To be an employee or not to be – that is once again the question

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Introduction

The issue of whether a franchisee is an employee or an independent contractor has been debated by both US and Canadian courts on numerous occasions. This question was once again raised in the recent Quebec Court of Appeal decision, *Comité paritaire de l'entretien d'édifices publics de la région de Québec v Modern Concept d'entretien inc.* In this particular case, the Quebec Court of Appeal examined whether Francis Bourque – an unincorporated franchisee operating a two-person cleaning services business as part of a janitorial services franchise network – qualified as an 'employee' pursuant to the Act Respecting Collective Agreement Decrees. It should be noted that the scope of the definition of employee under the act includes artisans (or workers in the English version of the act).

In order to determine the nature of the relationship between Modern Concept d'Entretien Inc (the franchisor) and Bourque (the franchisee), the court questioned which of the two parties:

- assumed the risks associated with operating the franchised business; and
- made a profit as a result of assuming said risk.

In the case at hand, the franchisor had structured a tripartite business model whereby it would enter into an initial service contract with a client with multiple locations to be cleaned, which contract would then be assigned, as to each location of the client, to that specific franchisee whose area of service included such location of the client. The court found that, despite the assignment of these service agreements to its franchisees, the franchisor remained wholly liable for the non-performance of the services under the contracts and, in doing so, assumed in practice all of the business risk of the venture. Moreover, the franchisee had little to no autonomy or power to expand its franchised business or increase profits. In light of these factors, the court ruled that the franchisee was an employee of the franchisor within the meaning of the act. In rendering its decision, the court emphasised that when analysing whether a franchisee qualifies as an employee or as an independent contractor, courts should look beyond the terms of the agreement between the parties.

Facts

The franchisor manages a janitorial services franchise network for public and quasi-public buildings in the province of Quebec. In the course of its operations, the franchisor uses a two-step business model whereby it first enters into a service contract with a client, which is then assigned, with the client's consent, to a designated franchisee by way of a franchise agreement. The franchisee is not in any way involved in negotiating the service contract between the franchisor and the client.**(1)**

In June 2012 the franchisor entered into a service agreement with the National Bank of Canada for the maintenance of its offices across Quebec. In May 2013 it concluded a substantially similar

contract with Quebec's liquor board, the *Société des Alcools du Québec* (collectively with the National Bank of Canada, the clients). Both of these contracts provided for an imperfect assignment mechanism, meaning that no novation occurred and the assignment of these contracts to a franchisee would not release the franchisor from its liability towards the clients under their respective contracts.**(2)**

In January 2014 the franchisor entered into a franchise agreement with the franchisee, which provided for the assignment of both clients' service contracts to the franchisee in respect of the clients' offices which were situated in the franchisee's territory. From January to May 2014, the franchisee performed its maintenance obligations in satisfaction of the franchisor's obligations under the service contracts.

After months of operating at a loss, the franchisee decided to terminate the franchise agreement in May 2014. Thereafter, the *Comité paritaire de l'entretien d'édifices publics de la région du Québec,* a public organisation tasked with representing maintenance workers in Quebec, applied to the Court of Quebec on behalf of the franchisee, alleging that it qualified as an employee pursuant to the Act Respecting Collective Agreement Decrees and was therefore entitled to certain unpaid wages and annual leave owed by the franchisor.**(3)**

Decisions

Court of Quebec

The Court of Quebec ruled that, although the franchisee did not participate in negotiating the initial service contracts, had little control in organising its work schedule and a considerable portion (ie, 43%) of gross sales resulting from the service contracts was retained by the franchisor in the guise of royalties and other service fees owed by the franchisee, these factors were not sufficient to establish that it was an employee of the franchisor within the meaning of the act. In the opinion of the Court of Quebec, the fact that both parties had entered into the franchise agreement for the purposes of realising a profit demonstrated that the franchisee was an independent contractor. The franchisee subsequently appealed the decision to the Quebec Court of Appeal.**(4)**

Quebec Court of Appeal

On appeal by the franchisee, the Quebec Court of Appeal reversed the decision of the Court of Quebec, emphasising that it was essential to the analysis to take into account the tripartite business model established by the franchisor. In fact, the lower court had failed to further its analysis by only considering the bilateral relationship between the franchisor and the franchisee. Accordingly, the *Comité paritaire de l'entretien d'édifices publics de la région du Québec*'s claim on behalf of the franchisee for unpaid wages and annual leave was granted.**(5)**

The court began its analysis by noting that for the purposes of the act, the relationship between an artisan and an employer does not necessarily include an element of subordination. Moreover, according to case law, a party may qualify as an independent contractor (as opposed to an employee) not subject to the act if:

- it assumes all of the risks associated with the operation of a business; and
- is accordingly compensated as such.

Consequently, these two factors guided the court in its determination as to whether the franchisee qualified as an artisan within the meaning of the act.**(6)**

In order to establish whether the franchisee met these conditions, the court went on to examine in detail the tripartite business model implemented by the franchisor. In the court's opinion, the main particularity of this model was the fact that it provided for the imperfect assignment of the initial service contracts to the franchisee. Under Quebec law, an imperfect assignment results in the assignor remaining party to the assigned agreement as co-debtor with the assignee for the obligations to be performed thereunder whereas a perfect assignment results in the assignor being replaced by the assignee and consequently released from any and all obligations towards its co-contracting party.**(7)**

In the case at hand, the court found that the assignment mechanism contemplated by the service

contracts was imperfect in nature given that the agreements expressly stipulated that, despite their assignment, the franchisor would remain entirely liable towards the clients for any potential breach of said contracts by the franchisee. In fact, the court concluded that the franchisor remaining as co-debtor was most likely an essential requirement for the clients in negotiating the service contracts given that they could exercise their rights under the service contracts against the franchisor in the event that the franchisee did not properly execute such contracts.**(8)**

As a result of this imperfect assignment, the franchisor had included various provisions in the franchise agreement granting it significant oversight over the franchisee's day-to-day operations. These monitoring mechanisms allowed the franchisor to supervise the performance of the maintenance work by the franchisee to ensure that it was not in breach under the service contracts. For example, the franchisor monitored the quality of the cleaning products used by the franchisee and required that it maintain a log book and data sheets detailing the services provided in each location it cleaned. Additionally, there was never any direct communication between the franchisee and the clients; the clients paid the franchisor directly, who then paid the franchisee. In fact, the franchisor even once reprimanded the franchisee for non-performance of its obligations by unilaterally reducing the payment owed to it which, according to the court, bolstered the franchisee's contention that it was an employee as opposed to an independent contractor.**(9)**

The court also specified that, given the amount of control exercised by the franchisor over the franchisee's business operations, their relationship did not fit within the parameters of a conventional franchise model. This was explained by the fact that the franchisor ran the risk of potentially jeopardising its relationship with the clients if it granted more autonomy to the franchisee in its performance of the service contracts.

Moreover, as a result of its intention to maintain control over the performance of the service contracts, the franchisor had contractually limited the franchisee's ability to expand its franchise business for profit. In fact, pursuant to the franchise agreement, the franchisee was generally prohibited from taking on new clients or assigning the service contracts to third parties without the franchisor's prior approval. Moreover, it reserved the right to buy back the service contracts in the event that the franchisee decided to terminate the franchise agreement.**(10)**

In light of the foregoing analysis, the court concluded that the franchisor assumed all of the business risk in connection with the service contracts with the clients and, by deducting certain royalty fees from the franchisee's remuneration (the franchisor retained an aggregate amount representing 43% of gross sales from the service contracts for royalties and other service fees), was compensated for assuming such risk. The court therefore ruled that the franchisee qualified as an employee pursuant to the act.**(11)**

It is, however, important to note that the Quebec Court of Appeal's decision was not unanimous. In his opinion, the dissenting judge agreed with the lower court's ruling that the intention of the parties should be determinative of the analysis and that in the case at bar, it was the parties' intention to enter into a mutually beneficial franchise agreement for profit as opposed to an employment contract.**(12)**

On 17 May 2018 leave to appeal to the Supreme Court of Canada was granted.**(13)**

Comment

The Quebec Court of Appeal's ruling in this decision may worry certain franchisors, but there are a number of mitigating factors to consider. The impact of this decision outside Quebec may be limited considering the fact that the franchisee's status as an artisan (and consequently an employee) or an independent contractor was discussed by the court within the context of this unique definition of an employee under the Act Respecting Collective Agreement Decrees.

Moreover, this decision was based on the franchisor's implementation of an unconventional tripartite franchise business model whereby the franchisor contracts directly with the franchisee's clients, without the involvement of the franchisee, accompanied by controls, rights and remedies that greatly exceeded those typically found in most franchise relationships. Another distinguishing characteristic was that the franchisee in this case was unincorporated.

In light of this decision, franchisors who may be tempted to use comparatively disproportionate measures of control should err on the side of caution. In particular, franchisors should aim to circumscribe the ways in which they exercise control over their franchisees' daily operations and avoid restricting their franchisees' ability to seek out new clients for their franchised business.

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Endnotes

(1) *Comité paritaire de l'entretien d'édifices publics de la région de Québec v Modern Concept d'entretien inc*, 2017 QCCA 1237, paragraphs 100-102.

(2) *Comité paritaire de l'entretien d'édifices publics de la région de Québec c Modern Concept d'entretien inc*, 2016 QCCQ 1789, paragraphs 9-14.

(3) *Comité paritaire de l'entretien d'édifices publics de la région de Québec v Modern Concept d'entretien inc*, 2017 QCCA 1237, paragraphs 112-117.

(4) *Comité paritaire de l'entretien d'édifices publics de la région de Québec c Modern Concept d'entretien inc*, 2016 QCCQ 1789.

(5) *Comité paritaire de l'entretien d'édifices publics de la région de Québec v Modern Concept d'entretien inc*, 2017 QCCA 1237, paragraphs 173-174; 263.

(6) *Ibid*, paragraphs 136-144.

(7) *Ibid*, paragraphs 145-150.

(8) *Ibid*, paragraphs 151-161.

(9) *Ibid*, paragraph 106.

(10) *Ibid*, paragraphs 115; 196-197; 201.

(11) *Ibid*, paragraphs 108; 178-207.

(12) *Ibid*, paragraphs 1-90.

(13) *Modern Concept d'Entretien inc v Comité paritaire de l'entretien d'édifices publics de la région de Québec*, 2018 CanLII 43777 (SCC).
