



FEDERAL ELECTION COMMISSION
Washington, DC 20463

April 10, 1992

CERTIFIED MAIL
RETURN RECEIPT REQUESTED

ADVISORY OPINION 1992-7

James H. Ingraham
Secretary and Associate Corporate Counsel
H & R Block, Inc.
4410 Main Street
Kansas City, MO 64111

Dear Mr. Ingraham:

This responds to your letter dated February 10, 1992, requesting an advisory opinion on behalf of H & R Block, Inc. ("Block" or "the company"), a Missouri corporation, and its separate segregated fund, H & R Block Political Action Committee ("BLOCKPAC") concerning the application of the Federal Election Campaign Act of 1971, as amended ("the Act"), and Commission regulations to the solicitation of contributions to BLOCKPAC.

In the past, BLOCKPAC has solicited and accepted voluntary political contributions from Block's executive and administrative employees. BLOCKPAC now proposes to solicit voluntary contributions from Block's "major franchisees," "satellite franchisees," and their executive and administrative employees. You request an advisory opinion as to whether BLOCKPAC may solicit such franchisees and their executive and administrative employees for contributions.

Since 1955, Block has been operating offices engaged primarily in the preparation of Federal, state, and local income tax returns. Since 1957, Block has granted franchises to others to operate such offices in certain areas of the country. In 1965, Block began to grant franchises only for smaller communities, generally with populations of 15,000 or less and has referred to such franchises as "satellite franchises." Prior to 1965, Block granted franchises, known as "major franchises," for larger areas, such as larger cities, one or more counties, or all or part of a state, and permitted major franchisees to grant subfranchises within their franchise territories.

As of last year, Block and its franchisees operated 8,955 offices throughout the United States, and in Canada, Australia, New Zealand, and Europe. Of these offices, 4,087 were owned and operated by Block and 4,868 were owned and operated by franchisees. Twenty-two major franchisees operated 848 franchised offices and had an additional 599 subfranchised tax offices in their areas. A total of 2,133 satellite franchisees operated 3,421 offices. You do not include the personnel of the 599 subfranchised tax offices in your request.^{1/}

The majority of the revenues generated at company-owned and franchised offices come from the income tax preparation services. In addition, Block and its franchisees have offered electronic filing services, and refund anticipation loan services (assistance in applying for a bank loan secured by an anticipated refund). Block and some of the franchisees also conduct instructional courses in the fall to train preparers. These additional services are known as "related services."

The Commission's response depends upon whether the franchisees are affiliated with Block. A corporation may "solicit the executive or administrative personnel of its subsidiaries, branches, divisions, and affiliates and their families." 11 CFR 114.5(g)(1). The Commission's regulations specify that the factors set forth at 11 CFR 100.5(g)(4) shall be used to determine whether an organization is an affiliate of a corporation. Id.^{2/} Included in these factors are: (1) whether an organization has the authority or ability to direct or participate in the governance of another organization through provisions of constitutions, bylaws, contracts, or other rules, or through practices and procedures; (2) whether an organization has the authority or ability to hire, appoint, demote, or otherwise control the officers, or other decisionmaking employees or members of another organization; and (3) whether an organization had an active or significant role in the formation of another organization. 11 CFR 100.5(g)(4)(ii)(B), (C), and (I). See 11 CFR 110.3(a)(3)(ii).^{3/}

In previous advisory opinions addressing affiliation of franchisees or licensees to the granting corporation, the Commission has found affiliation to exist on the basis of the corporation's control over business policies, practices, and procedures of an entity and the extent of the entity's contractual obligations to the corporation. See Advisory Opinions 1988-46, 1979-38, 1978-61, and 1977-70. See also Advisory Opinion 1985-31. This basis is similar in effect to two of the regulatory factors cited above. By contrast, the Commission, in Advisory Opinion 1985-7, found that the degree of influence held by a corporation, Anheuser-Busch, over its wholesale distributors was insufficient to establish affiliation. The relationship "reflect[ed] more the characteristics of a typical business contract between two independent and separate entities, as distinguished from the relationship where one entity exercises pervasive supervision and direction over the daily operations and business policies of another entity such as a franchisee." Advisory Opinion 1985-7.

The materials submitted by you indicate continuing control and direction by Block in the licensing of and use of service marks by both the major and satellite franchises. Under both franchise agreements, Block grants to the franchisee the exclusive right to use the name and service mark "H & R Block" and any other name or service mark adopted or registered by Block for use in the operation of income tax preparation services and the performance of related services (e.g., "NATION'S LARGEST TAX SERVICE") from a location or locations within a specified franchise territory. The franchisee must operate its business of preparing income tax

returns and related services under Block's licensed marks only. The franchisee may not use Block's licensed marks for any other purpose without Block's written permission.^{4/}

Under both types of agreements, the franchisee covenants not to compete with Block or other franchisees in tax return preparation or related services during the duration of the franchise and for a period following termination or transfer of the agreement. The Major Franchise Agreement covenant is not limited to competition within a specified area, while the Satellite Agreement specifies a mileage radius. Both types of franchises are also subject to prohibitions on divulging trade information or methods.

In addition to the licensing, trade information, and territorial restrictions, your materials indicate Block's continuing control or direction with respect to Block policies, restrictions, and procedures governing daily operations of both major and satellite franchises. These include requirements as to the accurate preparation of returns, hours of operation, maintenance and condition of offices, quality and appearance of supplies and equipment, employment of sufficient well-trained personnel, and procedures pertaining to related services such as electronic filing and refund anticipation loans. You state that the "standards, policies and procedures imposed by Block upon its satellite franchisees are even more stringent than those imposed upon major franchise owners," noting explicit requirements (which appear in the "Franchisee's Conduct of Business" clause) pertaining to payments of tax penalties and maintenance of liability insurance, and other requirements.

Under the Major Franchise Agreement, any material and substantial breach of its terms by the franchisee constitutes grounds for termination of the agreement by Block. The Satellite Agreement may be terminated for a material and substantial breach of the franchise agreement or the electronic filing agreement, or for "other good cause." There are explicit provisions for the implementation of a timely cure and for arbitration. Some breaches, however, are not curable, such as a nonpayment of indisputable royalties continuing for 30 days beyond a notice of nonpayment.

Block provides extensive training, guidance, and oversight for the franchises. Block provides major and satellite franchise owners with extensive instruction and advice concerning the setting up and management of their offices. This includes furnishing guidelines in the selection and location of offices, furnishing information necessary to establish an operating budget, designing forms to be used in tax return preparation, making training materials available for use by the franchisee in training employees, and, if requested, assistance in handling managerial or other problems. Moreover, the satellite agreement provides that Block will train the franchisee and provide certain necessary equipment without charge (other than freight). Both agreements also provide for the sale to the franchisee of certain office supplies, forms, and equipment; if the franchisee does not purchase these items, he or she must purchase items of similar appearance and of the same quality or better.

You state that satellite franchisees are assigned to a specific "satellite director/district manager of Block" located in the general area of the satellite territory. Major franchisees are assigned to a Block regional manager. As soon as possible after a satellite agreement is signed, the satellite director will train the new owner in conducting the business.^{5/} Satellite directors work with old

and new satellite owners, through frequent visits, calls and satellite complex meetings, and regional managers hold a yearly regional convention for satellite owners for time management training. Satellite owners may be visited intermittently by auditors from Block's Internal Audit Department in order to assure compliance with the franchise agreement and Block's policies and procedures.

Major franchisees or their representatives are visited intermittently by Block regional directors or vice presidents. The auditors also visit the franchise offices to assure compliance. The major franchisees or their representatives also attend twice yearly operations meetings at national headquarters or elsewhere.^{6/}

The franchise agreements also impose restrictions upon the transferability of the franchises. Block's prior written approval is necessary for any assignment or transfer of interest in the franchise, including approval rights after a franchisee's death, other than transfers to a "controlled entity" (discussed below). If the proposed transferee is a corporation or partnership, but not a controlled entity, the franchisee will inform Block about each officer and director, and the ownership interest of each shareholder of the transferee. The franchisee will also give Block information as to a director or partner, the "principal," who will personally assume the obligations of the franchise agreement and to whom Block will look, in addition to the proposed transferee, for proper performance. The principal must be approved by Block.

If the transferee is a controlled entity, i.e., a corporation or partnership in which the franchisee or the franchisee's immediate family holds a majority voting or controlling interest, then the franchisee must provide Block with notice of the transfer. The franchisee remains personally liable for the obligations of the proposed entity until another principal is appointed and approved by Block or the franchise agreement is transferred or assigned to a transferee approved by Block.

Based on the above information, it appears that Block has a substantial degree of participation and control over the policies, practices, and daily operations of both the major franchises and the satellite franchises. The ability to grant a franchise and the franchise agreements' granting of pre-approval authority for assignment and transfer, and some authority as to termination, also give Block some degree of authority over who the franchise's decisionmakers will be. In addition, Block seems to have control over the formation of the franchises. Although the franchisees may have engaged in tax preparation practice before, the person or entities, in order to function as H & R Block franchises, must be granted the license to operate as such by Block. See Advisory Opinion 1990-22.

The Commission concludes, therefore, that Block or BLOCKPAC may solicit voluntary political contributions from the executive and administrative personnel, and the families thereof, of Block's major and satellite franchisees. See 11 CFR 114.1(c). Block and its SSF may also solicit contributions from the franchisees themselves as long as they are not corporations, e.g., if they are individuals or partnerships. See Advisory Opinions 1988-46 and 1983-48. The designated "principals" of incorporated franchisees would qualify, under the terms of the franchise agreements, as franchisees. This conclusion is limited to the solicitations of executive and administrative employees of the Block franchise itself. Without further information as to the

make-up of incorporated franchisees, this opinion does not reach those who have no executive or administrative employee relationship with a Block franchise.

The Commission notes that Block has franchises in Canada, Australia, New Zealand, and Europe. The Act and Commission regulations prohibit the making of a contribution by a foreign national, or the solicitation or acceptance of a contribution from a foreign national with respect to any election. 2 U.S.C. 441e(a); 11 CFR 110.4(a)((1) and (2).^{7/} Block and BLOCKPAC may, therefore, not solicit or accept contributions from employees who are foreign nationals. The Act and regulations do not, however, prohibit, the solicitation or acceptance of contributions from executive and administrative employees who are not foreign nationals, even if they work for a foreign major or satellite franchisee of Block. See Advisory Opinions 1982-34 and 1979-59.

This response constitutes an advisory opinion concerning application of the Act, or regulations prescribed by the Commission, to the specific transaction or activity set forth in your request. See 2 U.S.C. 437f.

Sincerely,

(signed)

Joan D. Aikens
Chairman for the Federal Election Commission

Enclosures (AOs 1990-22, 1988-46, 1985-31, 1985-7, 1983-48, 1982-34, 1979-59, 1979-38, 1978-61, and 1977-70)

ENDNOTES

1/ The Commission notes that you have submitted, as part of your request, copies of a major franchise agreement and a satellite franchise agreement, but not a subfranchise agreement.

2/ The Act and Commission regulations treat the committees established by the same corporation or group of persons, including any parent, subsidiary, branch, division, department, or local unit thereof as a single committee. 2 U.S.C. S441a(a)(5); 11 CFR 110.3(a)(1)(ii). See 11 CFR 100.5 (g)(2). The regulations clarify the term "local unit," stating that it may include, in appropriate cases, a franchisee or licensee. 11CFR 100.5 (g)(2) and 110.3 (a)(1)(ii).

3/Commission regulations at 11CFR 100.5 (g)(4)(ii) and 110.3 (a)(3)(ii) list ten such factors but indicate that this list is not exhaustive.

4/ There are also significant and restrictive licensing agreements for both types of franchises with respect to the provision of the electronic filing service, which is made available to all franchisees and used by a substantial majority.

5/ Initial training of major franchisees took place many years ago although they have, in recent years, received substantial training in electronic filing and automated tax preparation at corporate headquarters in Kansas City.

6/ According to the franchise agreements, the books and records of major satellite franchisees are open to inspection by Block during regular business hours, and major franchisees must ship such records to Block upon request.

7/ A foreign national is a foreign principal as defined in 22 U.S.C. s611(b), or an individual who is not a U.S. citizen or lawfully admitted for permanent residence, as defined in 8 U.S.C. s1101(a)(20). 2 U.S.C. s441e(b); 11 CFR 110.4 (a)(4).