier is retrofitting an existing building, and thus the site or shell of the building is outside

continued on page 9

The Debut of LEED for Retail and LEED for Volume, *continued*

of the tenant's control. In developing the new LEED for Retail program, the USGBC recognized the rigidity of the previous LEED rating systems, and tailored LEED for Retail to the unique needs and issues of a retail or hotel facility. The new rating system includes threshold and calculation changes, submittal clarifications and new credits specific to retail and hotel projects.

Under the LEED for Volume Program, a prototype-based approach allows the applicant to certify a large number of projects at the same time, rather than an on an individual basis. This program is for retailers and hoteliers planning at least 25 ground-up or interior construction projects. The primary goals of the LEED Volume Program are to streamline the certification process under each LEED platform, increase the efficiency of certification and lower associated costs, all without compromising LEED's rigorous benchmark standards. There are three general steps for compliance under the LEED for Volume Program. First, the applicant should submit an application to the Green Building Certification Institute (GBCI) for initial assessment. Once the applicant is accepted, the registration process begins, which requires the submission of a prototype project. Next is the precertification process, during which the registered prototype is reviewed by GBCI to confirm that technical uniformity measures, managerial practices and educational plans are in place, and to ensure that procedures are in place for continued compliance with LEED requirements. Finally, once the applicant achieves precertification, it enters the ongoing certification phase and may begin work on all projects. To ensure

continued compliance, GBCI conducts random audits of completed sites.

Two major hoteliers—Marriott Hotels and Starwood Hotels—were among the participants in the LEED for Retail and LEED for Volume pilots. Marriott plans to certify 300 hotels in the next five years. Construction costs for LEED certified Marriott sites are estimated to be three to four percent higher, but the sites are designed to be 25 percent more efficient, and Marriott plans to recoup the initial costs in five to six years. More than 60 Starwood Hotels across nine brands are pursuing LEED certification, and Starwood Hotels' Element brand requires LEED certification for all of its sites. The Element prototype has demonstrated energy savings of 18 percent and reduced water consumption by 30 percent.

Accordingly, LEED for Retail and LEED for Volume should allow retailers and hoteliers to quickly catch up with the ever-increasing demands of governmental authorities and consumers for greener (and LEED certified) sites. For more details on these programs, please visit www.usgbc.org.

Baker Donelson is a member of the USGBC and is steadily working to form a green building initiative from members of the Real Estate, Construction and Government Regulatory Actions Groups. Three of our attorneys—Kevin Garrison, Stephen Pudner and Trevor Jones—have earned LEED A.P. accreditation, which uniquely qualifies them to advise clients in industries related to construction and commercial real estate development and leasing, including builders, suppliers, developers, retail industries and engineers and architects, as to the LEED certification process and requirements.

Mr. Jones is an attorney in our Birmingham office.

BAKER DONELSON
BEARMAN, CALDWELL & BERKOWITZ, PC

Oregon Affirms Commitment to Franchisee as Employee Ruling

Joel Buckberg, 615.726.5639, jbuckberg@bakerdonelson.com

The Oregon Court of Appeals recently affirmed its 2009 interpretation of Oregon's unemployment insurance act to cast franchisees of cleaning services as employees, rather than franchisees and independent contractors, of the franchisor. In *Gross v. Oregon Unemployment Department*,[1] a computer repair service provider called "Rent A Nerd" (RAN) matched customers in need of computer repair or other assistance with independent computer technicians. The technician arranges to visit with the referred customer, uses the technician's own tools, location and effort to resolve the repair issue or refers the customer to another RAN technician, and collects the repair fees and parts charges from the customer. Twice a month, the technician files a report and pays the RAN entity its share of the collected fees. The technicians were given written guidelines to follow in the performance of their services. The issue of whether this arrangement is a franchise under the Federal Trade Commission Franchise Rule,[2] or the Oregon franchise statute[3] was not an element in the case or the decision, but the business model resembles franchises operating in the computer and home services space.

After leaving the RAN world, a technician applied for unemployment benefits. The Oregon Employment Department (OED) investigated and determined that RAN was structured as an employment arrangement. The owner of RAN was assessed for unemployment taxes. He appealed the decision and an administrative law judge affirmed the OED's determination and assessment. The RAN owner then appealed to the Oregon Court of Appeals, which agreed with the OED and its judge that the arrangement was employment and was not an independent contractor arrangement. The court dismissed the RAN owner's arguments that the technicians were *his* employer or *he was* the independent contractor in the relationship. The court endorsed the OED's reasoning, which relied heavily on RAN's claim that the retail customers were customers of RAN and not customers of the individual technicians. Customer "ownership" and good will retention is one of the hallmarks of a franchise system; the concept forms a key part of the system's value – loyalty is to the brand and not to the individual store.

To reach its conclusions, the court drew heavily on its 2009 decision in *Employment Dept. v. National Maintenance Contractors*,[4] in which it construed the definitions of "employment," "services" and "remuneration" under the Oregon unemployment insurance contribution statute[5] to cause it to apply to a commercial cleaning franchise. Like most franchises in that genre, the customers were expressly owned by the franchisor and it collected the cleaning fees, deducted its franchise fee and paid the balance over to the franchisee operator of the business. The court held that the franchise arrangement was in effect subcontracting of cleaning services by the franchisor to the franchisees, and thus within the ambit of the unemployment insurance contribution statute.

But in this computer technician case, the relationship is much more akin to a conventional franchise. The court's recitation of the business model explained:

> [RAN]'s business arrangement did not simply involve the payment of a finder's fee by the technicians in exchange for receiving a stream of referrals. Here, the technicians were required to abide by certain written guidelines and oral expectations given to them by [RAN]…at the time they were approved to begin receiving referrals. [RAN] set a common fee structure for the technicians, he provided the technicians with a common invoice form, he chose the technicians to whom he referred customer inquiries, he required the technicians to keep him apprised of any customer appointments, and he prohibited the technicians from being directly contacted by the customers, even when a customer was dissatisfied with the technician's work. Instead, all calls from customers were required to be made to petitioner. Accordingly, [RAN] remained involved in the relationship between the technician and the customer throughout its duration. Indeed, the very nature of [RAN]'s business arrangement prevented the technicians from independently taking on repeat business from the customers.[6]

This court was not persuaded that the referral service element of the relationship removed it from the employment context, and

continued on page 11

Oregon Affirms Commitment to Franchisee as Employee Ruling, *continued*

it referenced franchising as an analogous business model for purposes of the Oregon unemployment statute.

These Oregon cases reveal an additional risk to franchise systems using the high-service, no-office, business model that has become so popular as capital for bricks and mortar franchises has become so difficult to assemble or borrow. Franchisors using the high service model typical of commercial cleaning, mobile facility, employment agency and similar concepts will need to assess whether Oregon is a friendly environment for business expansion. This court pays no heed to the mischief that could arise from its ruling, and whether carefully crafted liability allocations and risk management planning of franchise systems operating in Oregon are thrown in jeopardy by Oregon's insatiable quest for unemployment insurance contributions.

Mr. Buckberg is an attorney in our Nashville office.

1. 237 Ore. App. 671; 240 P.3d 1130; 2010 Ore. App. LEXIS 1198; Unemployment Ins. Rep. (CCH) P8922
2. 16 CFR Part 436.1(h).
3. OR. Rev. Stat. § 650.005(4)
4. 226 Ore. App. 473, 204 P.3d 151, rev den, 346 Ore. 363, 213 P.3d 577 (2009).
5. OR. Rev. Stat. § 657.030.
6. 237 Or. App. at 686.

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