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FRANCHISE ALERT | NIXON PEABODY LLP

MARCH 26, 2020



Coronavirus and the franchise system

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Global franchise companies are struggling with the effect of the coronavirus on their businesses and on the businesses of their franchisees. Franchisors must develop an effective coronavirus response plan and must communicate that plan to affected parties, including employees, franchisees, consumers, suppliers, and landlords. The Nixon Peabody Franchise & Distribution team has been providing guidance to our clients as they lead their organizations through this unprecedented situation.

The response by franchisors to the coronavirus pandemic requires both short-term, emergency measures, as well as a long-term strategy for assuring a thriving franchise system. To ensure that franchisors are able to take advantage of emergency measures, we have been working closely with our Coronavirus Response Team and can provide assistance to franchise companies on the entire range of virus-related issues, including employment, access to SBA disaster relief programs, real estate issues, restructuring, and stimulus program assistance. For your ease of reference, we have assembled below a checklist of issues that franchisors should consider and have included links to articles or resources that may be useful to franchise systems. On a less urgent basis, we understand that the pandemic will have lasting effects on the way in which franchisors and franchisees do business, and we are incorporating the lessons of the pandemic into franchise agreements, Franchise Disclosure Documents, and franchise operations.

- **Franchise system changes.**
 - Analyze whether to recommend or impose new or additional health, hygiene, maintenance, or sanitation measures upon franchisees, weighing potential brand damage against the implications for joint employment and vicarious liability.
 - Consider temporary changes to the business model and system standards to respond to changing restrictions; for example, moving from dine-in to takeout and delivery, or limiting operating hours to reflect changes in demand.
 - Consider whether to temporarily suspend or modify obligations such as marketing requirements, on-site events, mandatory operating hours, mandatory inventory levels and inventory ratios, etc.
 - Provide advertising support and a communications plan to publicize the changes.

- If franchisees are unable to actively manage their franchise due to illness, consider conditions for temporary or permanent transfers.
- **Supply chain considerations.**
 - Analyze the strength of the supply chain. If there will be shortages of branded goods or other proprietary ingredients or critical materials, consider expedited approval of alternate products and vendors.
 - Analyze force majeure and other provisions in vendor agreements to determine franchisor's rights and obligations.
 - Explore options for alternate suppliers in case existing suppliers must reduce capacity or file for bankruptcy.
- **Leases and landlords.**
 - Analyze current leases to understand obligations, including opening schedules and timelines, rent commencement dates, force majeure provisions, and other lease provisions.
 - Negotiate short-term arrangements with landlords to waive or defer rent payments, with rent deferrals containing extended repayment terms.
 - Consider creative solutions to reduce marginal costs such as relaxation of continuous operation covenants that require tenants to be open, lights on, for certain hours each day.
 - Re-negotiate lease terms so that landlords share some of the lease risk with the franchisor, such as a percentage rent concept or other profit-sharing methods.
 - Provide franchisees with assistance on lease reviews and landlord negotiations.
 - Develop template communications that franchisees can use to seek rent reductions and deferrals.
- **Labor and employment.**
 - Develop a written communicable illness response program containing specific material for outbreaks.
 - Assuage fears among employees by ensuring open communication and dialogue.
 - Limit employment-related travel in light of CDC guidance. Note that there may be potential legal exposure in prohibiting workers from personal travel.
 - Permit telecommuting on a temporary basis, to the extent possible; avoid establishing telecommuting as a reasonable accommodation for medical conditions and illnesses.
 - Comply with anti-discrimination and other laws, and consider whether any action could be interpreted as potential discrimination against a particular race, ethnicity, or nationality.
 - Determine whether the staffing at franchisor's corporate headquarters must be downsized or reprioritized to better support struggling franchisees.
 - Encourage sick workers to stay home and use accrued paid sick days, and remind employees of their options to use medical leave and/or paid vacation days.

- Remind franchisees of their obligation to operate their businesses in a safe manner, to comply with all laws, and to ensure that their conduct does not have a negative impact on the brand or the franchisor's goodwill.
 - Communicate to franchisees that they, and not the franchisor, are responsible for controlling their day-to-day operations, and encourage franchisees to consult with their attorneys to obtain legal advice.
 - Adopt heightened procedures for decontaminating common work areas at headquarters and company-owned locations, and incorporate such procedures into the operations manual so that franchisees must adhere to the same standards for disinfecting their locations.
- **Insurance.**
 - Review business interruption insurance policies to determine whether insurance benefits are available.
 - Consider whether franchisees have similar insurance coverage and provide franchisees with data needed to support claims under such coverage.
- **Loans and financing agreements.**
 - Analyze whether increased costs and decreased revenue impact franchisor's ability to fund itself and maintain its financial obligations and covenants.
 - Consider whether discussions with creditors should be commenced to determine if forbearance or deferral options are needed and available.
 - Consider fee deferrals or waivers and other support for franchisees who are suffering from reduced sales or closures, while protecting franchisor's rights in the event of a franchisee's bankruptcy.
 - Determine whether the franchisor or franchisees qualify for [SBA assistance under the federal disaster loan program](#), or similar state programs.
- **Financial restructuring; proactive investments.**
 - Consider whether a preemptive Chapter 11 bankruptcy filing might be a prudent strategy.
 - Determine whether franchisor is in a position to make a strategic acquisition or investment in a distressed company, or to provide a direct loan to a distressed company that could turn into an ownership stake.
- **Be vigilant regarding ongoing developments.**
 - Stay fully informed of all governmental orders (e.g., mandatory lockdown orders); they will have a significant impact on the nature and applicability of relief available, such as business interruption coverage.
 - Monitor new local, state, and federal aid packages; it is imperative to act quickly if any government relief is available.
- **Refer to our Coronavirus Response page early and often.**
 - We are closely tracking a number of topic areas; the links below provide quick reference to our ongoing thought leadership:
 - [Employment](#)
 - [Relief and stimulus](#)

- [Contracts and litigation](#)
- [Real estate and housing](#)
- [M&A and corporate](#)
- [Health care](#)
- [Immigration and travel restrictions](#)
- [Government investigations](#)
- [Retail industry](#)
- [All practices](#)

Nixon Peabody's Franchise Team has been skilfully guiding franchisors through threats and crises for many years. We would be happy to provide guidance on, and develop strategies for, weathering the coronavirus pandemic. For more information on the content of this alert, please contact our [Coronavirus Response team](#), your Nixon Peabody attorney, or

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