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Protecting Your Brand and Networks during COVID-19: Practical Steps for Brand Owners Relying on Independent Contractors

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This article is for brand owners (franchisors, suppliers, licensors) that rely on authorized brand users (franchisees, distributors, dealers, licensees) to operate businesses identified by the brand name that distribute the specific goods or services that the brand owner designates or supplies. Below is a collection of best practices to assist brand owners, their authorized independent operations and their employees during the COVID-19 pandemic.

Be Your Brand's Spokesperson

Your brand will be remembered for the messages you send to your employees, independent contractors, suppliers, and customers during the worst of times. Put the human response first. Make your brand message transparent and authentic to your brand's core values. As COVID-19 spreads to new epicenters in the United States, be ready with a regionalized brand message. Because local media may want to interview your local brand users, arm them with talking points.

Downside Projections

By now, you should have downside financial models (30, 60, 90 day) in place carefully scrutinized by your CPA that identify your cash flow needs. You should have evaluated your eligibility for government loan programs if your own business is closed or adversely affected. If you secure a Payment Protection Plan (PPP) loan, use the proceeds to keep employees on your payroll and pay your rent, but plan ahead for after the end of the first 8 week "forgiveness" period. Identify the need for future furloughs or layoffs and negotiate with landlords for rent adjustments or abatements to begin then. Contact the banks with which you have established relationships to identify available lending or loan reduction, abatement periods and other relief. Help your licensees do their own financial models, encourage them to apply for PPP loan assistance, and tap their banking relationships. Share financial modeling tools or encourage them to speak with their CPAs. Knowledge is the best antidote to panic.

Closures

Given the interdependence between licensee sales and royalty fees, your licensees' economic pain and uncertainty is your enterprise's own economic pain and uncertainty. The extent of economic uncertainty that your network may face directly correlates with the business you are in and where you operate. Across the United States, public health orders have closed nonessential businesses and differ in how they define "essential." At the time of this article's publication, some states or cities are slowly reopening, not with the light switch speed that some imagined at the start of the national emergency, but generally in a slow, controlled manner. There is no one-size-fits-all when it comes to addressing closures and the impact of these closures on your licensees' businesses. Some licensees may resist reopening until consumers display confidence in being able to remain personally safe while shopping, dining out or engaging with service businesses like hair salons and gyms. Prepare to be patient.

Doing the "right thing" by your independent operators, however, does not mean risking your company's viability as the brand owner. As the brand owner, you need to keep your own lights on so that you are available to your entire network. To accomplish this, you will need to reorganize priorities: consider trimming your own staff and salaries and dispensing with nonessential services, for example.

It is important to consider different approaches to provide financial support for your licensees. For example, two of the largest franchisors without immediate liquidity concerns, Taco Bell and KFC, have announced a 60-day grace period on royalty fees: April and May's royalties are now due in June, interest-free. This, of course, is the exception, but it can be wise to be creative and flexible. With the priority of keeping the greatest number of licensees financially viable, many other brands are deferring, but not waiving, percentage royalty fees. The deferral period varies. In addition, brand owners with minimum royalty fees are waiving them for a specific time interval, then reevaluating whether to extend the time period.

Brand owners should look beyond royalty fees, however. If you sell products to your licensees for their use or resale, consider reducing prices or using their markup for the short term to help their licensees stay open. Transparent messaging means telling your brand users that price reductions are temporary.

Closures may also affect your supply chain as manufacturing plants may be forced to shut down. Being nimble means identifying alternative suppliers, if possible, where a substitution does not sacrifice your brand's core value. Some branded outlets may want to close even if they are not in a geography where local government mandates this. Be understanding of these requests and work with your licensees; you want them to remain good brand ambassadors during this crisis.

To avoid closures, help your franchisees negotiate rent reductions, deferrals, and free rent periods. Landlords may expect something in return, such as an agreement to extend the lease. If this happens, let your licensee know you will extend the current license agreement for an equal period of time.

Finally, if you or a franchisee are considering layoffs, be sure to consult with an employment attorney. You'll need to consider federal and state laws regarding time periods for notice to employees; some states have temporarily relaxed their rules.

Taking on New Brand Users

Some essential businesses (*e.g.*, grocery stores; restaurants with well-established take-out and delivery service) are experiencing heightened demand and may be tempted to onboard new branded outlets and sign on new licensees. This, however, is rare as most brand owners have put expansion plans on hold and are not awarding new licenses.

Renewals in the Pipeline

If your existing licensee is eager to re-up their commitment, there is no need to put them on hold. On the other hand, if you have licensees up for renewal that are unsure if they can remain financially viable, offer to extend their current franchise agreement for another 90 days. They will be grateful.

Transfers in the Pipeline

If your licensees are in the midst of selling their businesses, their deals may crater soon (if not already). Transitioning ownership of an existing licensee-owned business to someone new to your franchise system may be impossible to accomplish with restrictions on travel, social distancing, and risks of community contagion.

Training may be physically impossible other than virtual or remote training, which may be ineffective for teaching important operating skills. During the current national emergency, it would not be unreasonable to withhold consent to a transfer unless the selling licensee remains financially and operationally responsible for the business for a period of time after the pandemic ends.

FDDs and Renewal Filings (for Franchisors)

There is a little good news for franchisors looking at looming deadlines for completing franchise disclosure document (FDD) updates and renewal filings: several states have already extended filing deadlines by 90 days. The International Franchise Association has worked with the FTC and state franchise agencies to extend the remaining deadlines. Best practice, however, is not to allow your existing registrations to lapse; doing so may result in the state franchise agency treating your next filing as an initial franchise registration application and subjecting your FDD to much stricter vetting and higher filing fees. Complete FDD fiscal year-end updates and renewal filings within the extended deadlines just as a placeholder even if you do not plan on resuming new franchisee recruiting for some time.

In addition, fiscal year-end updates need to speak as of the last day of your last fiscal year, which for most companies is December, 31,2019, before COVID-19 arrived in the United States. Consequently, when we emerge from the pandemic, your FDD will need to reflect any material changes in your financial condition, outlet count and other potential disclosures attributable to this crisis.

Financial Performance Representations—Item 19 (for franchisors)

If you plan to use your updated FDD during these uncertain times, consider removing Item 19 financial performance representation (FPR) as they may no longer meet the *reasonable basis* legal standard even if they accurately reflect pre-pandemic operating data. When we turn the corner on this pandemic and sunshine lights the end of the tunnel, the FPR that you add back to your FDD may not look the same as the current one.

Joint Employment Legal Risks

Directing your licensees and their employees to comply with CDC and World Health Organization (WHO) protocols will not expose you to joint employment legal risks. If you issue directives specific to your business model that are not addressed by the CDC or WHO, frame these directives as brand standards.

> Don't be afraid to answer your licensees' questions on what they should be doing vis-à-vis their employees by framing your advice according to what you're doing within your own organization or by sharing what you regard as the best practices among other licensees.

Third-Party Resources

Besides the CDC and WHO websites, there are many excellent resources specific to the industry in which your brand operates providing up-to-date information, to which you can link your website. For brand owners, the International Franchise Association has an excellent website (*https://www.franchise.org/*) with material relevant to brands that utilize independent contractors (even if you are not a franchisor!). Talking about COVID-19 on your company's landing page communicates a proactive response to your stakeholders, which can differentiate your brand from your competitors and deliver comfort to your customers. A recent Harvard Business Review article (*see https://hbr.org/2020/03/how-chinese-companies-have-responded-to-coronavirus*) about how Chinese companies are responding to COVID-19 also offers insight into what the other side of the pandemic may look like in the United States.