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N.J. Judge: Arbitration Clause Can't Bar Suit by Snap-on Franchisee Wives

By Frank Reynolds
Franchise & Distribution Litigation Reporter

In a potentially groundbreaking decision for the franchise industry, a New Jersey judge has found that a global arbitration clause does not stop the wives of Snap-on Tools Co. franchisees from suing the franchisor for fraud.

The judge said the wives have an independent right to sue for economic and emotional damages they say they suffered because Snap-on's negligent misrepresentation wiped out family finances.

Since the language of the arbitration clause, which forces franchisees to arbitrate rather than litigate any disputes, is similar to that of many other franchise agreements, the impact of the ruling would be significant if other courts follow the judge's reasoning.

Judge Mathias Rodriguez of the Middlesex County Superior Court found that since the wives did not sign the agreements they were not barred from going to court with their claims that their household finances and sometimes their marital relationships were wrecked because their husbands were tricked into investing heavily in businesses that Snap-on knew had little chance of success.

"This has important ramifications for other franchisees who have found the door to the courthouse barred by arbitration clauses," said plaintiffs' attorney Gerald Marks of Marks & Associates in Red Bank, N.J. "If the husband sustains a great loss due to a failed franchise it has a disastrous effect on the family."

Marks noted that franchisees are often mom-and-pop enterprises, but in this case the wives were prevented from becoming partners in the franchise — and claimed that this alleged gender discrimination turned out to be Snap-on's undoing.

"The decision has nationwide implications for all 3,400 current Snap-on dealers as well as all former dealers and their wives who claim that they were defrauded in their franchise agreement by Snap-on," said Marks, who plans to filed additional suits on behalf of wives of franchisees in New York, Florida, California, Ohio and other states.

"A jury trial offers the most objective forum for the spouses to prove their claim that Snap-on had engaged in a consistent, deliberate policy of inducing families to invest their money into a franchised tool route, when Snap-on knew that the territory contained an insufficient amount of customers or that a previous dealer had failed in that very same

route," Marks said.

In a press release Susan Kezios, president of the American Franchisee Association, said the decision means that "like other franchise companies, Snap-on will no longer be able to hide adverse decisions against it through the arbitration process."

Counsel for Snap-on did not respond to requests for comment.

The Lawsuit

Plaintiffs Nancy Casey and Maritza Franco of New Jersey charge that their husbands were duped into investing in a franchise with Snap-on.

Franco's lawsuit claims that the company makes its money by selling large quantities of tools to franchised dealers, who are usually stuck with much of the inventory because their available customer base in the franchise territory they have acquired is far smaller than they have been led to believe.

The repair shops in their area are soon saturated with tools, sales dry up and real incomes from the territories are usually far below the levels projected by regional sales managers, the suit says.

The dealer ends up borrowing money from Snap-on to finance a required purchase of inventory from the company and eventually goes out of business when he is unable to repay, Franco alleges. The company then replaces that dealer with a new franchisee who is required to buy a new inventory — the key to the "dealer churning" scheme, Franco says.

The suit charges fraudulent inducement, intentional infliction of emotional distress, negligent misrepresentation, gender discrimination and consumer fraud.

The plaintiff wives complain that although they were involved in the financial decision to commit between $25,000 and $40,000 for the franchise and about $85,000 for inventory, they were not permitted to sign the franchise agreement or have any contact with the field managers who were Snap-on's representatives.

That gender discrimination ultimately backfired for the franchisor, attorney Marks said, because it exempted the wives from the all-inclusive arbitration clause and allowed them to sue as a group.

In response to Snap-on's motion to compel arbitration, Judge Rodriguez ruled that non-signatories to arbitration clauses are not normally bound by them.

"Non-signatories cannot be bound to arbitrate unless under traditional principles of contract and agency law they are equated to the signatory of the underlying agreement," the judge wrote. "A court may only compel a party to arbitrate where that party has

entered into a written agreement to arbitrate that covers the dispute."

Judge Rodriguez also rejected the argument that the wives are barred from suing because they are beneficiaries of the agreements. That principle applies only when the third party receives some direct benefit from the contract containing the arbitration clause, the judge concluded in denying the motion.

Plaintiffs are represented by Gerald Marks of Marks & Associates in Red Bank, N.J.Defendants are represented by James McGovern Jr. of Lomurro, Davison, Eastman & Munro in Freehold, N.J.