Monitoring Costs and the Law of Franchise Tying Contracts: A Behavioral Perspective

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ABSTRACT

The traditional law-and-economics analysis suggests that the per se illegality rule that governs franchise tying contracts is inefficient. Legal economists particularly argue that a per se illegal standard fails to account for the enhancement in efficiency that a franchise tying contract provides. One central improvement in efficiency that a franchise tying contract creates, according to legal economists, is a decrease in the franchisor's monitoring costs. Particularly, by requiring a franchisee to purchase products directly from the franchisor, a tying contract reduces the costs that the franchisor will have to incur in order to monitor the quality of products sold by the franchisee to customers.

Building upon a noteworthy body of empirical research, this article will argue that the traditional law-and-economics analysis is incomplete. Although a franchise tying contract may reduce product quality-related monitoring costs, it is also likely to significantly increase other monitoring costs.

More specifically, this article will argue that a centralized franchise tying relationship is likely to continually constrain the franchisee's autonomy. Consequently, the tying relationship is likely to decrease the franchisee's satisfaction with the relationship. The emotional experience of decreased satisfaction is likely to promote aggressive retaliatory behavior, which may take the form of franchisee opportunistic behavior. Ultimately, a centralized tying relationship will increase the likelihood that the franchisee will take three central types of opportunistic actions towards the franchisor: manipulate information, shirk the contractual obligation to provide adequate customer service and shirk the contractual obligation to maintain cleanliness standards in the entire franchise unit. These potential opportunistic actions, as they accumulate, are likely to significantly increase the franchisor's information, customer-service and cleanliness-related monitoring costs, thereby off-setting the product-quality monitoring cost savings arguably generated by a franchise tying contract.

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INTRODUCTION

The use of a tying contract – that is an agreement under which the seller agrees to sell a product to a buyer, but only on the condition that the buyer also purchases a different product from the seller – has become a common phenomenon in the franchise industry.[1] Frequently, franchise agreements, labeled as 'franchise tying contracts,' require a franchisee to purchase products from a franchisor or a designated supplier as a condition of receiving the franchise license.[2] To illustrate, pizza franchisors often license their franchisees on the condition that the franchisees buy dough, tomato sauce and paper cups exclusively from the franchisor, or from approved suppliers.[3] Similarly, fried chicken franchisors frequently require their franchisees to purchase cookers, fryers, packaging supplies, and napkins from the franchisor.[4] Likewise, ice cream franchisors occasionally tie the purchase of their ice creams to the sale of their trademark.[5]

For the last few decades, one of the most vital debates in the field of franchise antitrust law has focused on one question: whether franchise tying contracts should be legal or illegal *per se*. On the one hand, courts have generally adopted a hostile attitude toward tying contracts.[6] Tying contracts are considered by courts as *per se*

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1 On average, about 30 percent of franchisors use tying contracts; *See*, ROGER D. BLAIR & FRANCINE LAFONTAINE, THE ECONOMICS OF FRANCHISING 140 (2005); Steven C. Michael, *The Extent, Motivation, and Effect of Tying in Franchise Contracts*, 21 MANAGE. DECIS. ECON. 191, 194 (2000).

2 Warren S. Grimes, *When Do Franchisors Have Market Power - Antitrust Remedies for Franchisor Opportunism Perspectives on Franchising*, 65 ANTITRUST L.J. 105, 142 (1996).

3 *See, e.g.*, *Queen City Pizza v. Domino's Pizza*, 124 F.3d 430, 433 & 438 (3d Cir. Pa. 1997).

4 *See, e.g.*, *Siegel v. Chicken Delight, Inc.*, 448 F. 2d 43, 46 (9th Cir. Cal. 1971). *See also Kentucky Fried Chicken Corp. v. Diversified Packaging Corp.*, 549 F.2d 368, 373 (5th Cir. Fla. 1977).

5 *See, e.g.*, *Krehl v. Baskin-Robbins Ice Cream Co.*, 664 F.2d 1348, 1351 (9th Cir. Cal. 1982).

6 Roger D. Blair and Jeffrey Finci, *The Individual Coercion Doctrine and Tying Arrangements: An Economic Analysis*, 10 FLA. ST. U.L. REV. 531, 531 (1983); BLAIR & LAFONTAINE, *supra* note 1, at 143.

illegal.[7] As Justice Scalia explained, "the per se rule against tying is just such a rule: Where the conditions precedent to application of the rule are met, i. e., where the tying arrangement is backed up by the [seller's] market power in the "tying" product, the arrangement is adjudged in violation of § 1 of the Sherman Act".[8] This *per se* illegal standard is mainly based on an anticompetitive rationale, known as the 'leverage theory,'[9] that a franchisor might use economic power in the franchise license market to restrain trade in the tied good market.[10]

On the other hand, traditional law-and-economics analysts have opposed the *per se* illegality rule.[11] Legal economists believe that a *per se* illegal standard fails to account for the improvements in efficiency that a franchise tying contract creates.[12] One central improvement in efficiency that a franchise tying contract creates, according to legal economists, is a decrease in the franchisor's monitoring costs.[13] In short, legal economists suggest that, typically, each franchisee has an incentive to free-ride on the

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7 *See, e.g.*, *Eastman Kodak Co. v. Image Tech. Servs.*, 504 U.S. 451, 487 (1992); For a review of the Supreme Court's rulings endorsing the *per se* illegality rule *see*, BLAIR & LAFONTAINE, *supra* note 1, at 143; The '*per se* rule' is also subject to certain defenses, which are described in Robert T. Joseph & Lee N. Abrams, *Antitrust Law*, in FUNDAMENTALS OF FRANCHISING (Rupert M. Barkoff and Andrew C. Selden, eds., 3rd ed. 2008).

8 *Eastman Kodak Co. v. Image Technical Servs.*, Inc. 504 U.S. 451, 487.

9 For other concerns on which the hostility of the courts to tying contracts is based, *see*, *Fortner Enterprises, Inc. v. United States Steel Corp.*, 394 U.S. 495, 513-514, 22 L. Ed. 2d 495, 89 S. Ct. 1252 (1969); *Eastman Kodak Co. v. Image Tech. Servs.*, 504 U.S. 451, 487 (1992).

10 *Times-Picayune Publ'g Co. v. United States*, 345 U.S. 594, 611 (1953) ("[T]he essence of illegality in tying agreements is the wielding of monopolistic leverage; a seller exploits his dominant position in one market to expand his empire into the next"); for criticism on the leverage theory *see, e.g.*, RICHARD A. POSNER, ANTITRUST LAW 198-199 (2nd ed. 2001); Ward S. Bowman, Jr., *Tying Arrangements and the Leverage Problem*, 67 YALE L.J. 19 (1957). For a reply to the critique, *see, e.g.*, Louis Kaplow, *Extension of Monopoly Power Through Leverage*, 85 COLUM. L. REV. 515 (1985); Warren S. Grimes, *Antitrust and the Systematic Bias Against Small Business: Kodak, Strategic Conduct, and Leverage Theory*, 52 CASE W. RES. 231, 253 (2001).

11 See *infra* Part I.

12 Blair & Finci, *supra* note 6, at 531.

13 See *infra* Part I. For other potential economic rationales for tying contracts, *see generally*, Benjamin Klein, *Tying*, in 3 THE NEW PALGRAVE DICTIONARY OF ECONOMICS AND THE LAW 630, 631-4 (Peter Newman ed., 1998).

business efforts of the franchisor and other franchisees, and particularly, to cut costs and supply less than the desired level of product quality.[14] A franchise tying contract, however, can decrease the likelihood of supply of low-quality products by a franchisee by requiring the franchisee to purchase products directly from the franchisor. The free-riding reduction attained by a franchise tying contract is likely, in turn, to reduce the costs that the franchisor will have to incur in order to monitor the quality of products supplied by the franchisee to its customers.

Building upon a sizeable body of empirical research, this article will argue that the traditional law-and-economics analysis is incomplete. Although a franchise tying contract may reduce the product quality-related monitoring costs, it is also likely to increase information, customer service, and cleanliness-related monitoring costs. More specifically, this article suggests that a franchise tying contract, by its nature, increases the level of relationship centralization, namely the degree to which decision-making authority is concentrated by the franchisor during the franchise relationship. Increase in the level of centralization, in turn, will reduce the franchisee's emotional satisfaction during the franchise relationship, and as a result, the franchisee is likely to retaliate and act opportunistically toward the franchisor throughout the relationship. Particularly, the franchisee is likely to take the following prototypical opportunistic actions towards the franchisor: manipulate information, shirk the contractual obligation to provide adequate customer service, and evade the contractual obligation to maintain the cleanliness of the entire franchise unit. As they accumulate, these opportunistic actions are likely to significantly increase the franchisor's monitoring costs and thereby off-set the reduction of the franchisor's product-quality monitoring costs arguably generated by a franchise tying contract.

Part I of this article will provide context by briefly reviewing the traditional law-and-economics approach's central argument in favor of the legality of franchise tying contracts – that is, that franchise tying contracts are likely to reduce the franchisor's monitoring costs. Part II will propose an addition to the conventional economic model. First, the article will argue that tying contracts increase the level of relationship centralization. Second, it will propose that an increase in the level of

[14] Benjamin Klein & Lester F. Saft, *The Law and Economics of Franchise Tying Contracts*, 28 J.L. & ECON. 345, 349 (1985).

centralization generated by a tying contract is likely to decrease the franchisee's emotional satisfaction. Third, the article will suggest that a decrease in the franchisee's emotional satisfaction will increase its inclination to act opportunistically toward the franchisor. Figure 1 below outlines a schematic of the new behavioral model presented in this article.

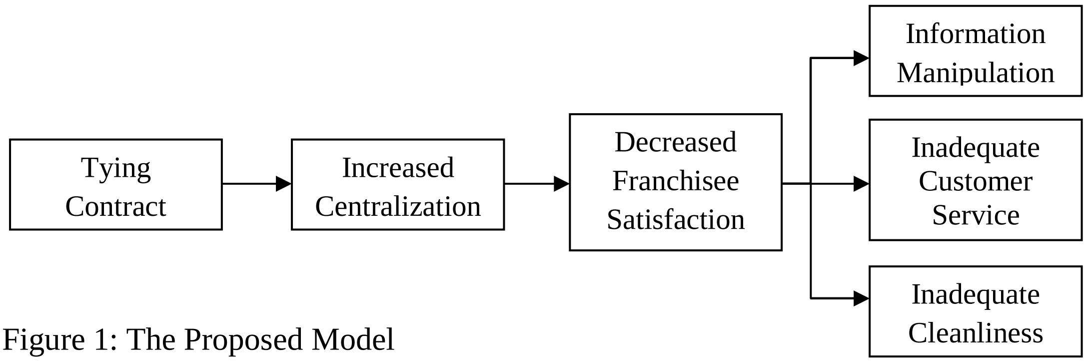

Figure 1: The Proposed Model

I. TYING AND MONITORING COSTS: THE LAW AND ECONOMICS APPROACH

According to the conventional law-and-economics perspective, the free-riding problem typifies franchise contracts.[15] Legal economists particularly suggest that if each individual franchisee is contractually responsible for supplying products to customers, each franchisee has an incentive to cut costs and supply less than the desired level of product quality.[16] Such incentive derives from two central cumulative factors: first, the individual franchisee directly benefits from the sales of the lower quality product, as it will receive the full amount of the savings from the reduced

[15] James A. Brickley, *Incentive Conflicts and Contractual Restraints: Evidence From Franchising*, 42 J.L. & ECON. 745, 748 (1999); James A. Brickley & Frederick H. Dark, *The Choice of Organizational Form: The Case of Franchising*, 18 J. FIN. ECON. 401, 406 (1987); Victor P. Goldberg, *The Free Rider Problem, Imperfect Pricing and the Economics of Retailing Services*, 79 NW. U. L. REV. 736, 746 (1984); Klein & Saft, *supra* note 14, at 349; Jonathan Klick et al., *Incomplete Contracts and Opportunism in Franchising Arrangements: The Role of Termination Clauses* 16 (American Law and Economics Association Annual Meetings, Working Paper 61, 2000) (‘‘Due to the public good nature of the franchise trademark, franchisees have an incentive to shirk by providing a sub-optimal level of service since they do not bear the full cost of any resulting deterioration of the trademark’s value.’’), *at* http://law.bepress.com/alea/16th/art61.

[16] Klein & Saft, *supra* note 14, at 349.

quality;[17] and second, the franchisee does not bear all the costs of shirking on quality.[18] The franchisee bears only part of the costs, for part is borne by other franchisees.[19] Because the franchise product is standardized, consumers who receive products of less than anticipated quality will blame the entire group of franchisees using the same trademark.[20] Thus, since the franchisee does not bear the full costs in terms of lost future sales, it will not have the correct incentive to supply high-quality products.[21]

The traditional law-and-economics analysis furthermore suggests that franchise tying contracts will decrease the likelihood that the franchisee will free-ride – namely, that it will supply less than the desired level of product quality.[22] The conventional

[17] Klein, *supra* note 13, at 631. If a franchisee allows quality to deteriorate, it will generate revenue because consumers perceive him as being of the same quality as other stores with the same trademark. *See* Paul H. Rubin, *The Theory of the Firm and the Structure of the Franchise Contract*, 21 J.L. & ECON. 223, 228 (1978).

[18] Klein, *supra* note 13, at. 631.

[19] Rubin, *supra* note 17, at 228; Klein & Saft, *supra* note 14, at 349-350.

[20] Klein & Saft, *supra* note 14, at 349; Rubin, *supra* note 17, at 228.

[21] Klein, *supra* note 13, at 631; For a description of the free-rider problem, *see also* Robert W. Emerson, *Franchise Terminations: Legal Rights and Practical Effects When Franchisees Claim the Franchisor Discriminates*, 35 AM. BUS. L.J. 559, n.29 (1998).

[22] Klein & Saft, *supra* note 14, at 353; Alan J. Meese, *Tying Meets the New Institutional Economics: Farewell to the Chimera of Forcing*, 146 U. PA. L. REV. 1, 64-65 (1997) [hereinafter Meese, *Tying Meets the New Institutional Economics*] ("By simply requiring a franchisee to purchase inputs from a franchisor, then, a tying contract can eliminate the market failure inherent in allowing the franchisee to choose its own inputs..."); Alan J. Meese, *Antitrust Balancing in a (Near) Coasean World: The Case of Franchise Tying Contracts*, 95 MICH. L. REV. 111, 119 (1996) [hereinafter Meese, *Antitrust Balancing*]; Alan J. Meese, *Regulation of Franchisor Opportunism and Production of the Institutional Framework: Federal Monopoly or Competition Between the States*, 23 HARV. J.L. & PUB. POL'Y 61, 69 (1999) ("Indeed, the sort of contractual devices most often deemed opportunistic - tying arrangements and maximum rpm - can be methods of controlling franchisee opportunism"); Mark R. Patterson, *Coercion, Deception, and other Demand-Increasing Practices in Antitrust Law*, 66 ANTITRUST L.J. 1, 11 (1997) ("In franchise cases, ties may be used to [...] prevent individual franchisees from free riding on the franchisor's reputation and other franchisees' investments..."); Andy C. M. Chen and Keith N. Hylton, *Procompetitive Theories of Vertical Control*, 50 HASTINGS L.J. 573, 605 (1999) ("To avoid free riding on product quality, firms need mechanisms to reduce or to eliminate the possibility of substitution between high-

assumption is that by requiring franchisees to purchase products from the franchisor or a designated supplier, franchise tying contracts can reduce the likelihood that the franchisee will supply low-quality products.[23] Because the franchise tying contract captures all elements of the quality of the product, the franchisee is not likely to attempt to cheat on quality.[24] The franchise tying contract essentially requires the franchisee to pre-commit not to buy low-quality products, thereby decreasing the probability of the latter's free-riding.[25] By reducing the likelihood of franchisee free-riding, the franchise tying contract ultimately reduces the monitoring costs that the franchisor will have to spend on monitoring the quality of products supplied by the franchisee to its customers.[26]

II. THE BEHAVIORAL CRITIQUE

The analytical power of traditional law-and-economics theory makes the monitoring costs reduction assumption appealing.[27] There is, however, a significant

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quality and low-quality products. Viewed in this light, the desire of firms to use tying [...] seems obvious...The purpose of this arrangement is to ensure that by using inputs of the same quality, a franchisee's incentive to free ride on the efforts by other franchisees could be eliminated"); *Queen City Pizza v. Domino's Pizza*, 124 F.3d 430, 440-441 (3d Cir. Pa. 1997) ("Courts and legal commentators have long recognized that franchise tying contracts are an essential and important aspect of the franchise form of business organization because they [...] prevent franchisees from free riding... ").

23 Meese, *Antitrust Balancing*, *supra* note 22, at 119; Comment, *A New Approach to the Legality of Franchising Tie-Ins*, 129 U. PA. L. REV. 1267, 1278 (1981).

24 *C.f.* Klein & Saft, *supra* note 14, at 352-353. (Klein & Saft explain that tying contracts reduce the cost of assuring high-quality, as compared with a contract that specifies the quality of the product. Specification of quality, as opposed to tying contracts, "will not capture all elements of quality," and therefore "the franchisee will try to cheat.")

25 Edward M. Iacobucci, *Tying as Quality Control: A Legal and Economic Analysis*, 32 J.LEG.STUD. 453-454 (2003).

26 Klein & Saft, supra note 14, at 346, 349 & 361; Klein, *supra* note 13, at 632; *Mozart Co. v. Mercedes-Benz of North America, Inc.*, 833 F.2d 1342, 1349 (9th Cir. Cal. 1987).

27 For a unique critique on this conventional economic argument *see*, Grimes, *supra* note 2, at 147 (arguing that when the quality of the franchisor's product "is relatively easy to monitor (as it should be with paper and plastic dinnerware) and if the franchisee's incentive to cheat is limited (as it should be when the franchisee will damage its own return business by providing inadequate

body of empirical data that questions the validity of this assumption. Previous empirical research on inter-firm relationships indicates that franchisees' perceptions of the existing relationship structure have deep effects on a wide range of franchisees' actions.[28] In particular, a relationship structure characterized by the centralization of franchisors' authority typically results in an increased level of franchisee opportunism.

To begin with, the sections below will briefly explain why a tying contract increases the level of relationship centralization. They will then present two major sets of empirical findings that accumulatively cast doubt on the conventional economic analysis: the first set demonstrates that an increase in the level of relationship centralization decreases the franchisee's satisfaction; the second indicates that a decrease in relationship satisfaction, resulting from a tying arrangement and its centralized nature, will increase franchisee opportunism. Eventually, such enhancement in opportunism will significantly increase the franchisor's monitoring costs.

A. Tying Contracts Increase Centralization

Centralization is defined in the franchise relationship context as the degree to which decision-making authority is concentrated by the franchisor.[29] In other words, the term denotes the degree to which a franchisor controls a franchisee through direct

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dinnerware), the requirements tie is simply not needed to maintain quality. The franchisor can address quality control by issuing standards or certifying a number of approved suppliers."

28 See *infra* Part I.

29 See *generally*, F. Robert Dwyer & Sejo Oh, *Output Sector Munificence Effects on the Internal Political Economy of Marketing Channels*, 24 J. MKTG. RES. 347, 353 (1987); Ronald E. Kidwell, Arne Nygaard & Ragnhild Silkoset, *Antecedents and Effects of Free Riding in the Franchisor-Franchisee Relationship*, J. BUS. VENTURING 522, 527 (2007); Anil Menon, Sundar G. Bharadwaj & Roy Howell, *The Quality and Effectiveness of Marketing Strategy: Effects of Functional and Dysfunctional Conflict in Intraorganizational Relationships*, 24 J. ACAD. MKTG. SCI., 299, 301 (1996); Dewar & Werbel, *Universalistic and Contingency, Predictions of Employee Satisfaction and Conflict*, 24 ADM. SCI. Q. 426, 428 (1979); Donald W. Barclay, *Interdepartmental Conflict in Organizational Buying: The Impact of the Organizational Context*, 28 J. MKTG. RES. 145, 147 (1991).

involvement in the franchisee's decision-making.[30] The level of centralization may be influenced, for example, by the degree to which the franchisor controls the franchisee's decision-making regarding opening hours, design and salaries to employees at each station.[31]

A franchise tying contract, by its nature, substantially increases the level of centralization during the franchise relationship. This increase is the result of two interrelated factors. Firstly, under a franchise tying arrangement the franchisor decides, for the franchisee, from which supplier to buy the tied product throughout the entire relationship. A tying arrangement forces the franchisee to consistently purchase the tied product from a supplier who is not necessarily the one most desired by the franchisee.[32] Secondly, by deciding for the franchisee from which supplier to buy the product, the franchisor, in fact, decides for the franchisee at what cost to buy the tied product during the whole franchise relationship. Specifically, a tying contract may force the franchisee to buy the tied product from the franchisor or its designee at a significantly higher cost than would be available from an independent vendor selling products of comparable quality.[33]

The franchise tying contract, therefore, increases the level of centralization by allowing the franchisor, during the entire relationship, to force the franchisee into the

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30 See *generally*, Keith G. Provan & Steven J. Skinner, *Interorganizational Dependence and Control as Predictors of Opportunism in Dealer-Supplier Relationship*, 32 ACAD. MANAGE. J. 202, 207 (1989).

31 Kidwell, Nygaard & Silkoset, *supra* note 29, at 539.

32 Meese, *Tying Meets the New Institutional Economics*, *supra* note 22, at 12; Meese, *Antitrust Balancing, supra* note 22, at 116-7. Under a tying arrangement the franchisee is forced to forego its free choice between competing suppliers. Joseph & Abrams, *supra* note 7, at 260; Richard A. Kleinev, *New Department of Justice Vertical Restraints Guidelines - A Search for Legal Certainty*, 40 BUS. LAW. 1335, 1364 (1985); *Mid-America Icee, Inc. v. John E. Mitchell Co.*, 1973 Trade Cas. (CCH) P74, 681, *29 (1973).

33 *Queen City Pizza v. Domino's Pizza*, 124 F.3d 430, 434 & 438 (3d Cir. Pa. 1997) (The franchisees alleged that the franchisor, Domino's Pizza, Inc., prohibited stores that produce dough from selling their dough to franchisees, even though the stores were willing to sell dough (of comparable quality) at a price 25% to 40% below Domino's Pizza's price); *Siegel v. Chicken Delight, Inc.*, 448 F. 2d 43, 46-7 (9th Cir. Cal. 1971); Joseph & Abrams, *supra* note 7, at 258.

purchase of a tied product that the franchisee might have preferred to buy elsewhere and potentially under different conditions.[34] Furthermore, the tying arrangement allows the franchisor to limit, throughout the franchise relationship, the franchisee's discretion to switch to a new supplier who provides products of superior quality, service, or price.[35]

B. Centralization Decreases Franchisee Satisfaction

Franchisee satisfaction is defined as the franchisee's effective attitudes toward the various aspects of the relationship between franchisee and franchisor.[36] A franchisee's overall satisfaction with the franchise relationship is based, among other things, on its specific perception of the quality of the franchisor's administrative personnel and service support, franchisee rewards and the franchise fee policies.[37]

Increase in the level of relationship centralization, created by a franchise tying contract, is likely to decrease the franchisee's satisfaction. This increased degree of centralization entails the constant deprivation of the franchisee's managerial autonomy.[38] Unable to select its suppliers and desired prices, the franchisee cannot fully experience the psychological success associated with setting one's own goals and objectives.[39] Furthermore, she will not be able to produce a desired change in his or her environment.[40] The continuous lack of managerial autonomy and self-control

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34 See *generally*, Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 12 (1984).

35 *Cf.* Warren S. Grimes, *Market Definition in Franchise Antitrust Claims: Relational Market Power and the Franchisor's Conflict of Interest*, 67 ANTITRUST L.J. 243, 246-7 (1999).

36 Patrick L. Schul, Taylor E. Little & William M. Pride, *Channel Climate: Its Impact on Channel Members' Satisfaction*, 61 J. RETAILING 9, 13 (1985). *See generally*, Inge Geyskens, Jan-Benedict E. M. Steenkamp & Nirmalya Kumar, *A Meta-Analysis of Satisfaction in Marketing Channel Relationships*, 36 J. MKTG. RES. 223, 224 (1999).

37 Schul, Little & Pride, *supra* note 36, at 13-4.

38 *See generally*, George John, *An Empirical Investigation of Some Antecedents of Opportunism in Marketing Channels*, 21 J. MKTG RES. 278, 280 (1984). See also *supra* Part II.A.

39 See *generally*, Dewar & Werbel, *supra* note 29, at 429; Thomas E. DeCarlo & Sanjeev Agarwal, *Influence of Managerial Behaviors and Job Autonomy on Job Satisfaction of Industrial Salespersons*, 28 IND, MKTG. MANAG. 51, 53 (1999).

40 *See generally*, Dewar & Werbel, *supra* note 29, at 429; DeCarlo & Agarwal, *supra* note 39, at 53.

generated by a franchise tying contract will eventually reduce the franchisee's relationship satisfaction.[41] Such dissatisfaction is particularly acute in the franchising context, given that franchisees are, by and large, autonomy-oriented entrepreneurs.[42]

Numerous empirical studies indicate that the greater the level of perceived centralization the lower the level of franchisee satisfaction. To illustrate, Patrick Schul, Taylor Little and William Pride explored, *inter alia*, the relationship between the level of franchisees' perceived managerial autonomy and their satisfaction with the franchise relationship.[43] The data used to explore this relationship were collected as part of a general study of franchisee-franchisor relationships in the real estate brokerage industry.[44] Participants in this study were franchised real estate agencies representing six major real estate franchise organizations in three south central states in the U.S.[45] Questionnaires were mailed to franchised real estate brokers representing all six organizations.[46] Three hundred and forty-nine usable questionnaires were

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41 *See generally*, Schul, Little & Pride, *supra* note 36, at 16; Robert A. Robicheaux & Adel I. El-Ansary, *A General Model for Understanding Channel Member Behavior*, 52 J. RETAILING 13, 25 (1975-1976); Geyskens, Steenkamp & Kumar, *supra* note 36, at 228. *See also*, Dewar & Werbel, *supra* note 29, at 429; Barclay, *supra* note 29, at 147.

42 John, *supra* note 38, at 280; David Strutton, Lou E. Pelton & James R. Lumpkin, *The Influence of Psychological Climate on Conflict Resolution Strategies in Franchise Relationships*, 21 J. ACAD. MKTG. SCI. 207, 209 (1993); Oliver Cochet, Julian Dormann & Thomas Ehrmann, *Entrepreneurial Autonomy, Incentives, and Relational Governance in Franchise Chains*, in ECONOMICS AND MANAGEMENT OF NETWORKS 117, 118 (2007). For literature on the strong desire for autonomy typical of franchisees, *see generally* , Alden Paterson & Rajiv Dant, *Perceived Advantages of the Franchise Option from the Franchisee Perspective: Empirical Insights From the Service Franchise*, 28 J. SMALL BUS. MANAGE. 46, 58 (1990); Rajiv P. Dant & Gregory Gundlach, *The Challenge of Autonomy and Dependence in Franchised Channels of Distribution*, 14 J. BUS. VENTURING 35, 36 (1998); Steve Baron & Ruth A. Schmidt, *Operational Aspects of Retail Franchises*, 19 INT'L J. OF RETAIL AND DISTRIBUTION MANAGE. 13, 19 (1991); John Stanworth & Patrick Kaufmann, *Similarities and Differences in UK and US Franchise Research Data: Towards a Dynamic Model of Franchise Motivation*, 14 INT'L SMALL BUS. J. 57, 66 (1996).

43 Schul, Little & Pride, *supra* note 36.

44 *Id*. at 17.

45 *Id*.

46 *Id*. at 18.

returned, yielding an effective response rate of 33 percent.[47] An analysis of the returned questionnaires showed that perceived autonomy has a significant positive effect on franchisee's overall satisfaction.[48]

Another empirical study yielded similar results regarding the relationship between perceived centralization and franchisee satisfaction. Yongkyu Kim used a mail survey method to examine the factors leading to an exporter's satisfaction in international markets.[49] Key informants who received the survey were identified from the exporters directory of the Korean Electronic Manufacturing Promotion Association.[50] The research surveyed electronic export firms located in the Seoul and Kyeong Ki areas.[51] The study found that the greater the control exerted by an exporter during its relationship with its parent corporation, the higher the exporter's satisfaction.[52]

An additional empirical study resulted in the same findings. Robert Dwyer conducted a laboratory simulation which examined among other things, the antecedents of franchisee satisfaction.[53] Eighty students were enlisted from sections of a basic marketing course and channel classes.[54] Among their assignments, students were given a franchisee position in one of numerous quads.[55] Each quad met for a two-hour session.[56] At the start of every session, subjects were provided with a two-

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47 *Id*. To evaluate the possibility of nonresponse bias, 36 randomly selected nonrespondents were asked several of the more important descriptive questions to determine whether nonrespondents were similar or dissimilar to respondents. No significant differences were found between respondents and nonrespondents on any of the measures analyzed. These results suggest that the respondents were representative of the overall population of franchised real estate brokers in the six franchise organizations included in the study. *Id.* at 18-9.

48 *Id*. at 30.

49 Yongkyu Kim, *A Study of Marketing Channel Satisfaction in International Markets*, 11 LOGISTICS INFORMATION MANAGEMENT 224 (1998).

50 *Id*. at 227.

51 *Id*.

52 *Id*. at 226, 227 & 230.

53 F. Robert Dwyer, *Channel-Member Satisfaction: Laboratory Insights*, 56 J. RETAILING 45 (1980).

54 *Id*. at 52.

55 *Id*.

56 *Id*.

page description of the procedures.[57] Operating statements and additional inventory, costs, and price data for the initial period were provided to serve as a basis for first-round negotiations.[58] An average of four to five decision periods was obtained by the end of each 2-hour session.[59] At the conclusion, participants completed an exit questionnaire designed to asses, among other things, their satisfaction with their rewards and their perceived control over decision variables.[60] Self-control was measured regarding marketing functions, such as shelf space allocations, retail prices, delivery schedules and retail inventory levels.[61] Correlation evidence gathered in the study suggests, once again, that franchisee satisfaction stems from her perceived self-control over decision areas.[62]

C. Decreased Franchisee Satisfaction Increases Franchisee Opportunism

A set of empirical findings indicate that a decrease in franchisee satisfaction, resulting from a centralized relationship, increases franchisee opportunism. First, the concept of franchisee opportunism will be elaborated. Then, this section will suggest a relationship between decreased franchisee satisfaction and franchisee opportunism.

1. Franchisee Opportunism: A Conceptualization

Franchisee opportunism is defined as behavior by the former towards the franchisor that involves "self-interest seeking with guile."[63] The fundamental nature of a franchisee's opportunistic behavior towards a franchisor is the deceit-oriented violation of implicit or explicit promises about its required role and behavior.[64] What

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57 *Id*.

58 *Id*.

59 *Id*. This rapid rate is not dissimilar to the pace required of a heavily worked retail or market manager in his or her multiproduct, multisite environment. *Id*.

60 *Id*.

61 *Id*. at 65.

62 *Id*. at 48, 55 & 63.

63 OLIVER E. WILLIAMSON, MARKETS AND HIERARCHIES, ANALYSIS AND ANTITRUST IMPLICATIONS 6 & 26 (1975).

64 John, *supra* note 38, at 279.

sets a franchisee's opportunism apart from the standard economic assumption of self-interest-seeking behavior is the notion of "guile."[65] Guile entails the franchisee's "lying, stealing, cheating, and calculated efforts to mislead, distort, disguise, obfuscate, or otherwise confuse" the franchisor.[66]

Opportunistic behavior on the part of a franchisee, as will be explained in greater detail below, includes three central prototypical actions:[67] manipulating information; shirking the franchisee's contractual obligation toward the franchisor to provide adequate customer service; and evading the contractual obligation to maintain the cleanliness of the entire franchise unit.

The manipulation of information may be carried out in numerous ways. First, the franchisee may understate the quantity of product sold to customers, in order to underpay fees to the franchisor. To illustrate, in *Dunkin' Donuts of America., Inc. v. Middletown Donut Corp.*,[68] the Supreme Court of New Jersey determined that the franchisee had failed to keep financial records.[69] The court concluded that the franchisee's delinquency in recordkeeping was part of a deliberate effort to underreport sales, which in turn would result in the underpayment of franchise fees, fund fees, and rental override charges.[70]

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65 Kenneth H. Wathne & Jan B. Heide, *Opportunism in Interfirm Relationships: Forms, Outcomes, and Solutions*, 64 J. MKTG. 36, 38 (2000).

66 OLIVER E. WILLIAMSON, THE ECONOMIC INSTITUTIONS OF CAPITALISM 47 (1985).

67 *See* generally, John, *supra* note 38, at 278; Dwyer & Oh, *supra* note 29, at 349. For other classifications of franchisee opportunism *see generally*, Wathne & Heide, *supra* note 65, at 38; *Sandy D Jap &* Erin Anderson, *Safeguarding Interorganizational Performance and Continuity Under Ex Post Opportunism*, 49 MANAG. SCI. 1684, 1686 (2003).

68 100 N.J. 166 (N.J. 1985).

69 *Id*.

70 The lease agreement contained a rental override provision, whereby the franchisee was obligated to pay, in addition to the basic monthly rental fee, 7% of the amount by which gross sales exceeded 150,000$ per year. *Id*. at 173, n.1. For other examples in which a franchisee understated the quantity of products sold, *see Baskin-Robbins, Inc. v. Taj Cal., Inc.*, 2003 U.S. Dist. LEXIS 19946, *17 (C.D. Cal. Sept. 9, 2003); *H.R.R. Zimmerman Co. v. Tecumseh Products Co.*, 2001 U.S. Dist. LEXIS 1920, *19 (N.D. Ill. Feb. 15, 2001); *David Glen, Inc. v. Saab Cars USA*, 837 F.

An additional way in which a franchisee can manipulate information is by overstating the quantity of product sold, in order to receive excessive payments from the franchisor. To illustrate, in *Craig Foster Ford, Inc. v. Iowa DOT*,[71] a car franchisee participated in a franchisor marketing program designed to give franchisees cash incentives to attract buyers through offers of cash rebates.[72] According to the program, the franchisor authorized its franchisees to issue universal bank drafts to buyers entitling them to rebates offered in connection with vehicle purchases.[73] The buyer would endorse the draft to the franchisee, applying the proceeds to the purchase of a vehicle.[74] The franchisee, in this case, manipulated information by reporting sales when, in fact, the sales were not made.[75] In several instances, the named "buyers" were actually the franchisee's employees.[76] The franchisee issued universal bank drafts payable to the named "buyers" and then endorsed the drafts in the payee's name, depositing the drafts in the franchisee's own bank account.[77]

The franchisee may manipulate information in a different way. It may overstate customer after-sale services, in order to receive a reimbursement from the franchisor. For example, in *R. A. C. Motors, Inc. v. World-Wide Volkswagen Corp.*,[78] a franchise contract for the sale of vehicles was signed between a retail automobile franchisee and an authorized distributor for Volkswagen.[79] The evidence showed that the franchisee submitted false reports to the distributor stating that it had performed a 300-mile free

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Supp. 888, 889 & 891, 1993 U.S. Dist. LEXIS 15092 (N.D. Ill. 1993); *Jiffy Lube Int'l v. Weiss Bros.*, 834 F. Supp. 683, 687, 1993 U.S. Dist. LEXIS 14617 (D.N.J. 1993).

71 562 N.W.2d 618, 1997 Iowa Sup. LEXIS 135 (Iowa 1997).

72 *Id*. at 620.

73 *Id*.

74 *Id*.

75 *Id*.

76 *Id*.

77 *Id*. For another example of a franchisee who overstated the quantity of product sold, *see R. A. C. Motors, Inc. v. World-Wide Volkswagen Corp.*, 314 F. Supp. 681, 683, 1970 U.S. Dist. LEXIS 11478, 1971 Trade Cas. (CCH) P73402 (D.N.J. 1970).

78 314 F. Supp. 681, 682, 1970 U.S. Dist. LEXIS 11478, 1971 Trade Cas. (CCH) P73402 (D.N.J. 1970).

79 *Id*

inspection on vehicles.[80] The distributor reimbursed the franchisee for each of the inspections.[81] Thus, the franchisee received a reimbursement for inspections that it had never performed.[82]

A franchisee may be able to distort information in another way. It can potentially misclassify customers' identity in order to evade paying fees to the franchisor. To illustrate, in *Jackson Hewitt, Inc. v. Alan Greene*,[83] the franchisor calculated its royalty fee based upon the franchisee's gross volume.[84] The franchise agreement excluded all revenue derived from a specific list of preexisting clients from the gross volume of business conducted under the franchise.[85] The franchisee's gross volume of business was reported to the franchisor via a computer-generated periodic sales report, the data for which was taken directly from the computer database of the franchisee.[86] The franchisee misclassified customers as preexisting clients.[87] Arguably, such misclassification will normally be employed in order to evade paying fees to the franchisor.[88]

Finally, in addition to the above ways in which a franchisee can manipulate information, the former may misrepresent its contractual efforts to the franchisor. In particular, the franchisee may distort information regarding its promotional efforts. To illustrate, in *H.R.R. Zimmerman Co. v. Tecumseh Products Co.*,[89] the franchisee

80 *Id*. at 683.

81 *Id*.

82 *Id*. For additional examples in which a franchisee provided a franchisor with false warranty claims, *see Ormsby Motors v. General Motors Corp.*, 842 F. Supp. 344, 346, 1994 U.S. Dist. LEXIS 974 (N.D. Ill. 1994); *see also H.R.R. Zimmerman Co. v. Tecumseh Products Co.*, 2001 U.S. Dist. LEXIS 1920, *19 (N.D. Ill. Feb. 15, 2001); *David Glen, Inc. v. Saab Cars USA*, 837 F. Supp. 888, 889 & 891, 1993 U.S. Dist. LEXIS 15092 (N.D. Ill. 1993).

83 865 F. Supp. 1199 (E.D. Va. 1994).

84 *Id*. at 1203.

85 *Id*.

86 *Id*.

87 *Id*.

88 *Id*. In this case, the court did not determine that there was fraudulent intent on the part of the franchisee, since such intent was not required in order to accept the franchisor's claim of a contractual breach by the franchisee. *Id*.

89 2001 U.S. Dist. LEXIS 18031 (N.D. Ill. Oct. 30, 2001).

allegedly falsely represented that his employees were devoting their time to managing a division that sold the franchisor's products.[90]

The second central prototypical opportunistic action that a franchisee can take is shirking its obligation to provide adequate customer service. Shirking this obligation can take numerous forms. First, the franchisee might misrepresent information to customers regarding the characteristics of the franchise product. For example, in *Barry Cook Ford, Inc. v. Ford Motor Co.*,[91] a car franchisee allegedly falsely represented to customers that leased vehicles could be subleased, that leased vehicles could be returned within a year without penalty, and that leased vehicles were not actually leased, but rather were sold.[92]

Second, the franchisee may sell customers products or services which they do not need. For instance, in *Aamco Industries, Inc. v. De Wolf*,[93] the customer was informed by a car franchisee that an expensive transmission repair was necessary even though the malfunction could have been corrected for a nominal cost.[94]

Third, the franchisee might provide delayed services to customers. To illustrate, in *Early v. Texaco Refining & Marketing, Inc.*,[95] the customers had their overheated car towed to the franchisee's station, where the franchisee agreed to look for a replacement engine.[96] This process was delayed and took seven weeks, during

90 *Id.*, at *12-3.

91 616 So. 2d 512, 1993 Fla. App. LEXIS 3213, 18 Fla. L. Weekly D 774 (Fla. Dist. Ct. App. 1st Dist. 1993).

92 *Id.*

93 312 Minn. 95, 250 N.W.2d 835, 1977 Minn. LEXIS 1668 (1977).

94 *Id.* Notably, the minor malfunctions were not corrected by the franchisee. *Id*. *See also* 951 F.2d 1059, 1061, 1991 U.S. App. LEXIS 28960, 91 D.A.R. 15331 (9th Cir. Or. 1991).

95 951 F.2d 1059 (9th Cir. Or. 1991).

96 *Id*. at 1061.

which the car remained at the station.[97] The franchisee apparently failed to keep the customers informed of the delay and lack of initiative in finding a replacement.[98]

Fourth, the franchisee might treat customers rudely. For instance, in *Early v. Texaco Refining & Marketing, Inc.*,[99] a customer reported to the franchisor that the franchisee was rude and belligerent, threw a greasy rag at him and used several phrases that the customer found upsetting.[100]

The third central category of opportunistic actions that a franchisee can take is shirking its obligation to maintain the cleanliness of the entire franchise unit.[101] Shirking this obligation can take numerous forms. To begin with, the franchisee may keep the outlet's premises unclean, including floors, walls, ceilings, storerooms, restrooms, and dumpster areas. To illustrate, in *Dayan v. McDonald's Corp.*,[102] the franchise unit walls were littered and covered with accumulations and crusts of dirt and grime.[103] In addition, toilet areas were extremely unclean.[104] Moreover, the floors, on which raw food products were stacked, were found to be very dirty.[105]

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97 *Id*.

98 *Id*. Some customers complained that the franchisee's transmission work took twice as long as the franchisee had initially estimated. *Id*. Other customers complained that the franchisee repair work was neither started nor finished when promised. *Id*. *See also Tappan Motors, Inc. v. Volvo of America Corp.*, 85 A.D.2d 624, 626 (N.Y. App. Div. 2d Dep't 1981).

99 951 F.2d 1059 (9th Cir. Or. 1991).

100 *Id*. at 1061.

101 *See generally*, Gillian K. Hadfield, *Problematic Relations: Franchising and the Law of Incomplete Contracts*, 42 STAN. L. REV. 927, 970 (1990).

102 126 Ill. App. 3d 11 (Ill. App. Ct. 1st Dist. 1984).

103 *Id*. at 18.

104 *Id*.

105 *Id*. at 18; *See also Dunkin' Donuts, Inc. v. Donuts, Inc.*, 2000 U.S. Dist. LEXIS 17927, *7-8 (N.D. Ill. Dec. 1, 2000) (a case in which the franchise unit was found with unclean floors, walls, countertops, toilets, sinks and trash areas); *Dunkin' Donuts Inc. v. Patel*, 174 F. Supp. 2d 202, 207 n.4 (D.N.J. 2001) (in which the restroom sink in the franchise in question was dirty); *Zeidler v. A&W Restaurants, Inc.*, 2001 U.S. Dist. LEXIS 653, *14 (N.D. Ill. Jan. 23, 2001) (in which filthy sinks and dirty bathrooms were found); *Dunkin' Donuts Inc. v. Kashi Enters Inc.*, 119 F. Supp. 2d 1363, 1365, 2000 U.S. Dist. LEXIS 19463 (N.D. Ga. 2000) (in which the franchise included an unclean dumpster area, restroom, toilets, sinks, floors, walls, ceilings, storeroom and restroom);

Second, the franchisee may maintain the franchise unit's equipment in an unclean manner. To illustrate, in *Dunkin' Donuts Inc. v. Kashi Enters. Inc.*,[106] the soft serve freezer, diary dispenser, meat slicer and other equipment were not sanitized at proper frequency.[107] Similarly, in *McDonald's Corp. v. Robertson*,[108] a meat staging cabinet and towels were not maintained in clean condition.[109] Likewise, in *Dunkin' Donuts Inc. v. Patel*,[110] the walk-in freezer was littered with debris, and trays and containers were dirty.[111]

Third and finally, the franchisee may shirk its obligation to maintain employee hygiene. For instance, in *Wojciechowski v. Amoco Oil Co.*,[112] the franchisee's employees themselves allegedly were not neat and clean.[113] Similarly, in *Dunkin' Donuts, Inc. v. Donuts, Inc.*,[114] the franchisee's sanitation violations included

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Dunkin' Donuts Inc. v. Barr Donut, LLC, 242 F. Supp. 2d 296, 307, 2003 U.S. Dist. LEXIS 783 (S.D.N.Y. 2003) (in which filthy surfaces were found in the franchise); *Tappan Motors*, *Inc. v. Volvo of America Corp.*, 85 A.D.2d 624, 626 (N.Y. App. Div. 2d Dep't 1981) (in which the franchisee's facilities were not as clean as the franchisor required); *Nazaino Azucy v. Amoco Oil Co.*, 1986 U.S. Dist. LEXIS 30394, *8 (N.D. Ga. Jan. 15, 1986) (in which the franchisee had not complied with the contractual provisions requiring him to maintain the station in a clean manner).

106 119 F. Supp. 2d 1363 (N.D. Ga. 2000).

107 *Id*. at 1365.

108 147 F.3d 1301 (11th Cir. Fla. 1998).

109 *Id*. at 1304.

110 *Dunkin' Donuts Inc. v. Patel*, 174 F. Supp. 2d 202 (D.N.J. 2001).

111 *Id.* at 207 n.4. *See also, Dayan v. McDonald's Corp.*, 126 Ill. App. 3d 11, 18 (Ill. App. Ct. 1st Dist. 1984) (in which the interiors and exteriors of refrigerators and freezers were incredibly filthy, greasy, and smeared with sauces and food; additionally, refrigerator fans, drains, and coils were blackened with dried food, chicken blood and grease residue); *Dunkin' Donuts, Inc. v. Donuts, Inc.*, 2000 U.S. Dist. LEXIS 17927, *7-8 (N.D. Ill. Dec. 1, 2000) (in which unsanitized utensils were used); *Dunkin' Donuts Inc. v. Priya Enters.*, 89 F. Supp. 2d 319, 323 (E.D.N.Y. 2000) (food preparation equipment not dismantled, cleaned and sanitized regularly).

112 483 F. Supp. 109 (E.D. Wis. 1980).

113 *Id.* at 112.

114 *Dunkin' Donuts, Inc. v. Donuts, Inc.*, 2000 U.S. Dist. LEXIS 17927 (N.D. Ill. Dec. 1, 2000).

insufficient employee hygiene.[115] Likewise, in *Dunkin' Donuts Inc. v. Priya Enters.*,[116] there was no employee sanitation training program in place.[117]

Following the above conceptualization of franchisee opportunism, the remainder of this article will proffer that deceased satisfaction, generated by centralization and tying, increases franchisee opportunism.

2. The Correlation Between Decreased Satisfaction and Opportunism

The above discussion of various empirical studies indicates that a decrease in a franchisee's relationship satisfaction, resulting from a tying arrangement and its centralized nature, will increase franchisee opportunism. A continuous feeling of dissatisfaction during the franchise relationship is likely to arouse the franchisee's anger.[118] This emotional experience is likely to promote aggressive retaliatory behavior, which typically takes the form of franchisee opportunistic behavior.[119] Particularly, centralization, and the dissatisfaction it creates, increase the likelihood that the franchisee will manipulate information, shirk the obligation to provide adequate customer service, and evade the obligation to maintain cleanliness standards throughout the entire franchise unit.

The first empirical study examining this correlation was conducted by George John.[120] A sample was drawn randomly from the population of retail dealers of a

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115 *Id.* at *7-8.

116 *Dunkin' Donuts Inc. v. Priya Enters.*, 89 F. Supp. 2d 319 (E.D.N.Y. 2000).

117 *Id.* at 323.

118 For a general discussion on the relationship between frustration and anger *see*, Leonard Berkowitz & Eddie Harmon-Jones, *Toward an Understanding of the Determinants of Anger*, 4 EMOTION 107, 111 (2004).

119 John, *supra* note 38, at 280; Barclay, *supra* note 29, at 147-8. *See also* Berkowitz & Harmon-Jones, *supra* note 118, at 111; Leonard Berkowitz, *Frustration-Aggression Hypothesis: Examination and Reformulation*, 106 PSYCHOL. BULL. 59, 69 (1989). For a seminal work contending that psychological frustration leads to aggression, commonly known as the frustration-aggression hypothesis, *see* JOHN DOLLARD ET AL., FRUSTRATION AND AGGRESSION 1 (1939).

120 John, *supra* note 38.

major oil company.[121] The survey instrument included questions measuring, among other things, the level of two major variables: the supplier's centralization and the dealer's opportunism.[122] The survey instrument yielded a sample of 147 usable responses.[123] The study showed that as the dealer's perception of the supplier's centralized structure increased, so too did dealer opportunism.[124] Particularly, centralization increased the dealer's inclination to manipulate information and to shirk promises made to the supplier.[125]

Another empirical study was conducted by Robert Dwyer and Sejo Oh.[126] In order to obtain variation on environmental munificence, a sample was drawn from five rich and five lean macroenvironments on a systematic basis from Standard Metropolitan Statistical Areas (SMSAs) profiled in the *Census of Retail Trade* and *Sales and Marketing Management's* survey of buying power.[127] The survey instrument included questions measuring, among other things, the levels of dealer opportunism and supplier centralization.[128] The results of the empirical study showed that centralization decreases the quality of the dealer-supplier relationship, as reflected in, among other things, dealer opportunism.[129] Dealer opportunism was measured by the inclination to manipulate information and shirk obligations toward the supplier.[130]

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121 *Id.* at 282.

122 *Id*. at 282, 287-8. The survey instrument was mailed to 1000 dealers. The survey yielded a sample of 147 usable responses. The 14.7% response rate raised the issue of selection artifacts. To check for nonresponse bias, John compared the obtained sample average for certain variables with their known population values obtained from company records. This check revealed no statistically significant differences. In addition, checks were done to ensure sufficient variability and no end-piling for the individual item from which the scales were computed. *Id*. at 282-3.

123 *Id.* at 282.

124 *Id.* at 287.

125 *Id.* at 288.

126 Dwyer & Oh, *supra* note 29.

127 *Id.* at 349-350.

128 *Id*. at 352. Questionnaires were mailed to 185 automobile dealers and 133 were returned. *Id*. at 350-1.

129 *Id*. at 355 & 349.

130 *Id*. at 352.

An additional empirical study was conducted by Keith Provan and Steven Skinner.[131] Data was collected via a national survey of farm and power equipment dealers.[132] A simple random sample of dealers from the membership directory of the National and Power Equipment Dealers Association was selected.[133] Once again, the survey instrument featured questions measuring, among other things, the extent of dealer opportunism and supplier centralization.[134] Two-hundred and twenty-six returned questionnaires were analyzed by Provan and Skinner.[135] The analysis showed that centralization was positively related to dealer opportunism, again, as measured by dealer inclination to manipulate information and shirk promises made to the supplier.[136]

A final empirical study was conducted by Ronald Kidwell, Arne Nygaard and Ragnhild Silkoset.[137] Their study of Norwegian franchisee dealers in a multinational gasoline distributor network identified structural and market factors that lead to free-riding by franchisees.[138] A Norwegian-owned multinational oil company's franchisee dealer network, which distributes relatively homogenous products, was chosen as the empirical setting.[139] Information was collected from both sides in a series of franchisor-franchisee relationships.[140] This survey instrument included questions measuring, among other things, the level of franchise the dealers' free-riding and the suppliers' centralization.[141] From an analysis of the 192 franchise dealers' responses analyzed, the field study showed that the level of centralization in a franchise relationship is positively related to a franchise dealer's free-riding behavior.[142] Among

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131 Provan & Skinner, *supra* note 30, at 206.

132 *Id.*

133 *Id*.

134 *Id*. at 211-2. Two-hundred and twenty-six returned questionnaires were analyzed by Provan and Skinner. *Id*. at 206.

135 *Id*. at 206.

136 *Id*. at 211.

137 Kidwell, Nygaard & Silkoset, *supra* note 29.

138 Kidwell, Nygaard & Silkoset, *supra* note 29, at 523.

139 *Id*. at 529.

140 *Id*.

141 *Id*. at 539 & 541.

142 *Id*. at 530 & 536.

other factors, free-riding behavior was measured by the franchise dealer's inclination to maintain an unclean station and to provide inappropriate customer service.[143]

CONCLUSION

Courts have generally adopted a hostile attitude toward tying contracts since they allow the buyer to use its economic power in one product to restrain trade in the tied good market. The traditional law-and-economics analysis suggests that the *per se* illegality rule that governs franchise tying contracts is inefficient. Legal economists particularly argue that a *per se* illegal standard fails to account for the improvements in efficiency that a franchise tying contract creates. One central improvement in efficiency that a franchise tying contract creates, according to legal economists, is a decrease in the costs that the franchisor will have to incur in order to monitor the quality of the products supplied by the franchisee to customers.

This article has argued that the traditional law-and-economics theory is incomplete. The franchisee is more likely, under a centralized tying relationship, to take the following opportunistic actions: understating the quantity of product sold to customers in order to underpay fees to the franchisor; overstating the quantity of product sold to customer in order to receive excessive payments from the franchisor; overstating customer after-sale services in order to receive a reimbursement from the franchisor; misclassifying customers' identities in order to evade paying fees to the franchisor; misrepresenting its contractual efforts to the franchisor; misrepresenting information to customers regarding the characteristics of the franchise product; selling customers unneeded products or services; providing delayed services to customers; treating customers rudely; neglecting to keep the outlet's premises sufficiently clean; avoiding maintaining the cleanliness standards required of the franchise unit's equipment; and overlooking employee hygiene. As they accumulate, these potential opportunistic actions are likely to increase significantly the franchisor's information, customer service, and cleanliness-related monitoring costs. The result is that under normal circumstances, an increase in all of these monitoring costs is likely to off-set the

143 *Id*. at 541.

arguable product quality-related monitoring cost savings generated by a franchise tying contract.

As it is doubtful that franchise tying contracts will reduce overall franchisor monitoring costs, it follows that courts should uphold a basic opposition to monopolistic franchise tying contracts. Furthermore, courts concerned with reducing franchisor policing costs should be dubious of the economic monitoring rationale advanced is support of the legality of anticompetitive franchise tying contracts.