Yours, Mine, Ours, and Theirs: The Role of Spousal Guaranties and Consents in the Franchise Relationship

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Franchisors often require a prospective franchisee to sign a personal guaranty. Should they also require the franchisee's spouse to sign a personal guaranty or consent agreement? Should the franchisee encourage his or her spouse to enter into some form of consent agreement? Why would the spouse of a franchisee even *want* to enter into the franchise relationship via either a spousal guaranty or consent?

A spousal guaranty is a document by which the non-franchisee spouse guarantees the obligations of the franchise to the franchisor. It provides the franchisor with the right to seek payment from the spouse, the spouse's personal assets, or the marital property in the event the business entity-franchisee defaults. The spousal guaranty can be executed in conjunction with the guaranty signed by the franchisee or after the franchise relationship has been established.

By comparison to a guaranty, a spousal consent often serves more diverse purposes. It can bind the non-franchisee spouse to the *non-financial* commitments in the franchise agreement, such as the covenant not to compete or restrictions on the transfer of the franchise; a spousal consent also may introduce additional terms that impact the operation of the franchise as it relates to the marital relationship between franchisee and franchisee's spouse. Moreover, a consent may address financial concerns outside of the franchise agreement, such as binding marital assets to, or shielding them from, the franchise relationship. A spousal consent may also define how the franchise itself is to be considered if the couple gets divorced. A spousal guaranty may also include terms that would make it both a guaranty and a spousal consent as we have defined them, but we are distinguishing the two documents for the purposes of this article.

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This article first discusses the overall role of spousal guaranties and consents in a franchise relationship. The advantages of a guaranty to the franchisor are obvious: it potentially gives the franchisor access to the spouse's assets and the marital property. A spousal consent by contrast is an instrument that can be used by either spouse to create or exclude an interest in the franchise generally. Additionally, a spousal consent may provide a way for the franchisor to enforce some, if not all, of the non-financial terms of the franchise agreement against the non-franchisee spouse.

The article next focuses on the two different types of state marital property laws—community property and equitable distribution—and how those laws affect a franchise relationship in the event of a divorce. Specifically, the discussion highlights the advantages of having a spousal consent executed to circumvent marital property laws to ensure that the intent of the franchisor, franchisee, and spouse are realized.

The penultimate part of the article discusses the potential impact of the Equal Credit Opportunity Act (ECOA) on the franchise relationship, specifically as it relates to married franchisees. Under the ECOA, a franchisor generally cannot refuse to deal with a prospective franchisee when the non-franchisee spouse refuses to sign a guaranty or consent.

Finally, we discuss alternatives to the traditional spousal guaranty, specifically the spousal consent. We propose that, although a franchisor should always attempt to obtain a spousal guaranty, in circumstances in which that is not possible, at least a spousal consent should be obtained. Whereas a guaranty may be viewed as one-sided in favor of the franchisor, a spousal consent offers advantages to all of the parties involved.

I. Embarking on the Franchise Relationship

A. *Reasons for the Spousal Guaranty*

Franchisors seek spousal guaranties because they bind the franchisee's spouse to the obligations of the franchisee under the franchise agreement. This may offer some practical benefit for the franchisor if the franchisee defaults on the financial obligations of the franchise agreement. If a spousal guaranty is in place, both spouses and their assets are attached to the franchise, making the status of the marital relationship irrelevant. As such, a spousal guaranty also benefits a franchisor in the event of a change in the marital relationship. In that instance, absent a spousal guaranty, there could be significantly fewer assets for the franchisor to pursue. A spousal guaranty may also benefit the divorced franchisee: it puts the other spouse on the hook for the franchise obligations rather than having the franchisee spouse shoulder the burden alone.

Another reason for a spousal guaranty is protection against a situation where the franchisee is looking to hide assets or circumvent the franchise agreement by transferring assets to the spouse.[1] A guaranty blocks this method of hiding assets if the franchisor becomes the franchisee's creditor. Franchisors need to develop a mechanism, whether through a guaranty or consent signed by the non-franchisee spouse to ensure that, at a minimum, the parties to a marital relationship are not working to undermine the franchisor.

B. *Reasons for a Spousal Consent*

Spousal consents are flexible and may be adapted for individual franchisees and their particular concerns.[2] Ultimately, a consent agreement can be viewed as akin to a "franchise prenuptial agreement" among the franchisor, franchisee, and non-franchisee spouse. A premarital agreement can be a mechanism for circumventing marital property laws when there is a divorce, and a spousal consent can function the same way. The practical effect of a spousal consent is the creation of a pre- or post-marital agreement specifically intended to address the franchise as an asset.[3] Much like a prenuptial exists to protect premarital assets and outline each person's obligations, a

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1. *See infra* Part III.C.

2. Since franchisors must include all term agreements as part of the Franchise Disclosure Documents (FDD), a disclosure problem may arise for the franchisor that elects to negotiate a consent on a case-by-case basis. However, as long as the promises and obligations of the parties to the franchise relationship are included in the FDD, there should not be an issue negotiating a consent with the non-franchisee spouse.

3. This agreement likely would be subject to the same considerations courts use to determine the enforceability of a premarital agreement. *See, e.g.*, Sides v. Sides, 717 S.E.2d 472, 473 (Ga. 2011) (citing three factors in evaluating the validity of a prenuptial agreement: (1) "Was the agreement obtained through fraud, duress or mistake, or through misrepresentation or nondisclosure of material facts?; (2) [I]s the agreement unconscionable?; and (3) Have the facts and circumstances changed since the agreement was executed, so as to make its enforcement unfair and unreasonable?" (internal citations omitted)); *In re* Marriage of Bracken, 2010 Wash. App. LEXIS 2187, *8–9 (Wash. Ct. App. Sept. 27, 2010) (identifying eight nonexclusive factors when considering the enforcement of a prenuptial agreement:

> (1) the proportional benefit between the parties,
> (2) restrictions on the creation of community property,
> (3) prohibitions on the distribution of separate property upon dissolution,
> (4) the economic means of each spouse,
> (5) preclusion of common law and statutory rights to both community and separate property upon dissolution,
> (6) limitations on inheritance,
> (7) prohibitions on awards of maintenance, and
> (8) limitations on the accumulation of separate property.

Id.

Noto v. Buffington, 2010 Conn. Super. LEXIS 675, *2–3 (Conn. Super. Ct. Mar. 22, 2010) ("Prenuptial agreements are governed by Connecticut General Statutes § 46b-36a et seq., also known as the Connecticut Premarital Agreement Act" which sets for standards for enforceability:

> (a) A premarital agreement or amendment shall not be enforceable if the party against whom enforcement is sought proves that:
>
> (1) such party did not execute the agreement voluntarily; or
> (2) the agreement was unconscionable when it was executed or when enforcement is sought; or

consent agreement in a franchise relationship can be employed in the same manner to realize the same objectives.

A spousal consent has distinct advantages for both franchisor and franchisee. For the franchisor, first and foremost, it can be used to bind the franchisee's spouse to some, if not all, of the post-franchise relationship and non-financial terms of the franchise agreement. Additionally, a consent can contain language that operates to discourage a franchisee from shielding or hiding assets from the franchisor by placing them in the name of the non-franchisee spouse or into marital property safe from attachment. Conversely, a consent could include language that specifically attaches marital property as security for the franchise's defaults on the financial obligations of the franchise agreement.

For the franchisee, a spousal consent that states whether the franchise will be marital or separate property upon divorce is beneficial because the parties will know in advance how a court will treat the franchise. A spousal consent can also be used to establish guidelines for how the increase in value of the franchise will be treated in the event of a divorce.[4] Both franchisee and franchisor may also want the post-franchise relationship provisions enforced against the non-franchisee spouse as well. It is not impossible to imagine a situation where the non-franchisee spouse after a divorce may wish to open a business substantially similar to the franchisee spouse's, utilizing the business knowledge and experience that has been learned during the marriage. Further, if a franchisee gets married after entering into the franchise agreement, a spousal consent, and its advantages, may provide an incentive for all parties to have the new spouse sign.

Accordingly, a spousal consent may be welcome to establish the expectations and obligations of the franchisor, franchisee, and non-franchisee spouse to each other when entering into a franchise relationship, during it, and after the franchise relationship ends; it operates similarly for phases of the marital relationship. A spousal consent can be as broad or as narrow as the parties choose. Ultimately, any consent agreement signed by the non-franchisee spouse that connects this spouse to the franchise agreement (or specifically does not connect them) can be advantageous to both the franchisor and franchisee.[5]

> (3) before execution of the agreement, such party was not provided a fair and reasonable disclosure of the amount, character and value of property, financial obligations and income of the other party; or
>
> (4) such party was not afforded a reasonable opportunity to consult with independent counsel.

Id. These considerations may be equally relevant to the enforceability of a spousal consent in the franchise context in the event of a divorce.

4. *See infra* note 59.

5. Although beyond the scope of this article, a spousal consent or guaranty may be beneficial to both spouses in the event of death of a franchisee. For example, either a spousal consent or guaranty may provide that, by accepting the responsibilities of a guarantor or the obligations set forth in the consent, the spouse will be named franchise successor in the event of the franchisee's

II. Binding the Non-financial Spouse to the Non-financial Provisions of the Franchise Agreement

A perfect example of the use of a spousal consent is to bind the non-franchisee spouse to the covenant not to compete contained in franchise agreements, which is an often-litigated issue.[6] Generally, there are three considerations for enjoining a non-signatory to a franchise agreement from working in the same industry as the former franchisee to circumvent the covenant not to compete found in the franchise agreement:

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death. By including language related to issues arising out of the death of the franchisee in a guaranty or consent, a franchisee and his or her spouse can obtain security and peace of mind regarding the future of the business. We also note, however, that some state laws protect the non-franchisee's spouse's interest in the business following the death of the non-franchisee spouse.

Both Bruce Schaeffer and Terrence Dunn address this topic in substantial detail. The main concerns facing a franchisee in succession planning include: (1) how to ensure the certainty of franchise transfer, specifically when death is unexpected; (2) obtaining economic benefit from the franchise for the heirs while maintaining control over operations; and (3) valuing the franchise for estate tax purposes. *See* Bruce S. Schaeffer, *Practice Tips: Succession Planning for Franchisees*, 21 FRANCHISE L.J. 90 (2001); Terrence M. Dunn, *The Franchisor's Control over the Transfer of a Franchise*, 27 FRANCHISE L.J. 233 (2008).

Of note, California and Indiana have statutes that further limit the situations in which a franchisor may refuse to consent to transfer ownership of the franchise. The California Franchise Relations Act (CAL. BUS. & PROF. CODE §§ 20000, *et seq.* (Deering 2013)) and the Indiana Deceptive Franchise Practices Act (IND. CODE ANN. § 23-2-2.7-1, *et seq.* (LexisNexis 2013)) prohibit franchisors from preventing a surviving spouse, heir, or the estate of the franchisee or a major shareholder of the franchisee from participating in the ownership of the franchise for a reasonable period after the death of the franchisee or major shareholder of the franchisee, provided that all of the franchisor's then-current standards and qualifications are satisfied. *See* Dunn, *supra*, at 238. In California, the spouse, heirs, and estate of a deceased franchisee can operate the franchise or transfer it to a qualified third party. *See* CAL. BUS. & PROF. CODE § 20027 (Deering 2013). Indiana grants the spouse, heirs, or estate the right to operate the business unfettered for a reasonable period of time. *See* IND. CODE ANN. § 23-2-2.7-2 (LexisNexis 2013). Similar language can be adopted into a consent agreement to create these rights in states where it has not been adopted by the legislature, which might encourage a spouse to provide a guaranty or consent.

6. A significant amount of case law and secondary sources discuss the enforceability of covenants not to compete against nonsignatories. *See, e.g.*, Everett v. Paul Davis Restoration, Inc., 2012 U.S. Dist. LEXIS 133682, *16–19 (E.D. Wis. Sept. 18, 2012); Comedy Club, Inc. v. Improv W. Assocs., 553 F.3d 1277, 1287 (9th Cir. 2009); Goodman Mfg. Co. L.P. v. Raytheon Co., 1999 U.S. Dist. LEXIS 13418 (S.D.N.Y. Aug. 30, 1999); Dawson v. Temps Plus, Inc., 987 S.W.2d 722, 729 (Ark. 1999); Gold Messenger v. McGuay, 937 P.2d 907, 912–13 (Colo. Ct. App. 1997); Norlund v. Faust, 675 N.E.2d 1142, 1156 (Ind. Ct. App. 1997); Kasco Servs. Corp. v. Benson, 831 P.2d 86, 90 (Utah 1992); MICHAEL R. GRAY & TAMI MCKNEW, COVENANTS AGAINST COMPETITION IN FRANCHISE AGREEMENTS (3d ed. 2012); Quentin R. Wittrock, *Litigation Against Competitors*, 32 FRANCHISE L.J. 146 (2013); Clay A. Tillack & Mark E. Ashton, *Who Takes What: The Parties' Right to Franchise Materials at the Relationship's End*; 28 FRANCHISE L.J. 88, 125–26 (2008); Michael R. Gray & Jason M. Murray, *Covenants Not to Compete and Nonsignatories: Enjoining Unfair Conspiracies*, 25 FRANCHISE L.J. 107, 112 (2006); Francis M. Dougherty, *Enforceability of sale-of-business agreement not to compete against non-signer or nonowning signer*, 60 A.L.R.4th 294 (1988).

Generally, these covenants have only been enforced against non-signatories in cases of nefarious behavior by the parties seeking to circumvent the noncompete. *See* Gray & Murray, *supra*, at 112. This article will only touch on the potential use of a spousal consent upon this common term in a franchise agreement.

(1) The franchisor must show that the former franchisee has breached the provision;
(2) The franchisor must demonstrate that the entity or individual "who is operating the competitive business conspired, acted in concert, or aided and abetted the franchisee's breach of the agreement;"
(3) While not required, a familial or close relationship substantially increases the odds of success.[7]

In this vein, the court in *Logan Farms v. Cajun Provisions*[8] enforced a covenant not to compete against the spouse of a former franchisee. In doing so, the court found the non-signing spouse was utilizing elements of the former franchise, such as recipes and clients, in her business.[9] Rather than having to undertake the three-factor analysis, a spousal consent may be used to remove, or at least limit uncertainty, and potentially avoid litigation, as to what terms of the franchise agreement are enforceable against the franchisee and the non-franchisee spouse. A franchise can benefit from a spousal consent that binds both spouses to all of the franchise agreement's terms, even without a spousal guaranty of the financial obligations.

Uncertainty remains on this issue, as some courts have held that the franchisee's spouse does not have an inherent interest in the franchise relationship, and as such, is not bound by its terms.[10] In *Everett v. Paul Davis Restoration, Inc.*,[11] for example, a franchisee's wife did not sign a non-compete and the court refused to enforce it against her personally after she bought the business from her husband and it had been terminated as a franchise. The court held that for the covenant to be enforceable, the franchisor would need to show that the wife "benefitted directly from the contract [i.e., the franchise agreement], not the business that the contract made more profitable."[12] Interestingly, the court noted that if an indirect benefit, such as profits from the business, was enough to enforce such provisions against spouses, there would be no reason to have individual guaranties in the first place.[13]

Courts have enforced other non-financial terms against non-signatories as well. A common example is when non-signatories to arbitration agreements

7. Gray & Murray, *supra* note 6, at 113.
8. Logan Farms v. Cajun Provisions, 1993 U.S. Dist. LEXIS 16687 (E.D. La. Nov. 19, 1993).
9. *Id.* at *10.
10. These cases are a reminder that franchisors must be careful to ensure clear terminology and intent when drafting franchise agreements and covenants not to compete. In determining that a spouse was not bound to the franchise agreement, a Massachusetts court simply stated that this issue was uncertain and "because Grease Monkey drafted the agreement, any ambiguity must be construed against it." Grease Monkey Int'l, Inc. v. Ralco Lubrication Serv., Inc., 24 F. Supp. 2d 120, 124 (D. Mass. 1998).
11. Everett v. Paul Davis Restoration, Inc., 2012 U.S. Dist. LEXIS 133682 (E.D. Wis. Sept. 18, 2012).
12. *Id.* at *18–19. The defendant argued and the court later agreed that Everett was "bound by the Franchise Agreement, even though she did not sign it, under the direct benefit estoppel doctrine. Under this doctrine, a nonsignatory party is estopped . . . if it knowingly seeks the benefits of the contract containing the arbitration clause." *Id.* at 15 (internal citations omitted).
13. *Id.* at *20–21.

have been compelled to arbitrate.[14] There are at least two circumstances when these arbitration provisions will be enforced: "(1) where the nonsignatory is a third party beneficiary of the contract containing the arbitration agreement; and (2) where 'a preexisting relationship existed between the nonsignatory and one of the parties to the arbitration agreement, making it equitable to compel the nonsignatory . . . to arbitrate his or her claim.' "[15] "The preexisting relationship generally gives the party to the agreement authority to bind the non-signatory. Examples of the preexisting relationship include agency, spousal relationship, parent-child relationship, and the relationship of a general partner to a limited partnership."[16] Once again, there appears to be recognition by some courts that there are situations in which the terms of a contract can be enforced against non-signatories when it is necessary to protect the fruits of the contract. For this reason, a spousal consent could be appealing to both spouses because it can address this issue by identifying what terms of the franchise agreement will be enforced both during and after the franchise relationship (and the marital relationship) by the franchisor against the non-franchisee spouse.

Another reason to obtain a spousal consent is protection against a situation in which the franchisee is looking to hide assets or circumvent the franchise agreement by transferring assets to the spouse. A guaranty blocks this method of hiding assets if the franchisor becomes the franchisee's creditor. If a guaranty is not obtainable, a franchisor may be able to use a spousal consent to protect against this situation, such as through language stating that assets transferred from the franchisee to the non-franchisee spouse may be attached if the transfer is done within a certain period of time or during a period in which the franchisee has defaulted on his or her financial obligations. In this instance, a spousal consent may not prevent the transfer of assets but would allow the franchisor to reach the non-franchisee spouse's assets.

In the triangular relationship among franchisor, franchisee, and the franchisee's spouse, all have identifiable interests to protect. A spousal consent allows for input by each of these parties on how their interests will be considered in both the franchise and the marital relationship. While it may appear as if the franchisor is unnecessarily dabbling into the world of family law, in reality, the franchise relationship can easily cross into that domain in a variety of circumstances. We discuss some of these circumstances in the next section. By encouraging the adoption of a spousal consent agreement among all the parties, this type of long-term planning can benefit everyone in the event of a breakdown of the relationships.

14. *See* Crowley Maritime Corp. v. Boston Old Colony Ins. Co., 158 Cal. App. 4th 1061, 1069–70 (Cal. Ct. App. 2008).
15. *Id.* (citation omitted).
16. *Id.*

III. Marital Property Laws: An Analysis of Community Property and Equitable Distribution States

A change in the marital relationship can also impact the franchise relationship. A state's marital property laws must be considered in evaluating this issue. A spousal consent may provide all parties with some certainty about the franchised business's continuity after the marital relationship ends. It is important to remember, however, that although some franchise agreements may restrict transfer of the franchise between spouses or to heirs, in some states, franchise relationship laws trump the terms of the franchise agreement.[17] Accordingly, in states without these franchise relationship laws, spousal consents and guaranties are particularly advantageous. Every state considers whether there is an agreement between the spouses before a court will get involved in dividing marital property and will attempt to honor that agreement.[18] A spousal consent agreement should be viewed as another agreement that can be utilized by married parties so that their property is distributed based upon their mutual agreement in the event of a divorce.

A. *Community Property States*[19]

Community property is generally all property acquired during marriage. Assets earned and liabilities jointly incurred during the marriage are split evenly, but anything brought into the marriage at its inception remains

17. *See supra* note 5 (discussion on franchise transfer laws in California and Indiana).

18. For example, New York courts are instructed to use restraint in evaluating separation agreements. H.K. v A.K., 950 N.Y.S.2d 723 (N.Y. Sup. Ct. 2012) (citing Ricca v. Ricca, 57 A.D.3d 868, 870 (N.Y. App. Div. 2008); Korngold v. Korngold, 26 A.D.3d 358 (N.Y. App. Div. 2006). To ensure that freedom of the parties was preserved despite the fiduciary relationship existing between husband and wife,

> courts have thrown their cloak of protection about separation agreements and made it their business, when confronted, to see to it that they are arrived at fairly and equitably, in a manner so as to be free from the taint of fraud and duress, and to set aside or refuse to enforce those born of and subsisting in inequity.

Id. (citing *Christian*, 42 N.Y.2d at 72); Kabir v. Kabir, 85 A.D.3d 1127 (N.Y. App. Div. 2011); Martin v. Martin, 74 A.D.2d 419, 423 (N.Y. App. Div. 1980). *H.K.* noted that the

> court should not interfere "when there has been full disclosure between the parties, not only of all relevant facts but also of their contextual significance . . . A spouse, when they finally bind themselves, and waive their right to statutory remedies, should be regarded as having done so only when they are in possession of every material fact affecting the act of agreement.

Id.

19. There are only nine community property states: Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin. The remaining forty-one states all subscribe to the equitable distribution model. Alaska is unique in allowing couples to elect which property will be classified as community property. Either before or during marriage, couples can choose to create a community property agreement or a community property trust. In doing so, they designate all their property as community property, or they can specify in their agreement that certain items, such as earnings during the marriage, remain separate property.

solely the property of its original owner.[20] As such, in community property states, even if only one spouse enters into a franchise agreement post-marriage, that franchise is presumed community property.[21] Upon divorce, a court will assign each spouse's sole and separate property to that spouse. It will also divide the community, joint tenancy, and other property held in common equitably without regard to marital misconduct.[22] If the parties are not able to come to an alternative agreement, the court will divide this property equally.

Agreeing in advance how an asset will be designated upon divorce is common. For example, one spouse may transfer real property by a written agreement that shows the intent that the asset be sole and separate property going forward,[23] or one spouse could change separate property to community

20. *See In re* Field, 440 B.R. 191, 195–96 (Bankr. D. Nev. 2009); *In re* Marriage of Tackett, 2007 Wash. App. LEXIS 1119, *11–12 (Wash. Ct. App. May 15, 2007); *In re* Marriage of Weaver, 127 Cal. App. 4th 858, 864–65 (Cal. Ct. App. 2005).

The operation of a franchise fits squarely within this analysis. In some community property states, a guaranty signed by only one spouse is enforceable only against that spouse's separate property and share of the community property. *See* TEX. FAM. CODE ANN. § 3.201 (2012); ARIZ. REV. STAT. §25-215 (LexisNexis 2013). *See also* Nelson v. Citizens Bank & Trust Co., 881 S.W.2d 128, 130–31 (Tex. App. 1994) (holding wife not personally liable for husband's guaranty of corporate note); Rackmaster Sys. v. Maderia, 193 P.3d 314, 317 (Ariz. Ct. App. 2008) (finding that a guaranty signed only by the debtor could not bind the community.). *But see* CAL. FAM. CODE § 910(a) (Deering 2013) ("[T]he community estate is liable for a debt incurred by either spouse before or during marriage, regardless of which spouse has the management and control of the property and regardless of whether one or both spouses are parties to the debt or to a judgment for the debt.").

In Wisconsin, the non-franchisee spouse's separate property and share of the community property cannot be sought for the debts of the franchisee-spouse. *See In re* Groff, 131 B.R. 703, 709 (Bankr. E.D. Wis. 1991) ("[A]ny lender approving a loan based upon such a guaranty in the absence of a spouse's consent, takes a risk that, in case of default, only the guarantor's non-marital property and the guarantor's interest in marital property is reachable."). A spousal guaranty would make available to the creditor franchisor any and all marital assets in addition to the separate assets of the non-franchisee spouse.

21. However, in *Rackmaster Systems v. Maderia*, a debtor and his wife successfully argued that community property could not be reached, despite liability for the personal guaranty executed by the debtor spouse entered into alone on behalf of his corporation. 193 P.3d 314, 317 (Ariz. Ct. App. 2008). Arizona follows a traditional interpretation of marital property for community property states. ARIZ. REV. STAT. § 25-318 (LexisNexis 2013). The court held that under Arizona law, a guaranty signed only by the debtor could not bind the community. *Id.* at 317. In concluding that debt was barred from being collected with the community property, the Arizona court noted that it was the legislature's intent to protect the "substantive rights of the non-signing spouse." *Id.* at 318. The court noted that a guaranty is a specific *exception* to the general power of one spouse to incur debts and bind the community. *Id.* at 319. Thus, if a franchise relationship was entered into unilaterally, the franchisor cannot touch any communal marital assets, as the franchise is solely and completely in the possession of the franchisee spouse. *See also* Consol. Roofing & Supply Co. v. Grimm, 682 P.2d 457, 463 (Ariz. Ct. App. 1984) (holding that a guarantee signed only by the husband was unenforceable against his wife or their community). This case highlights the benefits of only one spouse signing the guaranty. When the franchisee does not want to expose marital property to creditors, or the franchisor knows the franchisee's spouse will not sign a guaranty, a consent can be a useful alternative to protect and enforce other terms of the franchise agreement.

22. *See* Toth v. Toth, 946 P.2d 900, 901–02 (Ariz. 1997) (citing ARIZ. REV. STAT. § 25-318).

23. *See* Gallegos v. Gallegos, 2007 N.M. App. Unpub. LEXIS 50, *3 (N.M. Ct. App. Sept. 4, 2007) (citing N.M. STAT. ANN. § 40-3-8(a) (5)); *In re Marriage of Weaver*, 127 Cal. App. 4th at

property by a change in title.[24] The change in property designation may also be done unintentionally if asserts are commingled. This occurs when separate assets and community assets become indistinguishable; this happens often with bank accounts.[25] As such, a franchise started prior to marriage will be considered community property if it has been commingled with marital funds to purchase, finance, or grow the business.

Courts have acknowledged that there are occasions, such as a business, when it is virtually impossible to effectively divide certain property of the divorcing couple.[26] In this situation, a court is authorized to make an equitable division of the business by awarding an amount of money to one spouse representing that spouse's share of the value of the business, but the specific property would be set aside for the other spouse.[27] Similarly, a trial court may in the exercise of its discretion order that a community property asset, such as a business, be sold in order to effectuate an equal division of the community property.[28]

In this light, the potential benefits of a spousal guaranty or consent begin to become manifest. Language in a spousal consent may be used to clearly delineate whether the franchise will be designated as separate or marital property or how it will be distributed in the event of divorce to provide clarity to all parties on what is expected of them both during and potentially

865 ("Under CAL. FAM. CODE § 2581, all property held in joint title by spouses during marriage is presumed to be community property upon dissolution, rebuttable only by written evidence to the contrary." This evidence must consist of "clear statement in the deed or other documentary evidence of title by which the property is acquired that the property is separate property and not community property, or by proof that the parties have made a written agreement that the property is separate property.").

24. *See* Steinmann v. Steinmann, 749 N.W.2d 145, 158 n.16 (Wis. 2008) ("Wis. Stat. § 766.31 explicitly allows property classified as individual property under a marital property agreement (as well as gifts, inheritances, and other separate property) to be reclassified as marital property through a gift, deed, or other conveyance." (internal citation omitted)); *In re* Marriage of Sims, 2003 Wash. App. LEXIS 86 (Wash. Ct. App. Jan. 23, 2003) ("[P]roperty acquired before marriage may be converted to community property if supported by a written agreement or if given as a gift to the marital community.").

25. *See* Lawson v. Lawson, 828 S.W.2d 158, 160 n.1 (Tex. App. 1992) (defining commingling as situations when there has been a blending of "community property and separate property the person claiming the status of separate property has the burden of tracing the property, and if the segregation of that portion which is claimed as separate property is impractical or impossible, the property becomes a part of the community estate of the parties."); Brown v. Meredith, 220 Cal. App. 2d 762, 764 (Cal. Ct. App. 1963) ("When separate and community funds are commingled the property remains unchanged in character as long as it can definitely be traced and ascertained.").

26. *See* Martin v. Martin, 752 P.2d 1038, 1043 (Ariz. 1988).

27. *Id.*

28. *See In re* Marriage of Rives, 130 Cal. App. 3d 138, 156 (Cal. Ct. App. 1982). Here, the court noted that selling a business and dividing the proceeds is appropriate because this

> division would avoid valuation problems, eliminate the need to place a disproportionate risk of loss on either party, be impervious to charges of favoritism, apportion the risk of future tax liabilities equally, accomplish an immediate division of the property, and provide the parties with the most post-dissolution economic stability.

after the marital relationship.[29] Although there is some difference from state to state in how this is handled, the marital property analysis is relatively similar; the cases below highlight how they apply to a franchise in community property states.

Absent a written agreement requiring a particular division of property, California law requires an equal division of the community estate.[30] Equal division means that from the total fair market value of the community assets, the joint obligations are subtracted, yielding the net community estate, which is divided in two. Unless agreed otherwise, each spouse must receive half of the net community estate.

In *Tougas v. Tougas*, a Hawaii case applying California law, a consent agreement specifically excluded a spouse from the assets of a family partnership.[31] Here, the wife's parents had created a partnership as part of their estate planning to provide exclusively for their three children; each of their children's spouses signed consent forms acknowledging that the partnership was "separate property, inaccessible during a divorce action."[32] A second partnership was then formed, but no consent forms were signed regarding the second business.[33] The family court determined that the husband was not entitled to any share of his wife's interest in the two partnerships formed by her parents, but awarded the husband 75 percent of the business that he and his wife operated.[34]

On appeal, the wife argued that she should have been awarded 50 percent of the marital business because both spouses had "contributed as equal partners to the formation and operation of [the business]."[35] The court noted that due to its discretionary power to make a just and equitable distribution of the estate, separate property holdings may factor into the court's consideration.[36] Finding that the wife's "partnership interests should [not] offset [the husband's] interest in the marital estate" in light "of the spousal consent agreement, which operates as a waiver by Husband of all rights to the partnerships," the court affirmed the family court's division of the jointly held business that awarded the wife 25 percent of the marital business.[37] Therefore, courts may alter the ultimate distribution of the marital estate based on the respective separate conditions of the spouses.

29. A franchisor must also ensure that the organizational documents (i.e., Franchise Agreement, LLC Operating Agreement or shareholder agreements) do not conflict with the terms of the consent.

30. In California, community property is subject to execution even if only one spouse is sued or if judgment is obtained against one spouse alone. *See* CAL. FAM. CODE §§ 910-916 (Deering 2013).

31. 868 P.2d 437, 450 (Haw. 1994).

32. *Id.* at 441.

33. *Id.*

34. *Id.* at 443.

35. *Id.* at 450.

36. *Id.* at 449–50.

37. *Id.* at 450.

In *Brehm v. Brehm*, the Texas Court of Appeals faced issues related to the distribution of a franchise business.[38] Here, the husband challenged the characterization and division of property by the trial court. He claimed that he had expended $170,000 of his separate property on community assets, such as the real estate where the family business was located, the franchise fee for the business, and the equipment used in the business.[39] The husband argued that he should be reimbursed for the money he spent toward community property.[40] Due to the husband's failure to provide clear and convincing evidence that the funds he used to purchase the community property were from his separate property, the court denied him any reimbursement.[41] The husband also argued to reverse the trial court's order that the community property business and real property be sold.[42] In upholding the decision to sell the property, the court held that there were insufficient community assets to allow the court to partition these properties in kind and that nothing in the court's order would have prevented the husband from buying the remainder of the business, but he took no steps to do so.[43]

Brehm is an excellent example of the protections that can be built into a spousal consent for the franchisee. Terms could be written into the consent agreement to ensure that expenditures are reimbursed, that there is a first option for purchase in the event the franchised business is deemed community property, or similar type provisions. This case is also a good example of the potential pitfalls a franchisee may face if division of the franchise marital property is left to the discretion of the courts.

38. 2000 Tex. App. LEXIS 2079, *7–13 (Tex. App. 2000). Texas defines community property as all property and debt acquired or earned from the date of marriage until the marital cut-off date that is not separate property. *See* TEX. FAM. CODE ANN. § 3.001(2012).The court starts with a presumption that all property held by either spouse during marriage is community property. *See Brehm*, 2000 Tex. App. LEXIS 2079, at *7. Like other community property states, this property will be divided by the court if the parties are unable to come to an agreement on their own. However, the court divides the community in a just and right fashion that means whatever the judge thinks is fair under the circumstances, so the equal split found in other community property states does not apply in Texas. In a decree of divorce or annulment, the court can order a division of the estate of the parties in a manner that the court deems just and right, having due regard for the rights of each party and any children of the marriage. *See* TEX. FAM. CODE ANN. § 3.001, *et seq.* (2012). In Texas, property that was owned by a spouse prior to marriage can be designated as separate property. To keep an asset separate, a spouse must prove by clear and convincing evidence that the asset is separate property. *See Brehm*, 2000 Tex. App. LEXIS 2079, at *7. Separate property includes anything that belongs to one spouse before marriage and kept separate throughout the marriage. Once a spouse proves that an asset is separate property, it remains his or hers, and the court cannot award it to the other spouse.

39. *Id.* at *9.

40. *Id.* The court noted that "in deciding whether to award reimbursement, the trier of fact should consider the benefits and detriments to each estate." *Id.* at *10 (internal citation omitted). "Reimbursement is not available as a matter of law but lies in the discretion of the court." *Id.* (internal citations omitted).

41. *Id.* at *10–11.

42. *Id.* at *11. The husband argued that the forced sale devalued the business and it should have been portioned to allow him the option to purchase the remainder of the business from his ex-wife. *Id.*

43. *Id.* at *12–13.

B. *Equitable Distribution States*[44]

Equitable distribution means that if the parties cannot mutually agree on how to divide their assets, the marital property is divided in a manner the court deems fair.[45] These states seek to find a fair and reasonable division of property, not necessarily one that is split evenly.[46] States identify factors in equitable distribution but these are often nonexhaustive; ultimately courts consider the broad picture of the marital relationship in making this determination.[47] While the factors vary state to state, the general focus is centered on variables such as the length of the marriage and the contribution of each spouse to the assets. Ultimately, each state is applying its own totality of the circumstances analysis. The court will determine what property is marital, and after putting a value on this property, a portion will be distributed to each spouse.[48] The court does not have the right to distribute any separate property. Separate property includes gifts and inheritances, unless they have been used to benefit both spouses as a married couple, which then renders those assets marital property.[49] Commingling can also occur in equita-

44. *See supra* note 19.

45. *See* Seymour v. Seymour, 960 So. 2d 513 (Miss. Ct. App. 2006) (noting that equitable distribution does not mean equal distribution and that "the goals of equitable distribution are a fair division of marital property based on the facts of each case and termination of the legal relationship in a manner which each party may realize self-sufficiency").

46. In general, equitable distribution states define the marital estate in two ways: all-property, which is also called the kitchen sink method, and dual classification, which means the spouses must determine when an asset was acquired to determine if it is separate property and immune from distribution. Fourteen states (Connecticut, Indiana, Kansas, Massachusetts, Michigan, Mississippi, Montana, New Hampshire, North Dakota, Oregon, South Dakota, Vermont, Washington, and Wyoming) are "all property" or "pure equitable distribution" or "kitchen sink" states. This distinction means that a judge can distribute any and all separate and marital assets of either spouse in the manner the court finds equitable. *See* Wendt v. Wendt, 1998 Conn. Super. LEXIS 1023, 66–67 (Conn. Super. Ct. Mar. 31, 1998).

Eight states (Alabama, Alaska, Arkansas, Hawaii, Iowa, Minnesota, Ohio, and Wisconsin) include separate property in the marital estate if there is a showing of need by the other spouse. *See* Brown v. Brown, 947 P.2d 307, 313 (Alaska 1997) ("The court must determine whether invasion of separate property is necessary to balance the equities. If invasion is necessary, then the court must determine what separate property the parties own, value it, and adjust the initial division as needed.") (citing ALASKA STAT. § 25.24.160)).

47. For examples, *see* C.R.S. § 14-10-113 (2012); 13 DEL. CODE § 1513(a)(2013); FLA. STAT. § 61.075(1) (2012); 750 ILL. COMP. STAT. § 5/503(d); KY. REV. STAT. § 403.190 (2013); MD. CODE ANN., FAM. LAW § 8-205(b) (2012); N.Y. DOM. REL. LAW § 236 (2013); 23 PA. CONS. STAT. § 3502(a) (2013); VA. CODE ANN. § 20-107.3(E)(2013).

48. *See* Hoverson v. Hoverson, 828 N.W.2d 510, 515–16 (N.D. 2013); Hill v. Hill, 2012 Tenn. App. LEXIS 709, *8 (Tenn. Ct. App. Oct. 5, 2012); Helms v. Helms, 2006 N.C. App. LEXIS 1822, *7-8 (N.C. Ct. App. Aug. 15, 2006); Vizel v. Vizel, 2005 N.Y. Misc. LEXIS 3471, *6 (N.Y. Sup. Ct. 2005); Cousino v. Cousino, 2001 Ohio App. LEXIS 4879, 5–6 (Ohio Ct. App. Nov. 2, 2001); Armistead v. Armistead, 1998 Va. App. LEXIS 69 (Va. Ct. App. Feb. 3, 1998); Scott v. Scott, 653 A.2d 1017, 1024 (Md. Ct. Spec. App. 1995); Chotiner v. Chotiner, 829 P.2d 829, 831 (Alaska 1992).

49. *See* Reed v. Reed, 71 Va. Cir. 78, 81 (Va. Cir. Ct. 2006) ("The classification of property can be changed from separate to marital by the nature and character of its use and maintenance by the parties during the marriage.") (internal citation omitted).

ble distribution states.[50] Therefore, absent any form of spousal consent or marital agreement in these states, the franchisee spouse risks a court splitting the business interests between the parties in an undesirable fashion.[51] If the franchise is determined to be marital property, it will be subject to the same analysis as the rest of the marital property.[52]

Absent an agreement to the contrary, courts will determine the value of a business or franchise and use that figure as part of the equitable distribution of the marital estate.[53] When a franchise is separate property, the increase in value of the business has been held to be marital property when it has been supported by the marital estate.[54]

50. *See, e.g.*, Wilburn v. Wilburn, 2013 S.C. LEXIS 24, *13 (S.C. Feb. 20, 2013)

> Property that is non-marital when acquired may be transmuted into marital property if it becomes so commingled with marital property that it is no longer traceable, is titled jointly, or is used by the parties in support of the marriage or in some other way that establishes the parties' intent to make it marital property.

Id. Fleishhacker v. Fleishhacker, 39 So. 3d 904 (Miss. Ct. App. 2009) ("[w]hen an individual commingles non-marital assets with joint marital assets, the non-marital assets are converted into marital assets, subject to an equitable distribution unless subject to an agreement to the contrary."); Robinson v. Robinson, 613 S.E.2d 484, 494 (Va. Ct. App. 2005) ("When marital property and separate property are commingled by contributing one category of property to another, resulting in the loss of identity of the contributed property, the classification of the contributed property shall be transmuted to the category of property receiving the contribution.") (citing VA. CODE ANN. § 20-107.3(A)(3)(d))); Tomlin v. Tomlin, 1987 Ohio App. LEXIS 6101, at*7 (Ohio Ct. App. Mar. 16, 1987) (holding that non-marital property may be changed into marital property if a gift of non-marital property into co-tenancy with the other party is made or if non-marital property is commingled with marital property); Sturgis v. Sturgis, 663 S.W.2d 375, 379–80 (Mo. Ct. App. 1983) (finding that when both marital and non-marital funds are deposited in the same account, those funds become marital property. "Such commingling is indicative of an intent on the part of the owner of the pre-marriage property to contribute it to the marital estate. It makes no difference whether title to the property acquired is held individually.").

51. *See* Reynolds v. Reynolds, 2010 Va. Cir. LEXIS 73, *10 (Va. Cir. Ct. July 22, 2010).

52. As mentioned earlier, a spousal guaranty allows the franchisor to attach all of the marital property to satisfy the franchise's debts. Absent this guaranty, marital property cannot be used to satisfy the debt of the spouse who entered into the franchise agreement alone. Essentially, the non-franchisee spouse has no specific or quantifiable interests in the other spouse's separate property and therefore no obligation to the franchisor. *See* Am. Guar. & Liab. Ins. Co. v. Timothy S. Keiter, P.A., 360 F.3d 13, 19 (1st Cir. 2004) ("[U]nder Maine law, a non-owner spouse does not, absent a divorce situation, acquire by virtue of the marital relationship alone an interest, beneficial or otherwise, in the owner-spouse's property.") (citing Long v. Long, 697 A.2d 1317, 1321 (Me. 1997) ("the 'marital property's designation grants no present rights [to the non-owner spouse] in the property during the marriage")).

The income generated during marriage to support the marital home and family will be considered marital property, but not the franchise business itself. *See, e.g.*, *In re* Marriage of Dann, 973 N.E.2d 498, 520 (Ill. App. Ct. 2012) (noting that proceeds from a non-marital business that have been received during marriage are presumptively marital property); Sprock v. Sprock, 882 S.W.2d 183, 187 (Mo. Ct. App. 1994) ("In Missouri, the general rule is that income earned from non-marital property acquired after marriage is marital property.").

53. *See In re* Marriage of Balanson, 25 P.3d 28, 36 (Colo. 2001) ("Once property has been deemed to be marital, a court must value the property in order to make an equitable division.").

54. *See, e.g.*, Fleishhacker v. Fleishhacker, 39 So. 3d 904, 910 (Miss. Ct. App. 2009) (holding that if an asset's value increased resulting from a spouse's efforts, the appreciation is marital); Robinson v. Robinson, 613 S.E.2d 484 (Va. Ct. App. 2005) ("Although the increase in value of separate property may be classified as marital property if attributable to either party's personal efforts, the underlying asset itself does not lose its separate character. (citing VA. CODE ANN.

When a business is owned by only one spouse, a court faces issues of both classification and equitable division upon divorce. In *Hankins v. Hankins*,[55] for instance, the wife appealed the trial court's decision that her husband's chicken farm was separate property. The wife argued that although the business was separate property when they married, the farm constituted marital property at the time of the couple's divorce because the capital investments made in furtherance of the business "were acquired during the marriage."[56] The Mississippi Court of Appeals found that the chicken farm should remain the husband's separate property because of factors such as: the husband alone obtained loans for the chicken farm, the wife did not contribute financially to the chicken farm, and the wife did not work on the chicken farm.[57] While the court concluded that both the farm and the value of the equipment should not have been included in the marital estate, it then distinguished the categorization of the business's value.

> [T]he relationship between a wage-earning spouse and a homemaking spouse is symbiotic. We presume that the efforts of each make the contributions of the other possible. The contributions are to be considered equal. [The wife] is not entitled to a portion of the business itself or of the value of equipment but she is entitled to that which she helped to create. She is entitled to an equitable distribution of the accumulated portion, or the increase in value of the business during the course of the marriage. It is this increase in value which should have been included in the calculation of the marital estate.[58]

Hankins is an excellent example of how a court might address a business held by one spouse and what factors it will consider. There is an implication that if the wife made any sort of financial contribution or direct investment into the business's operation, the business itself, not just the increased value, might have been considered marital property.[59]

§ 20-107.3(A)(3)(a))); Duffey v. Duffey, 416 N.W.2d 830, 832 (Minn. Ct. App. 1987) ("The increase in the value of non-marital property attributable to the efforts of one or both spouses during their marriage, like the increase resulting from the application of marital funds, is marital property. . . . [On the other hand,] an increase in the value of non-marital property attributable to inflation or to market forces or conditions, retains its non-marital character.").

55. Hankins v. Hankins, 866 So. 2d 508, 511 (Miss. Ct. App. 2004).

56. *Id.*

57. *Id.* at 512.

58. *Id.* (internal citations omitted).

59. In *Smith v. Smith*, the Arkansas Court of Appeals affirmed an award to the wife for her contributions during the marriage toward the increase in value of the husband's non-marital property. 798 S.W.2d 442 (Ark. Ct. App. 1990). The court found that the increase in the value of property acquired prior to marriage was specifically exempted from the definition of marital property. *Id.* at 446. The court also noted its ability to make other equitable divisions, holding that while this increase in value is not marital property, recognizing a spouse's contributions toward that increase in value when making a property division is appropriate. *Id.* at 447. The court recognized the broad power given to courts under the statute to distribute all property in divorce, both non-marital and marital property, in order to achieve a fair and equitable division. Accordingly, the award of non-marital property to the wife based on her contributions toward the increase in value was upheld. *Id.* at 447–48. With a spousal consent, issues related to distribution of the franchise due to a spouse's contributions and the increase in the franchise's value can remain in the hands of the franchisee.

Even if the franchisee entered into additional franchise agreements during the marriage to expand a pre-nuptial franchise relationship, these franchises may still be considered separate property and not property that has been acquired during the marriage. For example, a "continuation of [the] premarital business" has been held to remain part of premarital property, and therefore separate property.[60] In *DH v. JH*,[61] a Delaware court equated the signing of new franchise agreements to the acquisition of new equipment, which a court previously held to be part of premarital property. Further, the court found that the additional assets acquired by the husband's business and the increase in value of the business alone did not comprise marital property.[62] The court drew a distinction between "increases in value to premarital property" and the acquisition of additional property when holding that these increases are "excluded from the marital estate."[63]

The court in *DH* also examined whether the wife's contributions to the franchise created a marital property interest in either the husband's interest in the franchise or the franchise's assets.[64] The wife argued that (1) any monetary contribution to the business "created a marital interest in the business because they otherwise would have been used for the family," and (2) her willingness to be a guarantor on a lease for one of the franchise locations was a "contribution to the equity" of the business, and such equity should be considered marital.[65] The court rejected both arguments because the wife was unable to show that any of her contributions increased the value of the husband's business interest.[66] The inference is that if marital property is used to increase the value of the franchise, this increase will be classified as marital property.

In *In re Marriage of Snyder and Snyder*,[67] the Oregon Court of Appeals upheld the trial court's division of marital property, including two franchises that were owned by the spouses. Approximately thirteen years into the marriage, the parties sold most of their property to acquire a Dairy Queen business that provided most of the family income.[68] Later, the husband devoted a substantial portion of his time to a Papa Aldo's Pizza franchise that the spouses acquired together.[69] In its property division, the trial court awarded the husband the Dairy Queen business and real estate and other property. The wife was awarded the family home, cash assets that were already held

60. DH v. JH, 2012 Del. Fam. Ct. LEXIS 49, at *19–20 (Del. Fam. Ct. Aug. 16, 2012).
61. *Id.*
62. *Id.* Conversely, the court noted that had the husband's percentage interest in the business increased during the marriage, this increase would have been considered marital property. *Id.* at *19 n.28 (citing *In re* Marriage of Scott, 1996 Del. Fam. Ct. LEXIS 148 (Fam. Ct. Dec. 12, 1996)).
63. *Id.*
64. *Id.* at *21.
65. *Id.* at *21–22.
66. *Id.*
67. *In re* Marriage of Snyder and Snyder, 792 P.2d 478, 479 (Or. Ct. App. 1990).
68. *Id.*
69. *Id.*

in her name, other property, and an equalizing judgment against the husband.[70] The court ordered the husband to sell the Papa Aldo's franchise and divide the proceeds equally with the wife, or, if he did not sell it by a set date, pay the wife for her portion in the business.[71] Thus, each party would ultimately receive an approximately equal portion of the marital estate.[72]

The wife appealed the lower court's decision regarding the duration and amount of spousal support.[73] She argued that she was entitled to permanent support because, among other reasons, as a result of the husband being awarded the marital business for which she had given up other opportunities, employment, and training, he would have a future earning capacity far greater than hers.[74] Based on these factors, the court awarded the wife permanent support.[75] Although this case arose out of a franchise owned by both spouses, the factors the court used to award the wife permanent support are readily applicable where only one spouse has entered into a franchise agreement.

In equitable distribution states, the court has significant discretion in the division of the marital estate.[76] An advantage to the franchisor in having a spousal consent would be to establish restrictions on transfers and ownership. By having an agreement between spouses in place, in the event of divorce the court will have guidelines to follow in determining the division of the assets, including those related to the franchise, rather than subjecting them to an equitable property determination and divestment.[77]

C. *Tenancy by the Entirety*

Tenancy by the entirety is a form of joint ownership by a married couple with neither partner able to act without the other's consent and each having

70. *Id.*
71. *Id.*
72. *Id.*
73. *Id.*
74. *Id.*
75. *Id.* at 479–80.
76. *See, e.g.*, Augspurger v. Hudson, 802 N.E.2d 503, 512 (Ind. Ct. App. 2004) ("Subject to the statutory presumption that an equal distribution of marital property is just and reasonable, the disposition of marital assets is committed to the sound discretion of the trial court."); Sexton v. Sexton, 125 S.W.3d 258, 264–65 (Ky. 2004); Anthony v. Anthony, 2001 Conn. Super. LEXIS (Conn. Super. Ct. Dec. 3, 2001); Khajanchi v. Khajanchi, 537 S.E.2d 845, 848–49 (N.C. Ct. App. 2000) ("Upon a party's application for equitable distribution, the trial court is to determine what is marital property and provide for an equitable distribution of such property.") (internal citations omitted)); Waits v. Waits, 1993 Tenn. App. LEXIS 173, *7 (Tenn. Ct. App. Feb. 26, 1993) ("Trial courts have wide latitude in dividing the marital estate in divorce cases."); Mellon Bank, N.A. v. Holub, 583 A.2d 1157, 1162 (Pa. Super. Ct. 1990) (noting that there is no easy way to divide marital property: "[t]he court has flexibility of method and concomitantly assumes responsibility in rendering its decisions."); Booth v. Booth, 541 N.E.2d 1028, 1030 (Ohio 1989) (holding that a trial court must have discretion to do what is equitable upon the facts and circumstances of each case).
77. *See* Cloud v. Brand, 259 S.W.3d 439, 443 (Ark. 2007) ("Knowing the intent of a spouse could aid a court in determining what was marital property and how that property should be equitably distributed in a divorce action.").

the sole right to the property should the other die.[78] This form of joint ownership by a married couple is worth mentioning because in some states it overlays the marital distribution laws discussed above. Under a tenancy by the entirety, creditors of an individual spouse may not attach and sell the interest of a debtor spouse: only creditors of the couple may attach and sell the interest in the property owned by tenancy by the entirety.[79] Property held in tenancy by the entirety is not subject to execution to satisfy the debts of either spouse individually.[80] In states with tenancy by the entirety, having the spouse sign a guaranty again opens up the potential of recovery from the marital property that would otherwise be exempt. Absent this guaranty, franchisors may have no way to enforce or collect against the franchisee spouse because all of the couple's assets may be held in tenancy by the entirety.

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78. *See, e.g.*, Levinson v. R&E Prop. Corp., 395 B.R. 554, 558 (E.D.N.Y. 2008) (finding that a tenancy by the entirety is an estate in land

> shared by husband and wife, whereby at the death of either the survivor is entitled to full fee simple ownership. The survivor takes the entire estate at the death of the deceased co-tenant not by virtue of that death, but because, in law, each was viewed to own the entire estate from the time of its creation. (internal citations omitted).

Popky v. United States, 419 F.3d 242, 244–45 (3d Cir. 2005) (explaining longstanding Pennsylvania common law definition of tenancies by the entirety); Beal Bank, SSB v. Almand & Assocs., 780 So. 2d 45, 52 (Fla. 2001) ("Tenancy by the entireties, as defined by applicable Florida law, is a unique form of property ownership only married couples may enjoy."); Shwachman v. Meagher, 699 N.E.2d 16, 18 (Mass. App. Ct. 1998) ("[T]he essence of the common law tenancy by the entirety, and the feature distinguishing it from other forms of concurrent ownership, was the wife's inchoate survivorship right, which the common law deemed indestructible, and inalienable except by the express written deed of both husband and wife." (internal citations omitted)); Rinehart v. Anderson, 985 S.W.2d 363, 367 (Mo.Ct. App. 1998) (noting that Missouri cases define tenancy by the entirety as "a form of ownership in property created by marriage in which each spouse owns the entire property rather than a share or divisible part, and thus at the death of one spouse, the surviving spouse continues to hold title to the property."); Talbot v. United States, 850 F. Supp. 969, 972 (D. Wyo. 1994) (establishing characteristics of a tenancy by the entireties estate); Baldwin v. United States, 805 F. Supp. 1026, 1030 (S.D. Fla. 1992) ("A tenancy by the entirety is by definition an undivided right of possession, title, and enjoyment of the whole property."); *see also* BLACK'S LAW DICTIONARY 1465 (6th ed. 1990) (defining tenancy by the entirety as "a tenancy which is created between a husband and wife and by which together they hold title to the whole with right of survivorship so that, upon death of either, [the] other takes [the] whole[.]").

79. Tenancy by the entirety jurisdictions include Alaska, Arkansas, Delaware, District of Columbia, Florida, Hawaii, Maryland, Massachusetts, Mississippi, Missouri, New Jersey, Oklahoma, Pennsylvania, Rhode Island, Tennessee, Vermont, Virginia, and Wyoming. The following states allow tenancy by entirety for real estate only: Illinois, Indiana, Kentucky, Michigan, New York, North Carolina, and Oregon.

80. *See* Howard Sav. Bank v. Cohen, 607 A.2d 1077, 1079–80 (Pa. Super. Ct. 1992) ("It is also a settled principle [in Pennsylvania] a husband and wife do not own separate interests in entireties property which can be reached by their individual creditors."); *see also* Valvanis v. Milgroom, 2008 U.S. Dist. LEXIS 42387 (D. Haw. May 22, 2008):

> In a tenancy by the entirety, neither husband nor wife has a separate divisible interest in the property held by the entirety that can be conveyed or reached by execution. Therefore, an estate by the entireties is not subject to the claims of his or her individual creditors during the joint lives of the spouses. (internal citations omitted).

IV. Equal Credit Opportunity Act Limits Demands on a Non-Franchisee Spouse

The Equal Credit Opportunity Act (ECOA) prohibits creditors from discriminating against applicants for credit on the basis of their being in certain protected classes, including marital status.[81] Whether a franchise agreement is considered a credit instrument under the ECOA is not clear, but seems likely under certain circumstances, such as when the franchise that will be operated jointly or secured by jointly held property.[82] The ECOA's purpose is to protect one party to a marriage from the obligations of the other spouse, especially if the applicant independently qualifies under the lender's standards of creditworthiness. The effect of the ECOA is that if a franchise applicant is creditworthy and the applicant's spouse is not an officer or director of the company, the non-franchisee spouse cannot be forced to sign any sort of guaranty.[83]

Moreover, a franchisor cannot request information about the prospective franchisee's spouse, unless (1) the spouse is also applying for the franchise, (2) the spouse will be actively involved in the franchise, (3) the prospect is relying on the spouse's separate property or on alimony or child support income from a former spouse, (4) the prospect resides in a community property state,[84] or (5) the prospect is relying on the spouse's jointly held property. Importantly, while franchisors may not ask about a prospective franchisee's marital status if the prospect is applying for a separate, unsecured account, franchisors may ask prospects to provide this information if they live in a community property state.[85] Franchisors in any state may request this information if the prospect applies for a franchise that will be operated jointly or secured by jointly held property (e.g., the family home).[86] Franchise cases addressing the ECOA state unequivocally that whether the franchisor's credit inquiry or guaranty requirements are permissible depend

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81. 15 U.S.C. § 1691 (a)(1) (2013).

82. *See* Harford Donuts, Inc. v. Dunkin' Donuts, Inc., 2001 U.S. Dist. LEXIS 25139, *22–23 (D. Md. Apr. 10, 2001). *See also* Citgo Petroleum Corp. v. Bulk Petroleum Corp., 2010 U.S. Dist. LEXIS 106495, *12–18 (N.D. Okla. Oct. 5, 2010); Harara v. ConocoPhillips Co., 377 F. Supp. 2d 779, 786 (N.D. Cal. 2005); McPherson v. Comerica Bank, 1993 U.S. Dist. LEXIS 19405, *16–18 (E.D. Mich. Dec. 8, 1993). Additionally, Beyer and Weber analyze this issue in great detail, noting that a "credit instrument' may include a franchise agreement if the franchisor grants the franchisee credit under it, finances the initial franchise fee, requires installment payments of the initial franchise fee, or leases land or equipment to the franchisee." David A. Beyer & Scott P. Weber, *Perilous Prospects—Part I: Lawsuits to Get Into the Franchise System*, 22 FRANCHISE L.J. 224, 225–26 (2003).

83. 12 C.F.R. § 202.7(d)(1) (2013) ("A creditor shall not require the signature of an applicant's spouse or other person, *other than a joint applicant*, on any credit instrument if the applicant qualifies under the creditor's standards of creditworthiness for the amount and terms of the credit requested.") (emphasis added).

84. David A. Beyer & Scott P. Weber, *Perilous Prospects Part II: Lawsuits to Get Into the Franchise System*, 23 FRANCHISE L.J. 34, 43 (2003) (adapting suggestions from Federal Trade Commission's website, www.ftc.gov/bcp/conline/pubs/credit/ecoa.htm).

85. *Id.*

86. *Id.*

on whether the non-franchisee spouse's "efforts or assets will support the franchise."[87]

ECOA claims have been successful against franchisors when the spouses were not joint applicants and no consideration was given to a state's marital property laws.[88] In these cases, spouses seeking to assert an ECOA claim or defense alleged that they were forced to sign the credit instruments *solely* because of married status, despite no involvement with the other spouse's business.[89] Crucial for any franchisor is to ensure that the decision to seek the guaranty is *not only* because the applicant is married. This concern is mitigated, however, in situations in which the spouse is also a prospective franchisee or interested in investing in the franchisee-spouse's business. Recall that it is also impermissible for a franchisor to deny a prospective franchisee because the non-franchisee spouse refuses to sign a guaranty.[90] Hence, a spousal consent may be a good alternative to protect the interests of the franchisor.

The ECOA does not apply when there is a joint applicant.[91] The term "joint applicant" refers to someone who applies contemporaneously with the applicant for shared or joint credit.[92] This term does not refer to someone whose signature is required by the creditor as a condition for granting the credit requested.[93] In *BayBank v. Bornhofft*, the Massachusetts Supreme Court explained that "joint applicant" refers to an application that is contemporaneously made by two applicants who share a common interest in the credit requested.[94] Therefore, if a franchisee and spouse are to be considered joint applicants, it would be best to have them both execute guaranties contemporaneously. The common interest, however, may hinge on how involved the non-franchisee spouse will be in the business.[95] An argument can be made, however, that the execution of the guaranty is the necessary

87. *See* Beyer & Weber, *Perilous Prospects—Part I*, *supra* note 82, at 225–26 (citing Harford Donuts, Inc. v. Dunkin' Donuts, Inc., Bus. Franchise Guide (CCH) P 12,100, 34,378 (D. Md. 2001)).

88. *See* Chen v. Whitney Nat. Bank, 65 So.3d 1170, 1172 (Fla. Dist. Ct. App. 1st Dist. 2011) ("[Mr.] Lin asserting . . . that his wife, Stefanie Lin, 'was required by the Bank to execute identical guaranty agreements simply because [he and] she [we]re married' "); Nat'l Auto Dealers Exch. v. Sauber, 2011 N.J. Super. Unpub. LEXIS 2472, *3–4, *11–12 (N.J. App. Div. Oct. 3, 2011) ("Cindy was never an officer or shareholder in Vantage and was not otherwise associated with Vantage . . . she asserts she was required to sign the loan because of her marital status").

89. *Id.*

90. *See* 12 C.F.R. § 202.7(d)(1) (2013).

91. *See id.*; *see also* BayBank v. Bornhofft, 694 N.E.2d 854, 858 (Mass. 1998) (finding that ECOA claim had no merit as a matter of law since wife was joint applicant for loan); Midlantic Nat'l Bank v. Hansen, 48 F.3d 693, 699 (3d Cir. 1995) (holding that wife was co-applicant and properly required to co-sign loan documents); Sw. Penn. Reg'l Council Inc. v. Gentile, 776 A.2d 276, 282–83 (Pa. Super. Ct. 2001) (vacating the trial court's judgment that the creditor violated the ECOA and finding that the wife was a joint applicant).

92. *Hansen*, 48 F.3d at 699 (citing 12 C.F.R. § 202.7(d)(1) (Official Staff Interpretation)).

93. *See* 12 C.F.R. § 202.7(d)(1).

94. *Bornhofft*, 694 N.E.2d at 858.

95. *Id.*

level of involvement to show a common interest between the spouses and the franchise.

Franchisors must have a distinct, nondiscriminatory basis for having non-franchisee spouses sign a guaranty because the ECOA's regulation is "not meant to prohibit spouses from signing as guarantors generally, but is instead meant to prohibit a spouse from being *required* to sign *because* he or she is a spouse."[96] Further, in making its determination of creditworthiness, a creditor is permitted to apply its own criteria as long as they are "valid and reasonable" and the creditor is not discriminating with regard to the applicant's marital status.[97]

The ECOA specifically addresses this situation and a creditor's right to rely upon certain nondiscriminatory factors when deciding whether to provide credit. The statute specifies that "consideration or application of State property laws directly or indirectly affecting creditworthiness shall not constitute discrimination for purposes of this subchapter."[98] A franchisor's consideration of a state's property laws as they may affect a potential franchisee's ability to pay in the event of a default cannot therefore constitute discrimination pursuant to the ECOA.[99] Further, considerations that may contribute to the appropriateness of requesting the non-franchisee spouse to sign a guaranty may focus on that spouse's level of involvement with the franchise, both monetarily and operationally.[100] Thus, in community property states, a franchisor, who may become a creditor one day, stands to benefit from requesting that the non-franchisee spouse sign or co-sign the guaranty and may do so without violating the ECOA's prohibitions on discrimination due to marital property laws in those states.

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96. *Sauber*, 2011 N.J. Super. Unpub. LEXIS 2472, *9–10 (emphasis added).

97. Resolution Trust Corp. v. Townsend Assocs. Ltd. P'ship, 840 F. Supp. 1127, 1141–43 (E.D. Mich. 1993) (citing Anderson v. United Fin. Co., 666 F.2d 1274 (9th Cir. 1982)). *See also* Haynes v. Bank of Wedowee, 634 F.2d 266, 270 (5th Cir. 1981) (finding that a married couple's ECOA defense failed as a matter of law because the spouse required to co-sign the guaranty at issue did not provide any evidence "to show that th[e] determination was purely a pretext to discriminate based upon marital status.").

98. 15 U.S.C. § 1691d(b)(2013). *See* United States v. ITT Consumer Fin. Corp., 816 F.2d 487, 489–91 (9th Cir. 1987) (finding a lender's policy of requiring the spouses of married applicants in community property states to cosign promissory notes is not discriminatory under the ECOA pursuant to 15 U.S.C. § 202.7d(b) because of the potential that the applicants' future earnings would not be available to repay the loans under state law).

99. *See ITT Consumer Fin. Corp.*, 8.16 F.2d at 491.

100. Beyer & Weber, *Perilous Prospects—Part I*, *supra* note 82, at 226. Beyer and Weber identify important questions that are relevant to both franchisor and franchisee, including:

> Will the spouse have an active interest in the franchise operation? Will the applicant fail to qualify without consideration of his or her spouse's income, assets, and qualifications? Are the assets being used as collateral, or as part of the credit evaluation, held jointly? Is it reasonable to conclude that the spouse's signature is necessary to reach the assets used as collateral and to determine creditworthiness?

Id.

V. Conclusion

Alternatives to traditional guaranties should be explored to ensure continuity of the franchise relationship beyond the marital relationship. If a non-franchisee spouse signs a guaranty, the franchisor is unquestionably allowed to pursue that spouse's assets, such as bank accounts, investments, personal property, and real estate, whether those assets are held jointly in marriage or separately after the marital relationship ends. Potential franchisees or their spouses, therefore, may refuse to provide a spousal guaranty. Moreover, as discussed in Part IV, it may be more difficult in some states for a franchisor to request, much less obtain, the spousal guaranty.

While there are elements to each type of document that can benefit all parties involved, there is an inherent tension between the effect and goals of spousal guaranties and consent agreements and the franchisor, franchisee, and spouse. Each of these parties may ideally be working towards a common goal of a successful franchise, yet each has distinct interests to protect. Together, a guaranty and a consent bridge the gaps in the relationship among them.

Accordingly, a spousal consent should be considered in the alternative or even in addition to a spousal guaranty. If the spouse signs a consent, the parties may agree that the non-franchisee spouse may be bound by some, if not all, of the terms of franchise agreement. For example, the spouse of a franchisee could sign a consent to the non-compete provisions of the franchise agreement in lieu of the traditional guaranty, if that is the object of concern for the franchisor. Although this spousal consent does not give the franchisor access to a larger pool of assets in the event of default, it does and can protect the franchisor's other proprietary interests.

A dual objective is met by the execution of a spousal consent executed. First, it allows the franchisor to clearly delineate what portions of and how the franchise agreement will be enforced against the non-franchisee spouse. It reduces the uncertainty as to whether a court enforces the franchise agreement against the non-franchisee spouse ensures that both franchisee and the non-franchisee spouse are unable to circumvent the franchise agreement. Second, a consent allows the franchisee and his or her spouse the opportunity to designate how the franchise will be treated in the event of a divorce, again removing uncertainty. We have provided some examples of how courts deal with franchises and family businesses in divorce. Through a spousal consent, control over the manner in which a franchise is distributed is in the hands of the franchisee and his or her spouse, not the courts.

The ultimate goal of any guaranty or consent is for the parties involved to have a mechanism to protect the fruits of the franchise agreement—the franchise business—into which they have entered. This objective is best realized by having the non-franchisee spouse at least sign a consent. The goal of such a consent must be for all parties involved to have a clear understanding of the rights, expectations, and limitations of the franchise agreement both during and beyond the existence of the marital relationship.