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STATE OF WASHINGTON

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DIVISION II, COURT OF APPEALS
OF THE STATE OF WASHINGTON

WASHINGTON STATE DEPARTMENT OF LABOR AND INDUSTRIES,

Plaintiff-Respondent,

v.

LYONS ENTERPRISES, INC., d/b/a JAN-PRO CLEANING SYSTEMS,

Defendant-Appellant.

ON APPEAL FROM PIERCE COUNTY SUPERIOR COURT
(Hon. Linda CJ Lee)

REPLY BRIEF

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I. INTRODUCTION

The Department's repeated pejorative characterization of Lyons' franchisees as "janitors" is exemplary of its mistaken focus on the nature of the work rather than the "essence" of the independent contract. But no matter how many times the Department says it, the franchisees are not "janitors"—they are independent business owners. This Court should reject the Department's view that the essence of an independent contract is "personal labor" simply because it involves someone's "physical labor." Here, the essence of the contract is a lawful and licensed franchise, in which Lyons provides franchise owners the intellectual property rights, initial training and ongoing services they need to successfully operate their own businesses, and for which the franchise owners pay royalties and fees to Lyons in return. Moreover, as the Supreme Court held in *White*, the fact that the franchise owners can and do hire employees of their own confirms that the essence of the franchise is not personal labor.

The Department's unprecedented application of RCW 51.08.180 to legitimate franchises would have a devastating economic impact on Lyons and franchise businesses throughout the State. While equitable estoppel can (and, if necessary, should) be used to minimize the harm to Lyons, it is unlikely that similar relief will be available to hundreds of other service-based franchisors—who, like Lyons, structured their businesses on the

assumption that independent franchise owners are not covered workers. The Department does not deny the consequences of its new policy, yet it is unwilling to subject that policy to legislative scrutiny, formal rulemaking or stakeholder input. This Court should reject the Department's effort to fundamentally transform the Industrial Insurance Act by interpretive fiat.

II. ARGUMENT

A. The Essence Of The Franchise Agreements Is A Franchise Relationship, Not The Franchise Owner's Personal Labor.

The Department concedes that Lyons' franchisees are independent contractors and, thus, the threshold question is whether the "essence" of the franchise agreements is "personal labor." There can be only one essence to a thing; if the essence of the franchise agreement is anything other than personal labor, then RCW 51.08.180 does not apply and the analysis ends. Both parties agree this Court must examine the "realities of the situation" to answer that question. In the Department's view of reality, which it seeks to test here for the first time, ***every*** franchisee in ***every*** service business is a "worker" under the Act because the franchise agreement, by definition, will always require someone's labor. Not only that, no service-related franchisee can ever qualify for exemption under RCW 51.08.195 because, again by definition, the franchisor must exert

some "control" over the franchisee in order to comply with the Franchise Investment Protection Act ("FIPA") and intellectual property law.[1]

This Court must reject that view. The essence of an independent contract is not personal labor where, as here, the contract creates a true franchise relationship between two independent business owners, both of whom owe significant obligations to the other wholly separate from the franchisees' labor. The Department's argument that the Court must look only to the "essence" of the "work," Resp. Br. at 19, 27-31, ignores both the language of the statute and nature of the franchise agreement itself—which describes the "work" both parties must undertake to maintain a traditional franchise in greater detail than the "work" franchisees must do to service their accounts. CP 317-65 (Ex. 1). If the Jan-Pro franchise involved goods, rather than services, the terms of the franchise agreement and the obligations of the parties would be largely identical. In both cases,

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[1] It is therefore the Department, not Lyons, that asks the Court to adopt a bright-line rule with respect to service-related franchisees. Lyons does not claim the Act requires exemption for all franchisees based solely on their "legal denomination" or how the parties "characterize their relationship." Resp. Br. at 1, 19, 27-31. Just as an employer cannot exempt itself from the Act by contract, RCW 51.04.060, merely calling an independent contractor a franchisee will not by itself preclude coverage. The Department and the courts must always look at the "realities of the situation" to decide whether the "essence" is a true franchise relationship or merely an improper effort to disguise a contract for "personal labor."

the "essence" of the agreement is the same too: the creation of a franchise relationship between two businesses, not personal labor.[2]

The Department further ignores the "realities" when it suggests that Lyons' franchisees are "indistinguishable" from employees. Resp. Br. at 27. There is a good reason the Department has never claimed that the franchisees are employees: it is not remotely true. The franchisees make a substantial financial investment in their businesses, have their own business licenses, procure their own insurance, hire and train their own employees, and pay their own taxes; they cannot be fired at-will; they can transfer or sell their franchise business; they pay Lyons to use the Jan-Pro brand and methods, not the other way around; they can enlist new customers or reject existing ones; they bear the risk of loss if a customer refuses to pay; and, as discussed below, they are free to service their accounts when and how they want, without any supervision or "control" from Lyons. In short, the franchisees look nothing like employees or

[2] The Department does not dispute that its approach would result in the absurd result that service-related franchisors who exercise minimal "control" over the franchisees' "work," like Lyons, would fall within the Act, while goods-related franchisors who exercise maximum "control" over the franchisees' "work," like *McDonalds*, would not.

workers; they act as independent business owners for their own benefit and that of their employees, not for Lyons' benefit.[3]

This view is entirely consistent with the purpose of the Act. While the legislature expanded the Act to include certain independent contractors who exhibit the characteristics of employees, it also narrowed the scope by excluding certain business owners. *See* RCW 51.12.020 (exempting sole proprietors, partners and members of LLCs). Where, as here, the parties enter into a true franchise agreement—one that complies with FIPA, is approved by the Department of Licensing, and bears all the hallmarks of a traditional franchise relationship—the Department should preserve that distinction, and recognize franchisees as independent business owners in their own right. To focus solely on the product they sell, *i.e.*, a service, is to ignore the "essence" of the parties' mutual relationship. For this reason alone, the franchisees are not "workers" under RCW 51.08.180.

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[3] The "realities" here readily distinguish *Dana's Housekeeping, Inc. v. Dep't of Labor & Indus.*, 76 Wn. App. 600, 886 P.2d 1147 (1995), upon which the Department relies. Resp. Br. at 28-29. *Dana's* did not involve a franchise, nor did the housekeepers act as independent business owners; the employer told them where and when to do the work, told them what work to do when they got there, insisted that they work alone, and paid them a fee for doing the work even if the customer did not pay. Although the court did not decide the issue, it is clear that the court viewed the housekeepers as *de facto* employees, whose work benefited only the employer's business, not their own. *Id.* at 607-09 & n.2.

B. Lyons' Franchisees Can And Do Hire Others To Perform The Work; *White*'s Third Prong Applies.

In the alternative, this Court may reverse based on the holding in *White v. Dep't of Labor & Indus.*, 48 Wn.2d 470, 294 P.2d 650 (1956). There is no merit to the Department's claim that the Court can ignore *White* given the "realities of the situation." *See* Resp. Br. at 14 n. 4, 24-26, 36 n. 6. Even if this Court believes that the "realities of the situation" suggest that the "essence" of the franchise agreements is personal labor, it must still exempt those franchisees who satisfy one of *White*'s prongs as a matter of law. No case or Board decision has ever refused to exempt an independent contractor under RCW 51.08.180 where at least one of *White*'s three prongs is present. This Court should not be the first. At bottom, the issue is not whether *White*'s third prong applies here, but whether it applies to exempt all or only some of Lyons' franchisees.

1. RCW 51.08.180's "Essence" Test Applies Only Where Labor Is "Personal" To The Independent Contractor; *White*'s Third Prong Applies To All The Franchisees Because The Parties Contemplated The Franchisees Would Delegate The Work To Others.

The Department does not dispute that the franchise agreements allow franchisees to use workers of their own, Lyons did not discourage them from doing so, and Lyons estimated that approximately 80% of the franchisees did, in fact, use others to do the work. CP 328 (Ex. 1); CP 2147 (9/26/11 Tr. at 89). That is enough to exempt all the franchisees

under *White*'s third prong. The essence of an independent contract is not personal labor where the parties contemplate that the work may be done by others—even if not all of it is. *Mass. Mut. Life Ins. Co. v. Dep't of Labor & Indus.*, 51 Wn. App. 159, 165, 752 P.2d 381 (1988); *In re Rainbow Int'l*, BIIA No. 882,664, 1990 WL 304362, *2, 6 (1990) (even though only 50% of the workers had helpers, *White* applied because they all had "authority to hire helpers to assist them in their duties" and the employer "was aware of the practice and did nothing to discourage it").

This is so because "personal labor means labor personal to the independent contractor." *Silliman v. Argus Servs., Inc.*, 105 Wn. App. 232, 238, 19 P.3d 482 (2001); *also Haller v. Dep't of Labor & Indus.*, 13 Wn.2d 164, 168, 124 P.2d 559 (1942) (statute applies where a contractor's "*own personal labor*, that is to say, the work which *he* is to do *personally*, is the essence of the *contract*") (emphasis in original). Where, as here, the parties contemplate that a contractor will delegate the work, RCW 51.08.180 does not apply because the parties "contemplated a specific type of labor, not a specific laborer." *Silliman*, 105 Wn. App. at 238. Contrary to the Department's argument, Resp. Br. at 32, *White* did not disavow this approach, it adopted it. In reigning in the broad language in *Cook* and *Crall*, the Court clarified that the issue for the third prong (as opposed to

the second prong) is not whether the work *could* be done by others, but whether the parties contemplated that it *would* be done by others.[4]

The Department's citation to *Jamison v. Dep't of Labor & Indus.*, 65 Wn. App. 125, 827 P.2d 1085 (1992), and *Dep't of Labor & Indus. v. Tacoma Yellow Cab Co.*, 31 Wn. App. 117, 639 P.2d 843 (1982), proves the point. Resp. Br. at 24-27. In *Jamison*, the parties' contract forbid the contractor from hiring others to do the work. 65 Wn. App. at 132. Thus, although there was "some evidence" that one or two contractors may have had part-time help, the parties never contemplated such a delegation. *Id.* at 132-33. In *Tacoma Yellow Cab*, although the contract did not forbid the contractors from hiring employees, none ever did and, indeed, the "day-to-day" nature of the contract made it unlikely they ever would. Thus, like *Jamison*, there was no evidence the parties contemplated others doing the work. 31 Wn. App. 123-25. Here, by contrast, not only did the franchise agreement expressly permit delegation, the parties contemplated the franchisees would delegate the work, and a majority actually did so.

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[4] Far from overruling the *Cook* [*v. Dep't of Labor & Indus.*, 46 Wn.2d 475, 282 P.2d 265 (1955)] and *Crall* [*v. Dep't of Labor & Indus.*, 45 Wn.2d 497, 275 P.2d 903 (1954)], the Court expressly held that both cases were correctly decided. *White*, 48 Wn.2d at 476. Indeed, as this Court correctly noted, "the *White* court cited *Crall* as standing for the proposition that the Act does not cover an independent contractor when the contracting parties contemplate that the labor will be done by others, in whole or in part." *Mass. Mut.*, 51 Wn. App. at 165.

Finally, this Court can reject the Department's claim that *White* can be overcome if the employer exercises "control" over the independent contractor. Resp. Br. at 25-26. What *White* and later Board decisions say is that even if *White* applies, the worker may still be a covered worker if he is actually an employee, and not an independent contractor at all. *White*, 48 Wn.2d at 477; *In re Rainbow Int'l*, BIIA No. 882,664, 1990 WL 304362, *1-2 (1990); *In re Traditions Unlimited, Inc.*, BIIA No. 870,600, 1989 WL 164536, *8 n.1 (1989). In that case, the "essence" test is irrelevant, and the Board must apply a totally different analysis. *Daniels v. Seattle Seahawks*, 92 Wn. App. 576, 584-85 & n. 4, 968 P.2d 883 (1998). As Lyons noted, this end-run around *White* doesn't help the Department here; the Department affirmatively disavowed reliance on an employer-employee theory at the administrative level, CP 146, and it did not argue the point in the superior court or on appeal.

2. If *White*'s Third Prong Applies Only Where An Independent Contractor Actually Hires Others To Do The Work, A Remand Is Necessary For Determination Of Which Franchisees Had Workers Of Their Own.

The Board construed *White* too narrowly. It concluded that the contractual permission and actual contemplation was not enough; only those franchisees who actually hired others were deemed exempt. CP 26. As explained above, that conclusion was erroneous. This false distinction

leads to the absurd result that one franchisee is exempt, while another is not, even though the franchise agreements and parties' expectations—*i.e.*, the "essence" of the independent contract—is the same in both cases. If that were not bad enough, the trial court went even further, and refused to apply *White* at all. CP 2396. While this Court should hold that *White*'s third prong applies to all the franchisees, at the very minimum, it must reverse the trial court's total abrogation of *White* and exempt at least those franchisees who actually did hire workers of their own.[5]

In that event, reversal should result in a remand to the Department for an accurate determination of the issue, not reinstatement of the Board's Final Order. As Lyons explained, there was no evidence to substantiate the completeness or accuracy of the Department's audit, adopted by the Board, which identified only 18 franchisees as having workers; the only

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[5] As noted, there is no authority to support the Department's argument that courts can ignore *White* based on the purported "realities of the situation," "control" or any other factor. Indeed, in every single case where it was shown that the independent contractor used others to do some or all the work, the Board applied *White*'s third prong to exempt the contractor under RCW 51.08.180. *See In re Mica Peak Constr. LLC*, Dkt. 11-21880, WL 1558388 (Jan. 15, 2013); *In re Alliance Flooring Serv., Inc.*, Dkt. 03-32294, 2005 WL 2386288 (June 13, 2005); *In re Heartland Indus. Inc.*, Dkt. 04-13149, 2005 WL 1075898 (Jan. 10, 2005); *In re Millennium Exteriors, LLC*, Dkt. 02-11265, 2003 WL 22696992 (Sept. 9, 2003); *In re John B. Strand*, Dkt. 93-2772, 1994 WL 396526 (June 27, 1994); *In re Rainbow Int'l*, BIIA No. 882,664, 1990 WL 304362 (1990); *In re Shanley & Wife*, BIIA No. 870,485, 1988 WL 169377 (1988); *In re Charles G. French*, Dkt. 58223, 1982 WL 20480 (May 26, 1982).

evidence presented on the issue proved that the number was far greater. The Department's suggestion that Lyons waived its right to argue this issue is silly: Lyons identified the challenged findings in its assignments of error, and specifically argued the point on the merits in its brief with citation to the record. Lyons' Br. at 3, 35-36 ("no evidence support the Board's conclusion that the Audit accurately identified all the franchisees who employed others"). Nothing more was required. RAP 10.3(a)(6), (g).

The absence of specific evidence is not surprising. Neither party litigated the question of whether particular franchisees were exempt at the hearing. Indeed, the IAJ refused to allow more of Lyons' franchisees to testify because he considered Mr. Lyons "fully competent" to testify about "all of the franchisees." CP 2053-55 (9/7/11 at 163-65). The Department did not object to representative evidence then, nor can it complain about it now. In *In re Millennium Exteriors, LLC*, Dkt. 02-11265, 2003 WL 22696992 (2003), like here, the issue was whether a company's contractors satisfied *White*'s third prong. None of the contractors testified, but the company's manager testified that "all of the subcontractors employed others to do all or part of the work." Because the Department "offered no evidence" to rebut the testimony, the Board found the facts "sufficient to support a finding under RCW 51.08.180(1) and the *White* case, that all of the subcontractors are excluded as workers." *Id.* at *3.

That is true here too; the Department offered no evidence to rebut Mr. Lyons' testimony that "about 80 percent" of Lyons' franchisees had employees or workers. CP 2147 (9/26/11 Tr. at 89). That undisputed testimony should be sufficient to exempt all of Lyons' franchisees under *White* but, at the very minimum, it is sufficient to show that the audit's findings were incorrect. Either way, there should be no pretense that this issue was adjudicated by the Board. Where the administrative record is insufficient to determine whether an independent contractor is a covered worker under RCW 51.08.180, remand is the proper remedy. *Malang v. Dep't of Labor & Indus.*, 139 Wn. App. 677, 691-92, 162 P.3d 450 (2007); RCW 34.05.574(1). If *White*'s third prong applies only to franchisees who had workers of their own, then this Court must reverse the trial court, and remand to the Board for further proceedings on that issue.

C. The Franchisees Are Exempt Under RCW 51.08.195.

Regardless of whether the "essence" of the franchise agreements is personal labor, RCW 51.08.195 provides an alternative ground for exemption. Rejecting the IAJ's extensive findings to the contrary, the Board concluded that Lyons' franchisees did not satisfy two parts of the statute's six-part test: the franchisees were not "free from control or direction," and were not "customarily engaged in an independently established trade, occupation, profession, or business." RCW

51.08.195(1) & (3). As Lyons explained, the Board's conclusion was erroneous as a matter of law and must be reversed. *See* Lyons' Br. at 38-42.[6] None of the Department's contrary arguments have merit.

Control or Direction. The Department simply ignores (but does not dispute) the relevant test for purposes of "control or direction." To fail subsection (1), Lyons must have "the right to control the ***methods and details***" of the franchisees' work. *Western Ports Transp., Inc. v. Employ. Sec. Dep't*, 110 Wn. App. 440, 452, 41 P.3d 510 (2002). The Department cannot point to any facts showing contractual or actual control over "methods and details." It is undisputed that Lyons did not tell the franchisees who could do the work; Lyons did not tell the franchisees when to do the work; Lyons did not provide the franchisees with tools or supplies for the work; and Lyons never supervised the work itself. Indeed, the Department does not and cannot explain how Lyons controlled the

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[6] The Department implies that the Board's conclusion that Lyons' franchisees did not qualify for exemption under RCW 51.08.195 is a factual finding reviewed for "substantial evidence." Resp. Br. at 38. Wrong. "When an administrative decision involves a mixed question of law and fact, the court does not try the facts de novo but it determines the law independently of the agency's decision and applies it to facts as found by the agency." *Xenith Group, Inc. v. Dep't of Labor & Indus.*, 167 Wn. App. 389, 394, 269 P.3d 414 (2012); (quotation marks omitted). Here, the underlying facts are undisputed; it is the Board's application of those facts to, and interpretation of, RCW 51.08.195(1) and (3) that matters. Those are questions of law that this Court reviews *de novo*. *Id.*

"methods and details" of the franchisees' commercial cleaning operations when no one from Lyons was ever present when the work was done.

The best the Department can do is cite the "extensive, five-week training" and manuals Lyons gives new owners. Resp. Br. at 38-39. But this supposed "extensive" training is not extensive at all: it amounts to a total of 30 hours scattered over several weekends and evenings and, of the five subjects covered, only two deal with cleaning. CP 327 (Ex. 1, § 8.1); CP 2152-53 (9/26/11 Tr. at 94-95). Similarly, only one of three manuals Lyons distributes relates to cleaning, and it does not cover "methods and details" of the work, but rather explains the proprietary techniques the franchisees license and are expected to use. CP 1937-40 (9/7/11 Tr. at 47-50); 2204-05 (9/26/11 Tr. at 146-47).[7] In a different setting, Washington courts have recognized that a franchisor's "procedures and standards" for uniform operation and management of the franchise do not constitute day-to-day "control" over the franchisee's business. *Folsom v. Burger King*, 135 Wn.2d 658, 671-73, 958 P.2d 301 (1998). The same is true here.

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[7] That Lyons does not "control or direct" the franchisees' work through this modest initial training requirement is all the more obvious since Lyons has no role in training the franchisees' workers who, in many cases, actually do the work. As an independent business owner, it is the franchisees who have responsibility for both hiring and training their own employees. CP 2153-54 (9/26/11 Tr. at 95-96).

Lyons' periodic customer audits do not constitute control over "methods and details" either. *See* Resp. Br. at 39. It is a function Lyons can and must perform to ensure compliance with the franchise agreement. CP 1909-10, 1917 (9/7/11 Tr. at 19-20, 27); CP 2173-74 (9/26/11 Tr. at 115-116). Here too, analogous case law is instructive. In the setting of an owner's duty to ensure workplace safety—where, like here, the key issue is "control over the manner in which an independent contractor completes its work"—Washington courts hold that "authority to merely inspect the work and demand contract compliance" is not control. *Kamla v. Space Needle Corp.*, 147 Wn.2d 114, 120-21, 52 P.3d 472 (2002). Again, the same is true here. The Department cannot cite a single case or Board decision holding that initial training or *post hoc* inspections are tantamount to supervision over the "methods and details" of the work. They are not.

Independently Established Business. The Department ignores the undisputed fact that Lyons' franchisees were validly licensed businesses, responsible for their own books, taxes, insurance, employees, equipment, scheduling and more. Lyons' Br. at 41. Instead, the Department argues that the franchisees were not "independent" because they agreed not to offer competing services during the term of the franchise and one year

thereafter. Resp. Br. at 40.[8] This kind of clause is standard in franchise agreements and, while it may restrict a franchisee's ability to compete, it does not render the independence of its business any less legitimate. An agreement not to compete is part of consideration a franchisee pays for the right to use Jan-Pro's brand, goodwill and proprietary techniques, and it provides Lyons with a means to protect its interest in those valuable rights. CP 1920 (9/7/11 Tr. at 30); CP 2201-02 (9/26/11 Tr. at 143-44).[9]

Washington courts recognize the value of reasonable non-compete clauses in franchise agreements, which they will enforce during and after termination of the franchise. *Armstrong v. Taco Time Int'l, Inc.*, 30 Wn. App. 538, 635 P.2d 1114 (1981); Annot., *Validity and Construction of Restrictive Covenant Not to Compete Ancillary to Franchise Agreement*, 50 A.L.R.3d 746 (1973). This includes the franchisor's ability to protect its intellectual property, but also "its ability to sell new franchise rights, and the protection of existing franchisees from competition by a fellow

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[8] The Department repeats the Board's apparent conclusion that the term "customarily engaged" means that that independent contractor must "have at least some history" in a particular business before entering into the contract at issue. Resp. Br. at 41-42. As Lyons pointed out, *see* Lyons' Br. at 42, no authority or public policy supports that view.

[9] The non-compete clause does not forbid former franchisees from doing business for one year after termination; it prevents them from soliciting existing customer accounts and owning, operating or working in a cleaning business only within Lyons' territory. CP 344-47 (Ex. 1, § 18).

franchisee." *Armstrong*, 30 Wn. App. at 546. Here too, the Department's position would force franchisors to make a Hobson's Choice of either sacrificing a valuable and traditional franchise right or risk disqualifying their franchisees from exemption under RCW 51.08.195(3). As a matter of both policy and precedent, the Department's position is untenable.

D. Lyons Justifiably Relied On The Department's 2005 Audit; All The Elements of Equitable Estoppel Are Satisfied.

The trial court properly found that Lyons had proven that the Department's 2005 audit was inconsistent with its 2010 audit, and that Lyons relied on the earlier audit in contracting with additional franchisees, expanding its territory, and otherwise investing in its business. CP 2399. The court denied Lyons equitable relief, however, concluding that Lyons suffered no "injury." *Id.* As Lyons explained, that conclusion was wrong because, if the Final Order is affirmed, Lyons' obligation to pay IIA premiums for franchisees going forward will result in a substantial and unexpected economic loss to Lyons; only after the 10-year term for any particular franchise agreement expires can Lyons adjust the agreement to take into account the economic reality of the Department's new policy; even then, Lyons cannot pass its tax burden on to the franchisees. *See* Lyons' Br. at 44-46; RCW 51.16.140(2). The Department agrees; it does not defend the trial court's conclusion on the issue of "injury."

Rather, the Department attacks the trial court's finding on reliance, arguing that Lyons did not "justifiably" rely on the 2005 audit. The Department first argues that Lyons was wrong to rely on the audit because it did not mention that Lyons was a franchisor. Resp. Br. at 43. The Department is wrong; the audit does note that Lyons "acts as a franchisor for Jan Pro Cleaning Systems[.]" CP 878. But more to the point, the fact that the 2005 audit did not emphasize Lyons' legal status as a franchisor weighs in favor of justifiable reliance—not against it—because it shows that the Department properly focused on the nature of Lyons' relationship with the franchisees—not on mere labels.[10] The nature of those relationships did not change between the 2005 and 2010 audits.

The Department next argues that the 2005 audit put Lyons on "notice" that the "essence" of Lyons' franchise agreements was personal labor under RCW 51.08.180 because, otherwise, the audit would not have cited RCW 51.08.195. Resp. Br. at 43-44. Wrong again; the audit found that Lyons' franchisees were exempt under ***both*** RCW 51.08.180 and RCW 51.08.195. CP 876 ("Of these subcontractors, only two did not meet the criteria for independent contractor under RCW 51-[08]-180 and 51-[08]-195."). Here too, regardless of whether the 2005 audit was based on

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[10] It is undisputed that the Department examined Lyons' franchise agreements as part of the 2005 audit. CP 2137 (9/26/11 Tr. at 79).

RCW 51.08.180 or RCW 51.08.195, Lyons reasonably believed the Department would not consider its franchisees covered workers so long as Lyons did not alter the nature of its franchise model, which it never did.

Along the same lines, the Department argues that because two franchisees were found to be covered workers in the 2005 audit, Lyons should have known that the Department might disqualify more franchisees in the future. Resp. Br. at 44-46. But the Department only disqualified the two franchisees because they did not have valid UBI numbers. CP 876. Thus, to the extent the 2005 audit relied on RCW 51.08.195 at all, the Department necessarily found that Lyons' franchisees ***satisfied*** all of RCW 51.08.195's other criteria—including RCW 51.08.195(1) and (3). To be sure, nothing in the 2005 audit suggests that, five years later, the Department and Board would take the position that none of the franchisees were "free from control or direction" or "engaged in an independently established trade, occupation, profession, or business" after all.[11] Indeed, the most Lyons could have known from the 2005 audit is that it needed to

[11] The Department briefly suggests that Lyons could not reasonably rely on the 2005 audit because the size of the franchise agreements grew over the years. Resp. Br. at 46. This is a red-herring. The Department cannot point to any evidence showing that Lyons' relationship with its independent franchisees changed following the 2005 audit in any way that would affect the analysis under either RCW 51.08.180 or RCW 51.08.195.

ensure that its franchisees obtained and maintained valid UBI numbers, which Lyons did. CP 2165-66 (9/26/11 Tr. at 107-108).

Finally, the Department does not dispute that, if Lyons' reliance was justified, estoppel is required to prevent a manifest injustice. Lyons' Br. at 45-46. Nor does the Department articulate how an equitable remedy would impair the government's functions. It wouldn't. Nothing in the legislative record indicates the legislature intended or expected the Act to apply to franchises—and, as Lyons' own case shows, prior to 2010, the Department did not believe the Act applied to franchises either. Thus, even if the Department's novel interpretation is accepted going forward, it can't be said that estoppel would fundamentally damage the purpose or policy of the Act; it would simply require the Department to adhere to its own long-standing interpretation of the Act in the context of franchises for one franchisor (Lyons) for a limited time (until the expiration of Lyons' pre-2010 franchise agreements) to remedy an injustice for which the Department is responsible (Lyons' justifiable reliance on the 2005 audit).

E. Lyons Is Entitled To Fees Under the EAJA; The Department's Position Is Not Substantially Justified.

It is no coincidence that franchises have existed in Washington for decades, and yet there is no statute, no legislative history, no agency rule, no case law, no administrative decision, and no interpretative guideline to

suggest that independent franchise owners are "workers" under the Act. They are not. At least until now, the Department itself recognized that. The 2005 audit of Lyons was not an aberration; it was a correct interpretation of the law. In the end, then, this Court should view this case for what it is: an effort by the Department to expand the scope of the Act to franchisees by *fait accompli*, rather than by legislation or notice-and-comment rulemaking. Its actions throughout this litigation were not only erroneous, there were not substantially justified. RCW 4.84.350(1). The EAJA ensures that Lyons is not forced to bear the expense of successfully litigating, whether legally or equitably, the Department's "test case."[12]

The Department's suggestion that Lyons waived its right to fees under the EAJA is baseless. As the Department notes, Lyons did not move for an award of fees under the EAJA in the superior court. Resp. Br. at 48. The reason is simple: Lyons did not prevail in the superior court and, thus, could not bring such a motion. RCW 4.84.350(1) (fees may be awarded only if party "prevails" in judicial review); CR 54(d)(2) (motion for fees due no later than 10 days ***after*** entry of judgment). Here, by

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[12] This is true even if this Court does not reverse the trial court's order in its entirety. A party is considered to prevail under the EAJA if the party "obtained relief on a significant issue that achieves some benefit that the qualified party sought." RCW 4.84.350(1). Thus, for example, reversal of that portion of the trial court's order refusing to apply *White*'s third prong to those franchisees who hired workers of their own would entitle Lyons to an award under the EAJA.

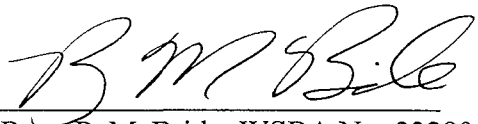
contrast, Lyons was required to move for fees, and did so, in its opening brief. RAP 18.1(b). If Lyons prevails on appeal, this Court can and should award Lyons EAJA fees at both the superior court and appellate court levels. *Nor-Pac Enter., Inc. v. Dep't of Licensing*, 129 Wn. App. 556, 571-72, 119 P.3d 889 (2005) ("We also remand for the superior court to determine the amount of attorney fees and costs to which Nor–Pac is entitled to [under the EAJA] for the proceedings below and on appeal.").

III. CONCLUSION

This Court should conclude that Lyons' franchisees are not "workers" under RCW 51.08.180 and/or that they are exempt under RCW 51.08.195. In the alternative, the Department should be equitably estopped from disavowing the position it took in the 2005 audit.

RESPECTFULLY SUBMITTED this 18th day of March, 2014.

LANE POWELL PC

By 

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CERTIFICATE OF SERVICE

I, Kathryn Savaria, hereby certify under penalty of perjury of the laws of the State of Washington that on March 18, 2014, I caused to be served a copy of the attached document to the following person(s) in the manner indicated below at the following address(es):

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Kathryn Savaria

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