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## You Can't Have Your Cake and Eat It Too: The Standards for Establishing Apparent Agency

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**YOU CAN'T HAVE YOUR CAKE AND EAT IT TOO:  
THE STANDARDS FOR ESTABLISHING APPARENT AGENCY**

I. INTRODUCTION

In *Allen v. Greenville Hotel Partners, Inc.*,<sup>1</sup> the United States District Court for the District of South Carolina determined that a franchisor could not be held liable under a theory of apparent agency for the acts of its franchisee whose alleged negligence ultimately contributed to the death and injury of several guests in a hotel.<sup>2</sup> The court made this determination despite the fact that the franchisee's advertising campaign, pervasive signage, and ubiquitous branded merchandise all made reference to the franchisor.<sup>3</sup>

Apparent agency results from the reasonable reliance of a third party on a principal's representation that another is an agent.<sup>4</sup> Establishing apparent agency in a franchise relationship is particularly difficult. This Note argues that because consumers do not understand franchising and because franchisors prefer to maintain and cultivate this confusion, the threshold for establishing apparent agency in a franchise relationship—as applied by the court in the *Allen* case—is too strict. However, the recently published *Restatement (Third) of Agency* (*Restatement Third*) suggests that courts will continue to move in the direction of the *Allen* court.<sup>5</sup>

To understand the context in which the *Allen* court considered apparent agency theory, Part II of this Note describes the facts of that case as well as the claims the respective parties made. Part III then discusses the theory of apparent agency in the context of franchise relationships, focusing in particular on how franchises relate to consumers, and considers the holding in *Allen* in light of a more accurate consumer perspective. Part III also discusses changes to the *Restatement (Second) of Agency* (*Restatement Second*) that support the holding in *Allen*. Part IV concludes that apparent agency will continue to be a difficult claim for plaintiffs to make.

II. *ALLEN V. GREENVILLE HOTEL PARTNERS, INC.*

On the morning of January 25, 2004, a fire broke out in a Comfort Inn and Suites in Greenville, South Carolina.<sup>6</sup> Prosecutors indicted Eric Preston Hans as the arsonist responsible for the crime.<sup>7</sup> The fire killed six hotel guests and seriously injured twelve other guests.<sup>8</sup>

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1. 409 F. Supp. 2d 672 (D.S.C. 2006), *aff'd sub nom.* *Allen v. Choice Hotels Int'l, Inc.*, 276 F. App'x 339, 340 (4th Cir. 2008) (per curiam).

2. *Id.* at 681–82.

3. *Id.* at 680–81.

4. *See id.* at 680.

5. *See* RESTATEMENT (THIRD) OF AGENCY § 7.07 (2006); discussion *infra* Part III.D.

6. *Allen*, 409 F. Supp. 2d at 673–74.

7. *Id.* at 674 (citing Sealed Indictment at 5, *United States v. Hans*, No. 6:05-1227 (D.S.C. Nov. 16, 2005)).

8. *Id.*

Three of the harmed guests brought suit against the hotel.<sup>9</sup> Keith Barfield, representing the estate of Allison Barfield, brought suit against Choice Hotels International, Inc. (Choice), the franchisor of the hotel; R.G. Hospitality, LLC (RGH), the franchisee of the hotel; and Greenville Hotel Partners, Inc. (GHP), the owner of the real property on which the hotel was located.<sup>10</sup> Barfield later amended his complaint to include as defendants Ronald Gedda, the sole shareholder of RGH,<sup>11</sup> and R.G. Properties, Inc. (RGP), a company whose employees' allegedly negligently contributed to the fire.<sup>12</sup> Against all the defendants, Barfield claimed negligence for failing to provide adequate security and fire protection.<sup>13</sup>

Elsie Marie Allen, representing the estate of Donna Lea Swaim, and William E. Harrell, Jr.<sup>14</sup> also brought suit against the hotel for damages resulting from the fire.<sup>15</sup> Allen and Harrell ultimately sued the same group of defendants that Barfield sued.<sup>16</sup> They brought claims for negligent construction and maintenance of the hotel premises, negligent failure to protect against the criminal acts of third parties, negligent failure to render aid, and breach of warranty.<sup>17</sup>

The plaintiffs claimed that Choice was both directly liable for its negligence and vicariously liable for the negligence of RGH.<sup>18</sup> The plaintiffs' sole claim alleging direct liability was that Choice was negligent in failing to require RGH to retrofit the hotel with a sprinkler system before the hotel had opened.<sup>19</sup> On Choice's motion for summary judgment, the court held that "Choice did not exert sufficient control over RGH . . . to create a duty to the [p]laintiffs."<sup>20</sup> Therefore, the court granted summary judgment to Choice on the claim of direct liability.<sup>21</sup>

The plaintiffs' claims asserting vicarious liability were much broader.<sup>22</sup> Specifically, the plaintiffs claimed that

9. *Id.*

10. *Id.*

11. *Id.* The plaintiffs claimed that Gedda was also a franchisee of Choice. *Id.* On Gedda's motion for summary judgment, the court denied the motion, holding that "an issue of material fact exist[ed] as to whether Gedda was a Choice franchisee." *Id.*

12. *Id.*

13. *Id.*

14. William E. Harrell alleged that he suffered severe burns and smoke inhalation; however, he did not die in the incident. Amended Complaint at 5, *Allen*, 409 F. Supp. 2d 672 (No. 6:04-CV-2328).

15. *Allen*, 409 F. Supp. 2d at 674.

16. Barfield, Allen, and Harrell all amended their complaints twice. All three plaintiffs proceeded against the same group of defendants. *Id.*

17. *Id.*

18. *Id.* at 675.

19. *Id.* at 676.

20. *Id.* at 677 n.3.

21. *Id.* at 678.

22. *See id.* at 675.

RGH and Gedda were negligent in providing inadequate security by (1) leaving the back door to the hotel unlocked, (2) failing to install surveillance cameras at the hotel, and (3) leaving boxes and materials in a place where the arsonist could gather them and use them to fuel the fire. Moreover, the Plaintiffs argue[ed] that RGH and Gedda were negligent in (4) training employees at the Comfort Inn to disengage an active fire alarm until confirmation of the presence of a fire and to delay in calling the fire department until after confirming the fire and (5) failing to install a sprinkler system at the hotel.<sup>23</sup>

The court began by noting that the underpinning of vicarious liability is agency theory.<sup>24</sup> Agency theory is the concept that a “fiduciary relationship . . . arises when one person (a ‘principal’) manifests assent to another person (an ‘agent’) that the agent shall act on the principal’s behalf and subject to the principal’s control, and the agent manifests assent or otherwise consents so to act.”<sup>25</sup> According to the *Allen* court, two types of agency theory compose vicarious liability: actual agency and apparent agency.<sup>26</sup> Actual agency, under South Carolina law, requires that the “principal has the right to control the conduct of [its] alleged agent.”<sup>27</sup> To establish apparent agency, a plaintiff must show “(1) [a] purported principal consciously or impliedly represented another to be his agent; (2) [a] third party reasonably relied on the representation; and (3) [the] third party detrimentally changed his or her position in reliance on the representation.”<sup>28</sup>

Regarding the establishment of actual agency, the sole question for the court was whether Choice’s control over RGH and Gedda was sufficient.<sup>29</sup> Looking to the rules and regulations of the franchise agreement, the court determined that Choice only controlled “uniform service within . . . the [hotel]” and “did not control the hotel’s daily operations or hotel security and life safety systems.”<sup>30</sup> As such, Choice did not have sufficient control over the franchisees to establish liability under actual agency theory.<sup>31</sup>

23. *Id.*

24. *See id.* at 678, 680.

25. RESTATEMENT (THIRD) OF AGENCY § 1.01 (2006).

26. *See Allen*, 409 F. Supp. 2d at 678, 680. Because the plaintiffs in *Allen* based their claims in tort, RGH was considered either a servant, *see* RESTATEMENT (SECOND) OF AGENCY § 267 (1958), or an employee, *see* RESTATEMENT (THIRD) OF AGENCY § 7.07, of Choice.

27. *Allen*, 409 F. Supp. 2d at 678 (emphasis omitted) (quoting *Fernander v. Thigpen*, 278 S.C. 140, 144, 293 S.E.2d 424, 426 (1982)) (internal quotation marks omitted).

28. *Id.* at 680 (quoting *R & G Constr., Inc. v. Lowcountry Reg’l Transp. Auth.*, 343 S.C. 424, 433, 540 S.E.2d 113, 118 (Ct. App. 2000)) (internal quotation marks omitted).

29. *Id.* at 678 (“As the facts concerning how Choice allegedly controlled RGH and Gedda are not in dispute, the court finds that whether there was sufficient control for an actual agency relationship to result . . . is a question of law for the court.”).

30. *Id.* at 679 (quoting *Hayman v. Ramada Inn, Inc.*, 357 S.E.2d 394, 397 (N.C. Ct. App. 1987)) (internal quotation marks omitted).

31. *Id.*

As to apparent agency, the court began by addressing the first requisite element of the purported relationship: representation by a principal that another is an agent.<sup>32</sup> To establish this element, the plaintiffs pointed to “a national advertising and marketing program [that was] designed to drive guests to [Choice] hotels.”<sup>33</sup> In carrying out this program, Choice utilized magazine ads, newspaper ads, internet banners, and billboards.<sup>34</sup> However, “[n]one of the advertisements indicated that the hotels were independently owned or identified local operators.”<sup>35</sup> In addition, the signs outside the hotel also made no mention of local independent ownership.<sup>36</sup> Finally, none of the hotel’s branded merchandise or forms made reference to a local owner or local operator.<sup>37</sup> This merchandise included “a front desk pad, generic business cards, Choice Privileges program forms, directories of Choice properties . . . , decals for telephones, note pads, pens, soap, shampoo, laundry bags, do-not-disturb signs, privacy lock inserts, comment cards, envelopes, . . . letterhead, [and] registration forms signed by guests.”<sup>38</sup> Instead of noting local ownership, each item merely contained the Comfort Inn logo.<sup>39</sup>

In an effort to refute this claim of representation, Choice argued that “advertising a franchisor’s brand alone does not subject the franchisor to liability.”<sup>40</sup> In support of this contention, Choice cited three cases dealing with gas stations as agents of oil companies.<sup>41</sup> In each case, the plaintiffs were unable to recover from the oil companies despite signs and merchandise making reference to the franchisor’s brand.<sup>42</sup> Choice also argued that three different signs within the hotel indicated local ownership.<sup>43</sup> The first sign read, “This inn is owned and operated by [R.G. Hospitality, LLC] under license from Choice Hotels International, Inc.”<sup>44</sup> The hotel placed this sign “adjacent to the registration desk” using the specific language required by its license agreement

32. *Id.* at 680.

33. Memorandum in Opposition to Choice’s Motion for Summary Judgment at 28, *Allen*, 409 F. Supp. 2d 672 (Nos. 6:04-1260-20, 6:04-2327-20, 6:04-2328-10).

34. *Id.*

35. *Id.*

36. *Id.* at 29.

37. *Id.*

38. *Id.*

39. *Id.*

40. Choice Hotels International, Inc.’s Memorandum in Support of Motion for Summary Judgment at 27, *Allen*, 409 F. Supp. 2d 672 (Nos. 6:04-1260-20, 6:04-2327-20, 6:04-2328-20) [hereinafter Choice’s Memorandum in Support] (citing *BP Exploration & Oil, Inc. v. Jones*, 558 S.E.2d 398, 403 (Ga. Ct. App. 2001)).

41. *Id.* at 27–28 (citing *Watkins v. Mobil Oil Corp.*, 291 S.C. 62, 66, 352 S.E.2d 284, 286 (Ct. App. 1986); *Mobil Oil Corp. v. Bransford*, 648 So. 2d 119, 120 (Fla. 1995); *Jones*, 558 S.E.2d at 401).

42. See *Jones*, 558 S.E.2d at 403; *Mobil Oil Corp.*, 648 So. 2d at 120; *Watkins*, 291 S.C. at 66, 352 S.E.2d at 286.

43. Choice’s Memorandum in Support, *supra* note 40, at 29–30.

44. *Id.* at 29.

with Choice.<sup>45</sup> The second sign, also in view of the registration desk, was a framed South Carolina Retail License that listed RGH as the owner.<sup>46</sup> The third notice, found in an elevator, also noted that RGH owned the property.<sup>47</sup>

The court held that the advertising and other use of the Comfort Inn name and trademark, in light of the three notices indicating local ownership, did not amount to a representation for the purposes of establishing liability under apparent agency.<sup>48</sup> In so holding, the court granted summary judgment to Choice, determining that “no genuine issue of material fact” existed regarding the plaintiffs’ claims that Choice represented that RGH and Gedda were its agents.<sup>49</sup> The court further stated that even if the plaintiffs successfully established this first element of apparent agency, no “genuine issue of material fact [existed] with respect to the second element, reasonable reliance on the representation.”<sup>50</sup> This element failed, according to the court, because of the same notices to the guests as well as the fact that the plaintiffs’ affidavits failed to establish reasonable reliance.<sup>51</sup>

### III. THE STANDARDS FOR ESTABLISHING APPARENT AGENCY IN THE CONTEXT OF A FRANCHISE RELATIONSHIP

#### A. *The Franchise Relationship*

The claim of apparent agency in *Allen* was rooted in the franchise relationship between Choice, the franchisor, and RGH, the franchisee. Generally, “franchising is a system of marketing and distribution.”<sup>52</sup> The core component of this system is the relationship between the franchisor and the franchisee.<sup>53</sup> Pursuant to this relationship, “a small independent businessman (the franchisee) is granted—in return for a fee—the right to market the goods and services of

45. *Id.*

46. *Id.* at 29–30. This sign stated that the hotel was a Days Inn, not a Comfort Inn. *Id.* The hotel was previously a Days Inn. *Id.* at 30 n.3. This is significant because an indication of local ownership is likely less effective when it lists the name of a business incorrectly.

47. *Id.* at 30. This sign also noted that the hotel was a Days Inn. *Id.*

48. *Allen*, 409 F. Supp. 2d at 680–81.

49. *Id.* at 681–82. The plaintiffs appealed only the District Court’s ruling as to direct liability, and the Fourth Circuit affirmed. *Allen v. Choice Hotels Int’l, Inc.*, 276 F. App’x 339, 340 (4th Cir. 2008) (per curiam).

50. *Allen*, 409 F. Supp. 2d at 681.

51. *Id.* at 681–82 (citing *Hayman v. Ramada Inn, Inc.*, 357 S.E.2d 394, 398 (N.C. Ct. App. 1987)). Interestingly, in support of this determination, the court cited *Hayman*, a case in which, according to the *Allen* court, there was “no misrepresentation as to the relationship between the hotel franchisor and franchisee where the franchisor required the franchisee to expressly indicate its licensee relationship in all advertising.” *Id.* at 682 (citing *Hayman*, 357 S.E.2d at 398). However, in *Allen*, Choice did not provide such an indication in its advertisements of the Comfort Inn. *See supra* notes 32–39 and accompanying text.

52. David J. Kaufmann, *An Introduction to Franchising*, in PRACTICING L. INST., UNDERSTANDING FRANCHISING: BUSINESS & LEGAL ISSUES 13, 14 (David J. Kaufmann ed., 2001).

53. *See id.* at 16.

another (the franchisor) in accordance with the established standards and practices of the franchisor, and with its assistance.”<sup>54</sup>

Franchisors and franchisees base their entire relationship with one another on a franchise agreement, which details the duties, rights, and obligations of each party.<sup>55</sup> Generally, a franchisor permits a franchisee to use its trademark, provides the franchisee with information, instruction, and supplies needed to operate the business, and requires a franchisee to follow uniform policies regarding, *inter alia*, advertising, store design, and general operations.<sup>56</sup> In return, a franchisee generally agrees to pay the franchisor an initial fee and a continuing royalty.<sup>57</sup>

Franchise relationships are mutually beneficial: “[T]he franchisor obtains new sources of expansion capital, new distribution markets, and self-motivated vendors of its products, while the franchisee acquires the products, expertise, stability, and marketing savvy usually reserved only for larger enterprises.”<sup>58</sup> Under this system, a franchisor can expand a business without expending capital.<sup>59</sup> By associating itself with a larger franchisor, a franchisee gains an initial market advantage<sup>60</sup> and ultimately has a higher likelihood of success.<sup>61</sup>

## *B. Consumer Knowledge About Franchising and Resulting Consumer Behavior*

### *1. Consumer Confusion over Franchise Relationships*

Many courts have recognized consumers understand that independent retailers use trademark names and sell trademarked goods as part of a franchise relationship.<sup>62</sup> These courts go so far as to describe this understanding as “common knowledge.”<sup>63</sup> Accordingly, pursuant to the common knowledge doctrine, judges dismiss apparent agency claims on summary judgment because “customers . . . cannot reasonably rely upon these signs as ‘manifestations’ of agency, permitting them to obtain relief against the trademark licensor

54. *Id.* at 14.

55. *Id.* at 16.

56. *Id.*

57. *Id.* at 17.

58. *Id.* at 14.

59. *Id.* at 20. In fact, a franchisee pays a franchisor to do so. *See id.*

60. *See id.* at 21 (noting that the franchise agreement provides the franchisee with benefits “which otherwise would take decades to obtain”).

61. *Id.* Kaufmann notes that a study of 366 franchise companies across 60 industries revealed that the average rate of failure for franchise companies within the first 5 years was 14% as compared to a 65% failure rate for non-franchise companies within the same time period. *Id.*

62. Robert W. Emerson, *Franchisors’ Liability When Franchisees Are Apparent Agents: An Empirical and Policy Analysis of “Common Knowledge” About Franchising*, 20 HOFSTRA L. REV. 609, 645 (1992) (citing twenty-five cases from sixteen different states for this proposition).

63. *See id.* Legal scholars refer to this theory as the “‘common knowledge’ doctrine.” *See id.* at 646.

(franchisor) for the acts of an apparent agent, the licensee (franchisee).”<sup>64</sup> This decision by courts is a bold move because “[c]ourts have not required the production of evidence (surveys, studies) to support a finding of common knowledge, but have simply taken judicial notice of it.”<sup>65</sup>

However, “most [people cannot] recognize the . . . existence of a franchise in the very circumstances where courts have found ‘common knowledge’ about independent dealers or trademark licensees.”<sup>66</sup> One survey regarding common knowledge about franchising found that the public, on the whole, does not understand which businesses are company owned and which are independently owned.<sup>67</sup> This lack of understanding applies in the hotel industry for both predominantly franchised hotel chains and completely integrated hotel chains.<sup>68</sup> The majority of respondents also believed that they, as hypothetical customers, could hold franchisors liable for the negligence of its franchisee.<sup>69</sup> Thus, “it is not necessarily customer reliance, but judicial reliance [on the common knowledge doctrine] which is misplaced.”<sup>70</sup>

## 2. *Franchisors and Franchisees Intend to Create Consumer Confusion*

Uniformity is the economic underpinning of franchising.<sup>71</sup> Consumers desire uniformity because it gives them a sense of familiarity and the impression of a standardized business.<sup>72</sup> Accordingly, franchisors usually contractually obligate franchisees to “join in the franchisor’s efforts to ‘fool the customer’ . . . [and] maintain the illusion that the business consists of uniform, wholly integrated outlets when . . . the ‘chain’ actually consists of separate, independent businesses.”<sup>73</sup>

A franchisor could avoid potential liability for the acts of its franchisee by requiring the franchisee to clearly and candidly acknowledge its independent status in signage and advertisement.<sup>74</sup> However, this acknowledgment may have

64. *Id.* at 645 (emphasis omitted).

65. *Id.* at 648.

66. *Id.* at 660.

67. *Id.* at 651–56. The respondents in this study were college students (having a median age of twenty-one) and older individuals (having a median age of forty-five). *Id.* at 648–49. According to the study, these groups were more educated than the average American adult. *Id.* at 649. Therefore, to the extent that these groups are not an accurate representative sampling of the public, the sampling should in fact have greater knowledge than the public when it comes to understanding franchising. *Id.*

68. *Id.* at 655 (referencing Holiday Inn and Motel 6, respectively).

69. *Id.* at 658.

70. *Id.* at 661 (emphasis omitted).

71. Kaufmann, *supra* note 52, at 14.

72. See Emerson, *supra* note 62, at 630.

73. *Id.*

74. See *id.* at 668–69 (suggesting as examples “Alfie’s McDonald’s; Central City Ltd.-Holiday Inn; and Nutri/System of North Florida, Independent Proprietors”).



a detrimental impact on the business.<sup>75</sup> Therefore, a “franchisor . . . might prefer to risk liability rather than to post disclaimer signs that, if read and understood, diminish customer goodwill and eradicate, or at least reduce, the consumer’s perception of chain-wide uniformity.”<sup>76</sup>

*C. Why the Standard for Apparent Agency as Applied by the Allen Court Is Too Strict*

Just as the common knowledge doctrine impedes consumers’ claims of reasonable reliance, the doctrine also makes it more difficult for consumers to claim that the franchisor represented that the franchisee is its agent.<sup>77</sup> The parameters of such a representation likely depend on how consumers perceive the purported representation. To this end, the inability to reasonably rely on national ownership likely inhibits a successful claim that a franchisor represented that a particular franchisee acted on its behalf and subject to its control.

In *Allen*, the court found both of these elements—representation and reasonable reliance—lacking in the plaintiffs’ claim under apparent agency theory.<sup>78</sup> The court made this determination even in light of a high degree of uniformity.<sup>79</sup> In essence, the *Allen* court permitted Choice to “reap the benefits created by public recognition of its [brand] and yet be held to no duty to assure the quality of the product, or services associated with that [brand].”<sup>80</sup>

In justifying its decision, the *Allen* court focused exclusively on three small signs located in the hotel indicating local ownership.<sup>81</sup> The court effectively determined that these three small signs were sufficient to overcome the large amount of other evidence indicating national ownership and management.

Balancing these competing pieces of evidence in favor of the franchisor in this case was improper for three reasons. First, given the realities of consumer understandings of franchising, to avoid liability Choice should have been obliged to require its franchisee to convince consumers of local ownership. Three small signs failed to achieve this end, especially because two of the signs indicated that

75. *See id.* at 663. When the survey directed respondents to assume that the franchisor, Burger King Corporation, would not be legally responsible for the goods sold and services provided at a particular franchise location, 33.8% of the respondents indicated that this fact made it less likely they would return to that location. *See id.* at 663, 684. *But see* Randall K. Hanson, *The Franchising Dilemma Continues: Update on Franchisor Liability for Wrongful Acts by Local Franchisees*, 20 CAMPBELL L. REV. 91, 105 (1997) (“There appears to be no logical reason why a franchisor would not insist on the use of prominent signs to indicate local ownership.”).

76. Emerson, *supra* note 62, at 633.

77. Reasonable reliance and representation are two of the three elements a claimant must satisfy in order to successfully establish liability premised on apparent agency theory. *See supra* note 28 and accompanying text.

78. *See supra* notes 48–51 and accompanying text.

79. *See supra* notes 33–39 and accompanying text.

80. Emerson, *supra* note 62, at 637 (quoting Scott P. Sandrock, *Tort Liability of a Non-Manufacturing Franchisor for Acts of Its Franchisee*, 48 U. CIN. L. REV. 699, 710 (1979)).

81. *See supra* notes 43–47 and accompanying text.

the hotel was a Days Inn and not a Comfort Inn.<sup>82</sup> At best, this inaccuracy would likely have indicated to a consumer that the signs were outdated and no longer valid.

Second, one of the signs was located in an elevator inside the hotel.<sup>83</sup> For a notice of independent ownership “to be effective, [it] must come at a meaningful time.”<sup>84</sup> By the time a guest saw the sign on the elevator, that guest had already reasonably relied on other representations made by the hotel, namely the trademark of the hotel. Therefore, the sign on the elevator did not come at a meaningful time and was ineffective.

Finally, the amount and pervasiveness of Comfort Inn advertisements alone should have sufficed in establishing a representation upon which consumers could reasonably rely. Choice cited a few state court cases dealing with gas stations for the proposition that advertising alone does not suffice.<sup>85</sup> However, these cases likely relied on the common knowledge doctrine, which is unrealistic because “[t]he public seems to have no more knowledge about ownership and operations of gas stations than it does of other businesses such as . . . hotel chains.”<sup>86</sup> Moreover, the element of representation requires only that a franchisor “impliedly represent[] another to be his agent.”<sup>87</sup> Given Choice’s incentives to achieve uniformity<sup>88</sup> as well as its minimal efforts to require its franchisee to indicate local ownership,<sup>89</sup> Choice, at a minimum, implied that RGH was its agent.

### 1. *Allen’s Relevance to South Carolina State Courts*

The United States District Court for the District of South Carolina had original jurisdiction over this matter on the basis of diversity jurisdiction.<sup>90</sup> However, South Carolina state courts are likely to rely on the holding in *Allen* as secondary authority. This is especially true because South Carolina state courts addressing agency issues have relied on federal court precedent in the past.<sup>91</sup>

82. *See supra* notes 46–47.

83. *See supra* note 47 and accompanying text.

84. *Simmons v. Tuomey Reg’l Med. Ctr.*, 341 S.C. 32, 47, 533 S.E.2d 312, 320 (2000) (quoting *Clark v. Southview Hosp. & Family Health Ctr.*, 628 N.E.2d 46, 54 (Ohio 1994)) (internal quotation marks omitted).

85. *See supra* notes 40–42 and accompanying text.

86. *Emerson, supra* note 62, at 654.

87. *Allen v. Greenville Hotel Partners, Inc.*, 409 F. Supp. 2d 672, 680 (D.S.C. 2006) (quoting *R & G Constr., Inc. v. Lowcountry Reg’l Transp. Auth.*, 343 S.C. 424, 433, 540 S.E.2d 113, 118 (Ct. App. 2000)) (internal quotation marks omitted).

88. *See supra* notes 71–76 and accompanying text.

89. *See supra* notes 43–47 and accompanying text.

90. *See Amended Complaint, supra* note 14, at 2–3 (citing 28 U.S.C. § 1332 (2006)).

91. *See, e.g., Roberson v. S. Fin. of S.C., Inc.*, 365 S.C. 6, 11, 615 S.E.2d 112, 115 (2005) (citing *Schultz v. Schultz*, 436 F.2d 635, 637 (7th Cir. 1971)) (discussing whether the use of apparent authority is sufficient to show authorization to accept service); *Fernander v. Thigpen*, 278 S.C. 140, 142, 293 S.E.2d 424, 426 (1982) (quoting *Hayward v. Holiday Inns, Inc.*, 459 F. Supp.

Moreover, South Carolina state court decisions are not in complete agreement over the elements of apparent agency theory.

For example, the South Carolina Court of Appeals has held that advertising a franchisor's brand, no matter how pervasively, does not constitute a representation on the part of the principal that the franchisee is its agent.<sup>92</sup> However, the South Carolina Supreme Court, in an earlier opinion, applied a more stringent standard, viewing the use of the principal's name as highly relevant in determining whether the principal represented that a franchisee was its agent.<sup>93</sup> Therefore, it is reasonable to expect that South Carolina courts will look to other jurisdictions for guidance in applying these seemingly conflicting holdings.

## 2. *Policy Prescriptions for Applying a More Liberal Standard*

To the extent that all franchisees have insurance, which franchisors commonly mandate under franchise agreements,<sup>94</sup> franchisees can satisfy many judgments by compensating victims with the aid of their insurance coverage. Mandating insurance coverage relieves the franchisor from any financial burden. With adequate insurance, it is likely that franchisees could bear this burden regardless of any representations made by the franchisor.

However, in situations where damages exceed the insurance coverage of the franchisee, a decision must be made: should the franchisor incur a financial burden or should an injured party not be made whole?<sup>95</sup> In certain circumstances, a party's injuries are left completely unsatisfied or only partially satisfied where they cannot establish apparent agency. Therefore, fairness is at the heart of the representation threshold of apparent agency theory. Accordingly, and out of fairness, the bar at which courts relinquish franchisors from liability for the

634, 636 (E.D. Va. 1978)) (discussing reliance upon a licensing agreement in conjunction with direct testimony to show agency).

92. See *Watkins v. Mobile Oil Corp.*, 291 S.C. 62, 66, 352 S.E.2d 284, 286 (Ct. App. 1986) ("The display of Mobil signs and its emblem merely represented to motorists and others that the station marketed Mobil's products.").

93. See *Beasley v. Kerr-McGee Chem. Corp.*, 273 S.C. 523, 528–29, 257 S.E.2d 726, 728–29 (1979). In *Beasley*, a customer purchased seed from a general store. *Id.* at 525, 257 S.E.2d at 727. The store was known as "Houser's Supermarket," but a portion of the store therein was named "Kerr-McGee Field Office." *Id.* The seeds were defective and the customer sought recovery from Kerr-McGee. *Id.* at 526, 257 S.E.2d at 727. The *Allen* court distinguished *Beasley* on the grounds that (1) the principal directly billed the customer in *Beasley* and (2) the franchisee used the franchisor's name to denote only a portion of a store—the "Kerr-McGee Field Office"—and did not use it in the name of the store as a whole. *Allen v. Greenville Hotel Partners, Inc.*, 409 F. Supp. 2d 672, 681 (D.S.C. 2006). The direct billing in *Beasley* is a valid distinction. However, the omission of the franchisor's name in the whole store name is not a fair distinction because the *Beasley* court relied heavily on the use of the franchisor's name in a portion of the store name as well as on a delivery ticket. See *Beasley*, 273 S.C. at 528–29, 257 S.E.2d at 728–29.

94. Kaufmann, *supra* note 52, at 20.

95. *Allen* likely fits into this latter group of cases given the magnitude of damages at issue. See *Allen*, 409 F. Supp. 2d at 673–74.

negligent acts of their franchisees should be set higher. To this end, courts should use a more liberal apparent agency standard in the context of franchise relationships; such a standard for holding a franchisor liable for the negligent acts of its franchisee should be easier for injured parties to satisfy.

A more drastic measure would require that a franchisee alter the name of its trademark in some way to give effective notice to consumers that it is locally-owned. However, studies suggest that business would decline at such locations because some consumers would instead consume goods or services at other locations deemed more safe and reliable.<sup>96</sup> Thus, the problem with this solution is that consumers generally have the option to choose a competing hotel with a trademark consumers deem an indicator of safety and reliability. If apparent agency theory required all hotel franchisees to slightly alter their franchisor's trademark so as to give effective notice of local ownership, most or all hotels in an area would have an altered trademark. These altered trademarks would likely still serve their prior function of identifying the source and quality of hotel services while simultaneously indicating local ownership. Accordingly, when adopted wholesale, this solution might not negatively affect the business of local hotel franchises.

The car sales industry is an example of such a practice. Car dealerships, while associated with certain manufacturers, alter the name of their business by commonly adding a personal name or geographical unit to the name of the car manufacturer. Most car dealerships' business names reflect local ownership and not simply the trademark of the car manufacturer; additionally, in some areas, multiple independently-owned dealerships are associated with the same car manufacturer. The effect of these practices is that consumers do not deem certain car dealerships more reliable than others based on a perception that a manufacturer owns or operates a dealership. Car dealerships are of course different than hotels: cars, sold by dealerships, do not change in quality from the manufacturer to the dealership, whereas the services provided by hotels can vary significantly from franchise to franchise. However, if all independently owned hotel franchisees modified their business name to reflect local ownership, no such hotel would have a comparative business advantage over another on the basis of a perception of franchisor ownership and management.

#### *D. Changes to the Restatement (Second) of Agency*

The standards the *Allen* court imposed on the plaintiffs for establishing apparent agency were too strict and unfair given that consumers generally do not understand franchising.<sup>97</sup> Instead of ascribing knowledge to consumers that they lack, the law should place a higher burden on the franchisor to convey

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96. See *supra* note 75 and accompanying text.

97. See *supra* Part III.B.1.

independent ownership to consumers. However, the recently published *Restatement Third* is in accord with the *Allen* holding.

The restatements are treatises meant to summarize the common law and indicate the direction of specified areas of the law. Although secondary authority, restatements are highly influential and are commonly used in judicial opinions and academic articles alike. Section 267 of the *Restatement Second* provides the following definition of apparent agency theory:

One who represents that another is his servant or other agent and thereby causes a third person justifiably to rely upon the care or skill of such apparent agent is subject to liability to the third person for harm caused by the lack of care or skill of the one appearing to be a servant or other agent as if he were such.<sup>98</sup>

South Carolina courts have used section 267 to support apparent agency theory.<sup>99</sup>

The more recent restatement, *Restatement Third*, omits section 267. Purportedly, the drafters of the *Restatement Third* included section 7.07 in lieu of section 267.<sup>100</sup> However, section 7.07 speaks only of the relationship between employers and employees.<sup>101</sup> This section approaches the theory of apparent agency, but it fails to encapsulate the theory because a franchisee is not an employee of the franchisor.

The *Restatement (Second) of Torts* presents plaintiffs seeking to establish apparent agency with a potential alternative:

One who employs an independent contractor to perform services for another which are accepted in the reasonable belief that the services are being rendered by the employer or by his servants, is subject to liability for physical harm caused by the negligence of the contractor in supplying such services, to the same extent as though the employer were supplying them himself or by his servants.<sup>102</sup>

98. RESTATEMENT (SECOND) OF AGENCY § 267 (1958).

99. See, e.g., *Fernander v. Thigpen*, 278 S.C. 140, 148, 293 S.E.2d 424, 429 (1982) (Littlejohn and Gregory, JJ., dissenting) (quoting *Schlick v. Berg*, 286 N.W. 356, 358 (Minn. 1939)) (noting that plaintiffs may use apparent authority as a basis of recovery in personal injury cases); *Osborne v. Adams*, 338 S.C. 82, 90, 525 S.E.2d 268, 272–73 (Ct. App. 1999) (relying on the three part test of the *Restatement Second*).

100. RESTATEMENT (THIRD) OF AGENCY § 7.07 Reporter's Note a (2006) ("This section is a consolidated treatment of topics covered in several separate sections of Restatement Second, Agency, including . . . 267."). Alternatively, section 2.05 of the *Restatement Third* could also replace section 267. See RESTATEMENT (THIRD) OF AGENCY § 2.05 (titled "Estoppel to Deny Existence of Agency Relationship"). However, unlike section 7.07, section 2.05 makes no mention of replacing section 267. See *id.*

101. See RESTATEMENT (THIRD) OF AGENCY § 7.07 (titled "Employee Acting Within Scope of Employment").

102. RESTATEMENT (SECOND) OF TORTS § 429 (1965).

Seemingly, this language could apply to all types of relationships in which a party hires an independent contractor. However, South Carolina courts have applied section 429 almost exclusively in the hospital context, where doctors associate themselves with hospitals only as independent contractors.<sup>103</sup> The extent to which section 429 applies in other contexts is unclear. Therefore, the change reflected in the *Restatement Third* indicates that support for the apparent agency theory is decreasing.

#### IV. CONCLUSION

By permitting franchisors to easily negate representations that their franchisee is their agent, the standard established in *Allen* makes the claim of apparent agency extremely difficult for plaintiffs to establish. Contrary to the prior belief of some courts, consumers on the whole do not understand franchise relationships. Therefore, expecting consumers to understand the implications of local ownership or much less even notice and read small, inconspicuous signage regarding the franchise, despite ubiquitous representations to the contrary, is unrealistic and unfair.

Modeling the hotel industry after the car sales industry could resolve this unfairness. If apparent agency theory required all hotels to indicate local ownership in the names of their businesses, no one hotel would be unfairly disadvantaged and thus suffer the negative consequences of decreased business.<sup>104</sup> Until such changes occur, however, changes reflected in the recently published *Restatement Third* indicate that courts will continue to apply the stringent standards for a representation as applied in *Allen*.

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103. See, e.g., *Simmons v. Tuomey Reg'l Med. Ctr.*, 341 S.C. 32, 50–51, 533 S.E.2d 312, 322 (2000) (applying section 429 to a case concerning whether a hospital owes patients a non-delegable duty of competent service).

104. See discussion *supra* Part III.C.2.

