Featured Articles

Agency Theory in Actions Against Co-operative Businesses: Considerations and Case Law

By Danielle N. Malaty

A Winnebago County trial court sitting in Illinois' 4th Appellate District recently granted a cooperative business' motion for summary judgment in a propane explosion case. *Maychszak v. True Value Company*, 15 L 259 (2018). The propane tank exploded, causing the Plaintiff serious bodily harm and permanent disfigurement. Codefendant had allowed the tank to fall into disrepair, along with his trailer, to which the tank was attached. The co-op did not sell the tank to the store, as the store was free to purchase its merchandise from vendors of its choice.

Prior to the explosion, the member store had serviced Codefendant's propane tank pursuant to a "Propane Gas Supply Agreement," to which the cop-op was not a party. The co-op did not manufacture or sell the tank, nor did it service or provide propane for the tank. Plaintiff filed a negligence suit against the member store, but named the co-op as a defendant solely under an agency theory. Specifically, plaintiff alleged that the co-op was liable because the member store was acting as its actual/apparent agent at the time the member store serviced codefendant's tank, and since the member store's alleged negligence caused the tank to explode, the co-op was vicariously liable for plaintiff's resulting injury.

It is important to note the significance of plaintiff's failure to allege direct negligence against the co-op. The Court recognized this in its opinion and echoed the Appellate and Supreme Court of Illinois in holding that actual and/or apparent agency cannot serve as separate and distinct, stand-alone legal theories of recovery and cannot serve as the basis for recovery. *Wilson v. Edward Hosp.*, 2012 IL 112989, 981 N.E.2d 971 (2012).

Critical Characteristics of Co-ops

In an action against a co-op, a plaintiff is put in a precarious position, such that it is nearly impossible to allege any direct negligence against the co-op who has no involvement with the member on a day to day basis. While control over day-to-day operations is nearly codified within the bylaws of a franchise and immediately noticeable upon entering any of its stores, the same cannot be said in the context of a co-op. A plaintiff filing suit against a co-op must typically resort to allegations "by and through" the member and purported agent, who carries the name of an entity, to which it does not answer, at the front of their stores. If a plaintiff cannot produce facts that demonstrate a right to control the manner in which a member accomplishes tasks on a day-to-day basis, there can be no finding of actual agency as a matter of law. *Tansey v. Robinson*, 24 Ill. App. 2d 227, 164 N.E. 2d 272 (1960).

Retailers, restaurants and hotels with well-known, recognizable logos sometimes opt for alternative business structures rather than franchises in order to shield themselves from being held vicariously liable for the tortious conduct of their member stores. A co-op is often named in a lawsuit alongside the member for having the deepest pockets, despite the fact that its only involvement with the member may include discounts on bulk purchases and the obvious benefit of displaying their reputable, recognizable logo on their storefront for purposes of increasing marketability and business development. As distinguished from a franchise structure, co-ops allow their independently owned and operated members to carry products from vendors of their choosing, while not necessarily obligating them to keep a certain amount of their own in stock. So the question then turns to who is in control, and to what degree.

A few notable co-operative business organizations include Ace Hardware, True Value, Best Western, United Western Grocers, and Certified Grocers. It is important to be cognizant of the attention that these household names draw when discussing vicarious liability. If someone is injured during their stay at a Best Western, can liability be imposed on any parent company? Does Ace control the day-to-day activities of the hardware store where plaintiff purchased his defective product? Did the plaintiff rely to his detriment on that bright, shiny sign carrying the logo of Certified Grocers when he walked through its doors? A close look at case law involving these specific co-ops can provide ample guidance on the facts that should be sought from the inception of a suit to rebut allegations of actual and apparent agency.

Summary Judgment Granted on Plaintiff's Actual Agency Claims

The Winnebago trial court considered several questions of law under the theory of agency, both actual and apparent. On the issue of actual agency, the court relied heavily on the absence of control over the retailer's day-to-day activities. In citing *Salisbury v. Chapman Realty and Oliveira-Brooks v. Re/Max Int'l, Inc.*, the Winnebago trial court found that the plaintiff's attempts to establish actual agency based exclusively on the Cooperative Agreement fell flat. 124 Ill App. 3d 1057, 465 N.E.2d 127 (1984); 372 Ill App. 3d 127, 865 N.E.2d 252 (2007).

Co-ops typically have an agreement set in place that defines the parameters of their relationship with a member, and in this case, its terms and conditions were dissected by both of the parties. While the co-op drew the trial court's attention to terms that required its members to identify themselves conspicuously as independent contractors, plaintiff selected anecdotal terms that exhibited minimal amounts of control that only spoke to the general purpose of the store. Notably, plaintiff could not reconcile certain terms that further allowed the member store to utilize the logos of other distributors from whom they purchased products in their inventory.

Plaintiff attempted to draw the court's attention to certain guidelines contained in the agreement for the store's layout (which was limited to one display in the member store), the luxury of having been given the right to use its logo, and a requirement to utilize the co-op as its primary supplier. Plaintiff further argued that the co-op exercised control over the retailer because the agreement instructed the retailer to adhere to the co-op's high standards of honesty, integrity, fair dealing and ethical conduct in how it dealt with its patrons. The Court held that these instructions only served to demonstrate an interest in protecting the co-op's reputation and goodwill, but did not demonstrate control over the store itself. In so ruling, the Court perceived the member store as though it were merely a licensee, rather than an agent.

Further, the Court rejected plaintiff's agency theory because the member agreement never outlined any control over the day-to-day business activities or gave any mandate whatsoever as to how it should operate. The retailer was free to make its own decision when it came to merchandise, and was further free to manage its employees in any way it saw fit. The co-op never exerted any control over the layout of the store and never retained the right to hire or terminate member store personnel, nor was it involved in its hiring process. In addition to these operative facts, the member agreement was supported by testimonial admissions by member employees, including store managers, confirming that the co-op never interacted with them directly, never trained them, and that the co-op was just another brand that they happened to carry.

While the member agreement spoke to some degree of training available to its members, the Winnebago trial court considered it relevant to its decision that any such training only consisted of optional seminars on best business practices. In ruling on the motion, the Court held that plaintiff was unable to prove actual agency without adducing facts that demonstrate an exertion of control over the day-to-day operations of an alleged agent. *Anderson v. Boy Scouts of America, Inc.*, 226 Ill App. 3d 440, 589 N.E.2d 892 (1992).

A decision from the Pennsylvania Courts provided the Winnebago trial court with ample guidance as to how the doctrine of vicarious liability should be applied to an action against a co-op, as this issue has not been heavily litigated in Illinois. *Myszkowski v. Penn Stroud Hotel*, 430 Pa. Super. 315, 634 A.2d 622 (1993). As previously mentioned, Best Western is one of those "big name" companies that operates under the protective business model of a co-operative organization. In *Myszkowski*, *Id.*, a plaintiff filed suit against Best Western under a theory of actual agency, further arguing that, based on a member agreement, Best Western retained the right to take away use of its trade name, while lacking control over the everyday business activities. *Id.* The Court focused on what Best Western lacked in granting its motion for summary judgment: direct, supervisory control.

The trial court further considered a case against a real estate entity with much better facts than those at present. That entity actually had training requirements for its purported agent's employees and even reserved the right to inspect its accounts on a regular basis. Salisbury, Id. Nevertheless, because the entity had no control over the day-to-day activities of the purported agent, the court found no actual agency. Moreover, the trial court considered precedent set forth in a suit against Certified Grocers, another recognizable co-op, wherein the court granted a motion for a directed verdict based upon the fact that it exercised zero day-to-day control over its member store, did not have the power to hire or fire employees, and could only withdraw its permission to use its name and terminate the grocery stores membership for a violation of its rules. *Yassin v. Certified Grocers of Illinois, Inc.*, 150 Ill App. 3d 1052, 502 N.E.2d 315 (1986).

In comparing the facts in both *Yassin*, *Id.*, and *Myszkowski*, *Id.*, the trial court recognized that the co-op retained

the same minimal level control in reserving the power to take away the store's right to use its logo, which the Court deemed insufficient as evidence of actual agency. The big takeaway from the Court's position on actual agency is that the absence of any facts that would demonstrate *direct, supervisory powers* over the method and manner in which the store accomplishes everyday tasks is fatal to a plaintiff's claim.

Summary Judgment Granted on Plaintiff's Apparent Agency

The Winnebago trial court also found the plaintiff's apparent agency claims against the co-op infirm as well. In reaching its decision, the trial court first emphasized that the Plaintiff needed to show facts satisfying the three factors of an apparent agency relationship between the co-op and the member store in order to survive summary judgment; (1) That the co-op held the member store out as its agent at the time Plaintiff was injured; (2) Plaintiff could reasonably believe that an agency relationship existed between the two entities; and (3) The Plaintiff relied on that agency relationship to his detriment. *Oliveira-Brooks v. Re/Max International, Inc.*, *Id*.

In finding that the Plaintiff failed to show facts satisfying the third factor, the trial court reasoned that the Plaintiff did not show evidence that he relied on the member store's apparent authority to act on behalf of the co-op at the time the member store serviced codefendant's propane tank leading to Plaintiff's injury. In reaching this conclusion, the trial court first recited the fact that neither the co-op nor Plaintiff was a party to the Propane Gas Supply Agreement between the member store–which serviced the tank.

Next, the trial court found the co-op's right to summary judgment was clear and free from doubt as to Plaintiff's apparent agency theory since the Plaintiff could not have possibly known that the member store was acting on behalf of the co-op in servicing the propane tank, since the co-op was not a party to Propane Service Agreement. In essence, the trial court concluded that summary judgment was due based on the two agreements at issue, the causes of action as pled in the complaint, and the co-op's ability to take advantage of the Plaintiff's failure to present facts supporting the elements of his claim, while at the same time showcasing case law favorable to the co-op's position.

The Court cited to a decision in a case against Re/Max, a co-op, wherein the plaintiff was unable to demonstrate apparent agency. In that case, plaintiff unsuccessfully relied on a number of facts to demonstrate apparent agency. For example, the purported agent mentioned the name of Re/Max to his clients to grow his business and increase his credibility; wore a pendant with the Re/Max logo; and even had the Re/Max logo affixed to his vehicle. *Id*. The most probative aspect to the *Re/Max* decision is the testimony of plaintiff's son. Specifically, he testified that he recommended Re/Max to his mother as a good company, and further, that she relied on his recommendation to her detriment. *Id*. On the other hand, plaintiff herself did not provide any such testimony. *Id*. The court concluded that Plaintiff had failed to adduce evidence to demonstrate *her own reasonable reliance* on an apparent agency relationship between the purported agent and the co-op. *Id*.

The trial court cited to the *Re/Max* decision in considering plaintiff's attempt to satisfy the requirements it set forth, as the facts were almost synonymous. Plaintiff attempted to rely on the testimony of the codefendant that purchased the propane tank, and since plaintiff himself could not have reasonably concluded that an agency relationship existed, plaintiff submitted to the court *codefendant's state of mind*, rather than his own, to satisfy court's test for apparent agency. Plaintiff's proof of an apparent agency relationship rested on codefendant's admission that he thought the store and the co-op were one in the same when he purchased the propane tank. The Court nevertheless rejected this argument in holding that any "reasonable conclusion" that an agency relationship exists must be made by the injured party who relied on it to his detriment. In so holding, the Court held that it was *plaintiff's* state of mind that was determinative—not that of a third party. *O'Banner v. McDonald's Corp.*, 173 Ill. 2d 208, 670 N.E.2d 632 (1996). Reliance of another cannot be imputed on an injured party in order to establish apparent agency. Other than codefendant, plaintiff could not point to any testimony that comported with codefendant's speculation.

Plaintiff was unable to demonstrate that he himself relied in any way whatsoever on the apparent authority of the store. In fact, the evidence adduced demonstrated that plaintiff was quite familiar with the layout of where the explosion occurred, in addition to the subject trailer and tank, as he had worked as a public safety officer for several years prior to the explosion. Moreover, it was within plaintiff's job description to address propane leaks or address a potential hazard observable by scent or sound. Plaintiff's state of mind carried the day in the Court's determination that apparent agency could not be proved, as no facts were adduced that could demonstrate *his own* reasonable conclusion that agency existed, or that *he himself* detrimentally relied on such a relationship.

Practical Advice for Handling Co-op Cases

When defending a co-op against allegations of actual and apparent agency, the first line of defense is to sit down and talk with your client about their business structure and make sure they understand the nature of the allegations. It is important to understand your co-op's business structure so that you can identify the intent behind the actual agreement in place with respect to its members. Furthermore, it is important to better understand the actual relationship your client has with its members, as well as the members' perception of the co-op. This is how you become fluent in the interplay between the parties involved in a multiparty lawsuit involving your client.

After you have taken these initial steps, you can move on to the second line of defense that occurs during discovery. First, it is important that the protections necessary to defend against these allegations are included and enumerated in the agreement. By having a conversation with your client about their relationship with the co-op, you can identify potential witnesses who may be called by the plaintiff to testify. Once you've identified those individuals, have conversations with them. Identify whether they will testify within the confines of the member agreement, as your motion for summary judgment may very well hinge on what they say under oath.

In addition to preparing for testimony provided by representatives of your co-op, you can begin to prepare for plaintiff's own testimony and any witnesses they may call to support plaintiff's theory. Elicit testimony from the plaintiff wherein they themselves commit to the allegations of actual and apparent agency as their only theory of liability against the co-op, knowing that those allegations are insufficient as a standalone cause of action. Go into plaintiff's discovery deposition knowing that they will not be able to make the leap of claiming they reasonably relied on apparent authority to their detriment, and further knowing that they may not entirely understand the nature of the allegations.

Defending a co-op requires a shrewd understanding of your client's contractual rights of control over their members. Armed with that understanding, take the complaint at face value and attack the cause of action pled at the summary judgment stage rather than providing plaintiff with a roadmap of your defense strategy by highlighting those deficiencies early in the case. Finally, reduce the complexities in a case, where the roles of the defendants risk being confused, down to simple and practical terms which showcase to the court that a plaintiff could not have reasonably relied on an agency relationship to his detriment.

Trends in Other Jurisdictions

The Winnebago Trial Court relied on the Pennsylvania Courts in ruling on this motion due to the lack of litigation involving co-operative business organizations and the narrow distinctions that the Courts must draw between these organizations and a prototypical franchise. While Illinois lacks substantial authority with respect to these distinct entities, other states are creating precedent for imposing vicarious liability on a co-op. In *Murphy v. Holiday Inns, Inc.*, the Supreme Court of Virginia determined that a mere franchise agreement did not make the franchisee an agent of the franchisor. There must exist some control of, or right to control, the methods or details of doing the work. 219 S.E.2d 874 (Va. 1975).

A Maryland Court grappled with a similar fact pattern in *Wood v. Shell Oil Co.*, 495 So. 2d 1034 (Ala. 1986). In *Wood*, *Id.*, the Court noted several factors that are also found in this case. Pursuant to a lease, Parker Shell had purchased gasoline and other products from Shell Oil and had retailed these products to the general public. The employees of Parker Shell received all their compensation and benefits from Parker Shell, and Parker Shell had exclusive authority for hiring and firing them. Parker Shell was not obligated to accept advertising material from Shell Oil; it determined for itself what products, if any, it wished to purchase from Shell Oil and in what quantities; it was free to purchase and sell products of suppliers other than Shell Oil; and it determined the retail price to be charged for the sale of its products. Further, by deposition, the dealer testified that Shell Oil did not interfere in the daily operation of the station and did not inspect the service station's premises for safety. No evidence was adduced that Shell Oil retained any right or control over the manner in which Parker Shell performed in order to meet the requirements of the lease and dealer agreement. Although the lease and the dealer agreement specified what Parker Shell must do in order to conform to the terms of these contracts, and gave Shell Oil the right to approve certain aspects of Parker Shell's operation, in no way did Shell Oil determine how Parker Shell was to achieve compliance with those terms.

The Courts in North Carolina have followed the trend of other jurisdictions in finding that a principal's vicarious liability for the torts of his agent depends on the degree of control retained by the principal over the details of the work *as it is being performed*. The controlling principal is that vicarious liability arises from the right of supervision

and control. *Vaughn v. North Carolina Dept. of Human Resources*, 252 S.E.2d 792 (N.C. 1979). South Carolina Courts have also followed suit in finding that liability depends upon the existence of an agency relationship, which is determined by the nature and extent of control and supervision retained and exercised by the franchisor over the methods or details of conducting the day-to-day operation. *Fernander v. Thigpen*, 293 S.E.2d 424 (S.C. 1982).

Similarly in Michigan, Defendant contended that, while it owned the land where a restaurant was located, it did not actually occupy or control a restaurant's premises, and thus was not a "possessor" liable for the plaintiff's injuries. *Little v. Howard Johnson Co.*, 455 N.W.2d 390 (Mich. 1990). Plaintiff contended that the mere fact that defendant owned the land on which the restaurant was situated created a question existed regarding defendant's direct liability. The Court disagreed in finding that title ownership of the premises is not determinative and thus fails to create an issue of material fact. The Court concluded that it is the possessor or occupier of land, not necessarily the titleholder, who owes a duty to invitees regarding the condition of the land.

The Georgia Courts took a strong position against the determinativeness of a written document establishing a franchisor/franchisee relationship. *Washington Road Properties v. Home Ins. Co.*, 145 Ga. App. 782, 784, 245 S.E.2d 15 (1978). In *Washington*, the fact that a contract was labeled a franchise agreement was not necessarily controlling, and the Courts must look to the contents to determine the character of the relationship created. *Id.*

Conclusion

Walking into any fast food chain or coffee store, it becomes readily apparent that someone is in charge of how things are organized and how tasks are performed, ranging from how the napkins are arranged, to the methods in which safety policies and procedures are implemented. Because of this apparent relationship to a parent organization, companies are often held liable for the tortious conduct of its franchisees, even though they played no contributory role in an alleged breach of duty. Organizing as a co-op rather than a franchise substantially limits a company's exposure to risk while still cultivating a profitable business structure. A company can find it much easier to separate itself from the tortious conduct of an alleged agent, over which they may have absolutely no control and for conduct which they should not be held liable.

It will be interesting to see how this business structure is treated by the courts in the coming years. However, at present, co-op defense is still in its formative years. This decision is a reminder of how much facts matter. By understanding your company's business structure, reading the agreement between the company and its members, and adducing the right testimony during discovery regarding the company's right of control over a securing agent, a zealous defense attorney can successfully defend a co-op, even in the absence of substantial legal precedent.

Danielle N. Malaty is an associate of Kopka Pinkus Dolin pc in Chicago, where she concentrates her practice on premises liability, product liability, employment law, municipal/public entity, construction, commercial transportation, contract breach, professional liability, and general insurance defense. Her clients include retailers, restaurants, property management companies, hardware stores, product manufacturers, cooperative business organizations, grocery stores, shopping centers, general contractors, sub-contractors, police departments, municipalities, and trucking/transportation entities.