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# INCREASED FRANCHISING OPPORTUNITIES FOR MINORITIES: SOME LEGAL OPTIONS

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ONE OF THE MOST significant lags in the movement toward full economic equality in the United States has, strangely enough, come at a time when notable gains are being made in equal employment opportunities for minority employees. The literature of the law and business journals is replete with the treatment of equal *employment* opportunities for blacks and other racial minorities as the central thrust of the issue of full economic equality.<sup>1</sup> Indeed, the primary thrust of reform in this area was centered around the 1964 Civil Rights Act.<sup>2</sup> But this statute regarded equality in terms of employment rather than

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<sup>1</sup> See, e.g., Caldwell, *Discrimination and Fair Employment Practices*, 16 LAB. L.J. 394 (1965); *Civil Rights Symposium*, 43 U. DET. L.J. 161 (1965); *Conference Issue Toward Equal Opportunity in Employment*, 14 BUFFALO L. REV. 1 (1964); Luthans, *The Impact of the Civil Rights Act on Employment Policies and Programs*, 19 LAB. L.J. 323 (1968); *Management, Unions and Minority Groups: A Symposium*, 17 N.Y.U. CONFERENCE ON LABOR 95 (1964); Rosen, *Law and Racial Discrimination in Employment*, 53 CALIF. L. REV. 729 (1965); Note, *Racial Discrimination in Unions*, 38 TEMPLE L.Q. 311 (1965); Note, *Employment Discrimination: State FEP Laws and the Impact of Title VII of the Civil Rights Act of 1964*, 16 W. RES. L. REV. 608 (1965).

<sup>2</sup> Civil Rights Act of July 2, 1964, Pub. L. No. 88-352, 78 Stat. 241.

in terms of the fuller economic equality resulting from the direct ownership of one's own business.

Comments from the usual liberal sources demonstrated this rather incomplete view of equality that was evident from the interpretations of the Civil Rights Act of 1964. It was a view that designated inadequate manpower use as the principal source of economic distress of blacks and other American minorities. Commentators in the *University of Detroit Law Journal* said that

[t]he single most important problem—the overriding issue—among this set of difficulties which Negroes and other minorities face is clearly that of economic security. All observers are agreed that jobs are crucial to the solution of all other educational, housing and family stability problems. In the writers' judgment what is needed to spearhead the drive called for by President Johnson "to end the one huge wrong of the American nation" is a national civil rights manpower policy designed to close the gap between Negro-White unemployment rates, job patterns and income levels.<sup>3</sup>

However, if black Americans and other minorities are ever to obtain full equality within this society, if they are going to be afforded the opportunity to develop and to use all of their capabilities, particularly in the economic arenas, then every avenue of employment—including self-employment—must be made available. We must broaden the focus of our attention, expand it beyond mere jobs, so that opportunity will be full opportunity.

<sup>3</sup> Field & Mister, *Civil Rights, Employment Opportunity and Economic Growth*, 43 U. DET. L.J. 235, 236-37 (1965).

This is not to say that black ownership or black capital has been totally ignored. In fact, it has been the fodder of several notable political campaigns. There has even been a great deal of verbal attention given to the concept of black ownership of business concerns. Nevertheless, the fact remains that "private industry has been inadequately responsive in taking the initiative to ease the economic problems of minority Americans."<sup>4</sup> And as private industry has devoted merely minimal attention, so too have the governments, federal, state and local. The more complete meaning and force of economic equality exposes this inattention as indefensible. As Dean Clarence Ferguson of the Howard University School of Law has noted,

it now seems clear to most perceptive observers that what is truly involved in the civil rights revolution is a fundamental remaking of the entire American society. The removal of race as a relevant factor in the employment relations must inevitably drastically alter the structure and dynamics of our economic order.<sup>5</sup>

We cannot expect only some avenues toward equality to be opened without pursuing all avenues. In short, we cannot expect the labor unions alone to bear the economic burdens of desegregation. Businessmen must also promote the activities of all Americans, black and white, as owners and operators within the American capitalist system.

<sup>4</sup> Harris, *Franchising for Minorities: An Avenue into the Economic Mainstream*, 3 CIV. RIGHTS DIG. 33 (1970).

<sup>5</sup> Ferguson, *The Federal Interest in Employment Discrimination*, 14 BUFFALO L. REV. 1 (1964).

One method of engaging businessmen in this enterprise involves the designation of minority group members as franchise holders. Franchising involves a continuing business relationship "in which a franchiser provides a licensed privilege to do business, plus assistance in organizing, training, merchandizing, and management in return for a consideration from the franchisee."<sup>6</sup>

Ideally stated:

The system gives the individual a chance to become an independent businessman under the most favorable circumstances. The small businessman receives the benefits of publicly-accepted, prestige products and expert managerial assistance from the supplier. Combining tested business methods with minimal capital costs enables the franchisee to operate on terms more equal to those of his larger integrated competitors. And, in some instances, the franchisee may receive financial help from the supplier on more favorable terms than are otherwise available.

The franchisee remains an independent businessman with his own capital investment in facilities. Usually, however, he is closely associated with the supplier. He is prominently identified with the supplier's good will, trademark, and distinctive business methods. And he is encouraged to follow quality and promotional controls tested and developed by the supplier.<sup>7</sup>

Franchises are becoming an increasingly popular marketing vehicle in the United

States. They rose in popularity just after World War II; franchises such as McDonald's, Dunkin' Donuts, AAMCO Transmission Centers, Kentucky Fried Chicken and Sheraton Motor Inns are some of the more notable and successful. These have been joined by the rapid addition of franchises bearing such celebrity names as Minnie Pearl's fried chicken chain, Johnny Carson's roast beef restaurants, Broadway Joe Namath's taverns and Pat Boone's automotive diagnostic centers. This new development has in fact been called "The Great Franchising Game."

The tremendous growth of franchise operations, which are mainly small businesses, was recently publicized at hearings conducted in January, March and April of 1970 by the Small Business Subcommittee on Urban and Rural Economic Development. In his opening notes Senator Harrison Williams remarked that

franchising now accounts for about \$90 billion in annual retail sales, or about 10% of our gross national product. Today, over 1,000 different franchisers are operating throughout the U.S. These franchisers have licensed approximately 600,000 franchises, mostly small business.<sup>8</sup>

As a result of the hearings, several senators and a large portion of the public have become convinced that some federal control of franchising is necessary. The suggestion for governmental reform has run the gamut of the franchising operation. Indeed, as we shall note later, even the gathering of trustworthy statistics to mark the dimensions of the franchising operation

<sup>6</sup> U.S. DEP'T COMMERCE, BUSINESS AND DEFENSE SERVICES ADMINISTRATION, *FRANCHISING COMPANY DATA FOR EQUAL OPPORTUNITY IN BUSINESS* viii (1969).

<sup>7</sup> J. ATKINSON, *FRANCHISING THE ODDS-ON FAVORITE* vi (1968), quoting SPECIAL REPORT OF THE CHAMBER OF COMMERCE OF THE UNITED STATES (1968).

<sup>8</sup> *Franchising Goes on the Griddle*, BUS. WEEK, Jan. 3, 1970, at 15.

has been and continues to be an impossible task. It has been suggested, therefore, that a federal depository, housed in either the Federal Trade Commission's Bureau of Economics or the Bureau of the Census, be created to gather and distribute statistical information on franchising. Additional testimony offered to the subcommittee criticized the advertising techniques of franchisee solicitation and the unfair provisions of certain franchise agreements. The proposed solution would require the full disclosure of franchise agreements through the filing of franchise registration statements with the federal government.

The devastating criticism of the limited participation by minorities in franchising highlighted an issue that had been virtually ignored. The criticism was directed at the total character of minority participation, but more specifically touched on the amount of participation as well as the terms under which that participation arose. Although the criticism was directed pri-

marily at governmental and business attitudes toward minorities, some of that criticism is capable of legal solution.

The first objection concerned the amount of blacks and other minorities participating in the franchise operation. In fact, franchising is a very large, multi-billion dollar operation. Its three largest components are auto dealers, food stores—grocery and restaurant—and gasoline service station dealers. The table below demonstrates the national scope of the enterprise.

Yet, as previously noted, even these figures are not totally reliable. As Senator Williams said:

One of the things we discovered very early as we began to develop the hearings is the difficulty in arriving at reliable statistics in this burgeoning industry of franchising. Now just the dollar figure of annual business, last week early, I heard the figure of \$60 billion in franchise business. Later on that week it was described as an \$80 billion business. I think Monday of this week

#### THE FRANCHISE INDUSTRY

Franchised Groups	1967 (in 000,000)	Percentage of Franchise Industry	Number of Outlets
Auto and Truck Dealers	\$44,043	49.4	27,774
Gasoline/Service Stations	15,884	17.8	224,000
Tire/Auto Parts Suppliers	11,500	12.9	110,000
Soft-Drink Bottlers	2,560	2.9	4,000
Motel/Hotel/Travel Inns	2,150	2.4	3,850
Convenience Grocery Stores	5,720	6.4	20,800
Drive-in Food/Drink/Ice Cream	4,048	4.5	31,420
Moving Companies	1,100	1.2	5,350
Auto Transmission Parts	810	0.9	8,600
Coin Operated Laundry/Dry Cleaning	620	0.7	41,600
Water Conditioning Services	231	0.3	2,950
Temporary Help Services	135	0.1	650
Carpet/Upholstery Cleaners	107	0.1	4,150
Hearing Aids	75	0.1	3,750
Swimming Pools	55	0.1	1,300
Totals	\$89,230	100.0	512,644

SOURCE: J. ATKINSON, *FRANCHISING: THE ODDS-ON FAVORITE 5* (1968).

someone that I rely on this staff, I think it was Mr. Ford, told me it was a \$90 billion business. Now you have hiked this to \$100 billion. Where do these statistics come from?<sup>9</sup>

These statistics aside, the lack of minority participation remains apparent. At the close of 1969, of almost 30,000 automobile dealers, only 24 were operated by blacks.<sup>10</sup> This is participation rate of .08 percent. According to Dr. Charles L. Vaughn, of the Center for the Study of Franchise Distribution of Boston College, in a study of 136 fast food franchises in six categories of restaurants, with 16,000 franchises, only 45 were owned by Negroes and 33 by Spanish-Americans—about 0.5 percent of the total.<sup>11</sup> In fact, the total of minority owned franchises in the United States has been estimated at only slightly over 300; there are more than one-half million franchise outlets in operation today.<sup>12</sup> In testimony before the Senate Banking and Currency Committee, Philip F. Zeidman, former Special Assistant to the Administrator of the Small Business Administration during the Johnson Administration, summarized the situation: “[T]here can be no denying that black Americans have simply not yet developed anything ap-

proaching an entrepreneurial tradition, and have not yet assumed anything approaching the proportionate share of the business of the nation.”<sup>13</sup> Moreover, there can be no doubt that blacks regard franchising as beneficial. Jackie Robinson, Vice President of Sea Host Inc., a New York City based franchise company, has said that

[t]he franchise industry can be a big saver for minorities, as most of us recognize who have had little if any experience in business. Our group needs the training, we need the accounting advice, the legal advice, and certainly we need the continuing support. A sincere, dedicated parent company can aid immensely in the growth and development of a business.<sup>14</sup>

Despite the benefits that would accrue to the entire nation as a result of an increase in black and minority franchising, there are some very substantial obstacles to overcome. Indeed, a second objection has been directed at the failure to provide for a significant number of minority franchisees after desegregation was achieved.

The most serious obstacle is the hesitancy of businesses to go beyond the token stages in providing for black and minority participation. For example, until last year only eight out of approximately 1,150 McDonald's franchises were owned and operated by Negroes. After a two month economic boycott and picketing of four McDonald's restaurants located in black

<sup>9</sup> *Hearings Before the Subcomm. on Urban and Rural Economic Development of the Senate Select Comm. on Small Business*, 91st Cong., 2d Sess., pt. 1, at 252 (1970) (testimony of Senator Harrison Williams) [hereinafter *Williams Committee Hearings*].

<sup>10</sup> Statistics quoted to co-author Dr. Philip Harris by the editor of the *Civil Rights Digest*.

<sup>11</sup> Letter from Dr. Charles L. Vaughn to Dr. Philip Harris, Oct. 14, 1969.

<sup>12</sup> *Williams Committee Hearings* at 252 (testimony of Abraham S. Venable).

<sup>13</sup> *Hearings Before the Subcomm. on Small Business of the Senate Comm. on Banking and Finance*, 91st Cong., 1st Sess., pt. 1, at 156 (1969) (testimony of Philip G. Zeidman).

<sup>14</sup> *Williams Committee Hearings* at 185 (testimony of Jackie Robinson).

neighborhoods of Cleveland, the company consented to turn over these four restaurants to a coalition of black groups. Special financing arrangements were made but only after the economic threat had been exercised and considerable animosity fostered.

On the McDonald's fiasco, Brady Keys, former professional football player and now president of the All-Pro Chicken Company, a franchise network, said: "We may take this opportunity to declare that for the economic franchise programs as they relate to black America, [they have] been more of a boondoggle than a boon for small business and blacks in our minority areas."<sup>15</sup> He further declared that the affair had demonstrated

the inability, unwillingness, and inaction presently on the part of the industry to embark on a real and meaningful inclusion of blacks in the ownership of major franchise contracts, realities of the tight money situation and how it affects the initiation of these projects, [and] the inability of government to perform or adequately deal with the problems.<sup>16</sup>

It would be unfair to indict all American enterprise; some corporations have been willing to assist in insuring the success of Negro owned franchises. International Industries, a restaurant franchiser has, for example, invested \$150,000 of corporate funds to sponsor, along with the Small Business Administration and the Minority Enterprise Office of the Department of Commerce, a proposal for small business

investment companies to aid minority business. Nevertheless, the amounts involved have been small, the effectiveness has been too inconsequential to measure, and the enthusiasm has been too isolated from the usual corporate attitudes in this area. It is not sufficient to rely upon the business sector alone as a source of minority franchising opportunities and not insist that the federal government play a more active role in insuring increased participation. In one sense, the pattern of restricted black ownership definitely suggests some pattern of conscious segregation, not unlike that ruled unlawful in statutes dealing with education, housing and employment. It therefore presents an opportunity for government action to compel business not having a representative number of minority franchises to reorganize their methods of operation so as not to exclude blacks and other minorities—either consciously or through a pattern having the same effect. This is suggested as the first legal remedy that would be available, but not first in terms of government priorities. Seemingly the days of government action in the courts to compel observance of civil rights laws by businesses having national operations have long since passed. However, the Government could effectively pursue more positive approaches to insure sufficient participation by members of minority groups. In short, government programs ought to be more affirmative in terms of encouraging the participation of black Americans.

One important facet of governmental policy is financial assistance. Minority citizens have been frustrated by the requirements of and the limited assistance in

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<sup>15</sup> *Id.* at 305 (testimony of Brady Keys).

<sup>16</sup> *Id.*

securing funding, and the current tight money situation has further inhibited their efforts. Therefore, there is a need for coordination between government agencies such as the Small Business Administration, and the banks to insure that loans are available, and available in sufficient amounts. The difficulty in obtaining funds was expressed by Brady Keys before Senator Williams' subcommittee:

SENATOR SPARKMAN. What has been your experience as a minority entrepreneur with the local banks in the localities where you operate?

MR. KEYS. Let me start back at the beginning and bring you up to now what has been my experience. When I tried to open my first store, I had just finished playing the Pro Bowl, which meant I was an all-pro football player. I was just about at the top of my career. I had a double A credit rating, a little money in the bank, but I was completely and totally unable to get a loan of \$5,000. That should give you an idea how the banks treated me.<sup>17</sup>

Even with a successful operation, Keys indicated his inability to borrow money from local banks; he finally realized success with the First National City Bank of New York.

The Government should consider two methods of raising more revenue for minority franchisees. The first involves a more coordinated system of information between government and banks. All too often the problem is one of getting the two parties together and preparing for the conduct of business. It has been said that

one area of frustration very frankly has

been in the area of minority lending. The black man cannot, with standing in front of a big oak desk of a banker and getting his three turndowns, so that he then can apply to the SBA. He gets discouraged too quickly.<sup>18</sup>

The Small Business Administration requires these three attempts at private sources before it will consider the applicant. Concerning the need for government cooperation, the same speaker noted that

[w]e have got to get the SBA to say "See Mr. Jones at the Smith Bank in downtown Paducah and he will help you," and have it moved along the line in an expeditious manner, so that we can build the confidence of this black man, and not continually move through a morass of frustration. We are trying and I know they are. We have not given up the ship.<sup>19</sup>

A second method of increasing the availability of capital is to provide incentives for banks to make loans. Various incentive forms such as veterans loans, student loans, housing loans and others have been used for other purposes. The incentives have included government funds from which money is drawn, government guaranteed loans to encourage banks to lend money without risk of failure, and government provided interest rate subsidies to guarantee a more favorable return to the lending institution. At this stage in the development of franchise business, it is too soon to measure the effectiveness of these alternatives. Furthermore, the effectiveness of these solutions might not be restricted to

<sup>17</sup> *Id.* at 306.

<sup>18</sup> *Id.* at 272 (testimony of Al Lapin, Jr.) (wording original).

<sup>19</sup> *Id.*



minority franchisees. The encouragement of individual enterprise throughout society is the appropriate goal of government. In any event, these programs ought to be seriously considered. Until we get a more accurate picture of the franchising operation, however, the possibilities for serious consideration of these alternatives by legislators in Washington remains bleak.

Although the availability of money is probably the most serious problem facing minority franchisees, it is not the final one. Once money is obtained, the problems of managing it and the business become critical to the franchise holder. As noted previously, very often the franchisee is a novice, completely reliant upon the franchiser for assistance in commencing business. The program for training franchisees, moreover, can vary in quality to the point of being unsatisfactory. In fact, widespread criticism of these training programs has been a focal point of reforming interests in the franchise operation. And for the minority franchise holder the need for adequate training is even more crucial. This man requires training in areas such as accounting procedures, legal matters, or management practices in general. Several counseling programs conducted at graduate schools of business, such as Columbia University, have demonstrated their usefulness and effectiveness. It has been said, with due reflection, that

if franchising, as a system, is to succeed as an economic vehicle for minorities, it is imperative for all those interested to stress the significance of minority training. This training is much more difficult and elusive than establishing standards for financing and contractual arrangements. Relatively

few franchisers have more than a superficial training course.<sup>20</sup>

Considering the limited assistance that has been given by the Small Business Administration, there has been a great deal of careless use of that assistance. Money has been given to applicants virtually without regard to the training programs offered by franchisers. And in addition to insuring an adequate initial training program, there should be some assurance of continuing business counsel. Seemingly, therefore, there is room for a government role in the development of management training programs for minorities. As Dr. Israel Unter- man has recognized "few businessmen would argue against a management training program for minorities. Yet, without federal legislation such training may be limited to relatively few franchisers."<sup>21</sup>

Further encouragement for minority franchising can be drawn from the cooperation of state and local tax authorities. Many states have realized the benefits that can accrue to the state and the communities of the state through the introduction of large plants and factories into their areas. The spread of municipal industrial revenue bonds in the 1960's represented a tremendous commitment of public money to the development of industry. And it was, from the standpoint of those communities, quite beneficial. It is now imperative that state and local communities recognize the advantages of locally owned small businesses within their communities. Con-

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<sup>20</sup> *Id.* at 652 (testimony of Dr. Israel Unter- man).

<sup>21</sup> *Id.* at 653.

sideration of deferred tax formula would demonstrate their interest in attracting small business. This can be done in the area of realty taxes as well as the usual business taxes.

Beyond mere adjustments in the tax burden, some notion by state and local government of the importance of minority investment in the community is required to assist the move toward full economic equality. An example of the positive contribution that can be made by local government was cited by the Commissioner of Commerce and Industry of the City of New York. His department planned a two-day franchising workshop for potential minority franchise holders. Although advised that the program would be of minimal success, he indicated that

the results went beyond our expectations by several orders of magnitude. More than 500 potential businessmen attended and at the present time, more than 12 deals are made or pending. Importantly, the fran-

chisers had their eyes opened to the surprising levels of skill and motivation in our minority community.<sup>22</sup>

Undoubtedly, there is a tremendous need today—from the standpoint of the total community and from the standpoint of minorities—to encourage minority franchising. The need has been recognized almost unanimously; the satiation of that need, however, is a task that requires cooperation from many components of society, not the least important of which is government. And for government many roles are appropriate. It can assist in increasing the number of minority franchises, in providing funds to assist the small businessman and in increasing the availability of technical assistance programs for the franchise holders. In so doing, a great deal of benefit could accrue to a great many people.

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<sup>22</sup> *Id.* at 646 (testimony of Kenneth Patton)