

## Can you take back your franchise contract?



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Everyone has probably answered the door to a door-to-door salesman offering you a magazine subscription or a deal that just sounds too good to be true. After signing on to that “amazing” deal, however, you read the small print and discover that you have three days to “rescind,” or completely take back, the terms of the contract or subscription you just purchased. You can call and get out of the purchase the next day.

Unfortunately, a franchisee who wants to rescind their franchise agreement on the basis of some type of fraud or misinformation months or years after signing the franchise agreement faces a slightly more difficult endeavor.

### **How long is too long to wait to rescind a franchise agreement?**

In most states, a party seeking to rescind a contract on the basis of fraud, fraudulent inducement, or any other reason for the rescission must act promptly after learning of the fraud or any other right to rescind. The failure to do so results in a waiver of any right to rescission. (*Heidtman Steel Products, Inc. v. Compuware Corporation*, 168 F.Supp.2d 743, 748 (N.D. Ohio 2001) (a party “asserting a right to rescind must do so “without unnecessary delay” or else loses the right to relief.”))

While there is no strict time period that limits a party’s right to assert rescission, a right to rescind might be

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lost once “there has been a change of position by, or prejudice to” the party who has breached the contract. (*Cincinnati Gas & Elec. Co. v. General Elec. Co.*, 656 F.Supp. 49 (S.D. Ohio 1986) (noting that “[o]rdinarily, the question of what is a reasonable time for rescission is a question of fact for the jury.”)) For example, one federal court interpreting Ohio law found that a delay in asserting rescission for two years after discovery of fraud was sufficient to waive the right of rescission. (*In re Bell & Beckwith*, 112 B.R. 858 (Bankr. N.D. Ohio. 1990))

However, courts have long held that if a franchisee continues to comply with the franchise agreement after discovering the reason to rescind, the right to rescind may be waived. In *City of Cincinnati v. Edison Electric Co.*, for example, the city of Cincinnati waived the right to rescind its contract with a light company by “deal[ing] with the other party, and permit[ing] large expenditures of money to be made, upon the theory that there is still a subsisting contract.” (9 Ohio Dec. 438 (1st Dist. 1899). *see also* 3 Williston on Contracts, § 688, p. 1983, Restatement of the Law, Contracts, § 309 (wherever a contract “not already fully performed on either side is continued in spite of a known excuse, the defense thereupon is lost and the injured party is himself liable if he subsequently fails to perform.”)) Further investing in a franchise business after discovering the right to rescind may also affirm the contract and waive the right to rescind. In *Albarqai v. 7-Eleven, Inc.*, for example, the Eastern District of Pennsylvania found that a franchisee, who claimed that he had a right to rescind the contract based on the franchisor’s alleged misrepresentation that the store was safe, was on notice about the alleged misrepresentation during his first week as a franchisee when the store was robbed at gunpoint. However, the franchisee waited two years – and made further investments into the store – before attempting to pursue the right to rescind the contract. (No. Civ. 12-3506, 2014 WL 616975, \*3 (E.D. Pa. Feb. 18, 2014)). The court found that he had waived his right to rescind. *Id.*

Even “constructive knowledge” of a fact that that might give a franchisee the right to rescind – and continuing to act on the contract despite that knowledge – may cause a franchisee to waive the right to rescind a contract. (See *Lithograph Bldg. Co. v. Watt*, 96 Ohio St. 74, 88 (1917) (holding that a principal will be deemed to have ratified lease where “he appears to have actual or constructive notice of its terms”)) A franchisee might receive information in franchise disclosure documents, meeting minutes, or uniform circulars that might cause a franchisee to have “constructive knowledge” about a fact that might give rise to rescission – therefore, a franchisee should carefully consider and read all of the information it receives from the franchise company.

While the goal of rescission is to return the contact parties to the status quo, realistically completing this goal becomes more difficult the longer a contract counterparty waits to assert the right to rescind. In *Albarqai v. 7-Eleven, Inc.*, for example, the court found that the franchisee was not entitled to rescind the contract; however, it also noted that returning the parties to the status quo would be quite difficult after the franchisee had operated the store for over two years. “After operating and profiting from the [s]tore for so long, it would be difficult to return both parties to their original positions.” (*Albarqai*, 2014 WL 616975, \*3).

The more time passes, the more difficult it becomes to separate the actions and consequences of the franchisor from the franchisee. In another case, the court found that “[b]y waiting for two years before filing suit, plaintiffs have given themselves an opportunity to determine if the profitability of their franchise

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is acceptable to them and have been responsible for the evolution of circumstances which make impossible the recreation of the conditions which existed [when the violation occurred].” (*A Love of Food I, LLC v. Maoz Vegetarian USA, Inc.*, 717 F. Supp. 368, 372 (D. Md. 1989)).

Ultimately, if a franchisee discovers any fact that may entitle it to assert the right to rescind its contract, it is the franchisee’s best interest to assert an action to rescind as soon possible. Otherwise, the franchisee may waive the right to recover any damages or assert the right to rescind at all.



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