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| People v Domino's Pizza, Inc. |
| 2021 NY Slip Op 30015(U) |
| January 5, 2021 |
| Supreme Court, New York County |
| Docket Number: 450627/2016 |
| Judge: Joel M. Cohen |
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**SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY**

PRESENT: HON. JOEL M. COHEN **PART IAS MOTION 3EFM**

Justice

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THE PEOPLE OF THE STATE OF NEW YORK, BY LETITIA JAMES, ATTORNEY GENERAL OF THE STATE OF NEW YORK,

INDEX NO. 450627/2016

Petitioner,

- v -

DOMINO'S PIZZA, INC., DOMINO'S PIZZA, LLC,
DOMINO'S PIZZA FRANCHISING, LLC,

DECISION AFTER NON-JURY TRIAL

Respondents.

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In this Special Proceeding, Petitioner (the Attorney General or "OAG") alleges that Respondents (collectively, "Domino's") misled their New York franchisees into believing that they could rely on the Domino's store management software program – "PULSE" – to calculate employee wages in compliance with applicable labor laws. According to OAG, PULSE systematically under-calculated wages for tipped employees (e.g., delivery drivers) and employees who worked long hours on a given day or at multiple stores during a given week, leading several Domino's franchisees to underpay their employees in violation of New York Labor Law. OAG seeks to hold Domino's liable under New York Executive Law § 63[12] for allegedly defrauding franchisees with respect to the capabilities of PULSE and for violating the Franchise Sales Act, General Business Law § 687, which prohibits fraudulent conduct in the sale of a franchise.¹

¹ OAG's principal claims against Domino's in this proceeding were based on the theory that Domino's was a "joint employer" of its franchisees' employees and therefore was liable directly

After a two-week bench trial, the Court concludes that OAG has failed to prove its case against Domino's. The evidence did not establish that Domino's misled franchisees with respect to PULSE's payroll-related features in connection with the sale of franchises or otherwise. The PULSE "payroll report" essentially was a spreadsheet that multiplied hours by wage and overtime rates set by the franchisee, and was described by Domino's (accurately) as generating data that could be provided to an accountant or a payroll consultant to calculate what the franchisee should pay its individual employees. Domino's did not represent, in writing or otherwise, that PULSE would (or could) calculate wages in conformity with the constellation of federal and state labor laws. Notably, the franchisee witnesses called by OAG – that is, purported victims of the fraud – did not support OAG's claims. Moreover, the statistical analysis offered by OAG's expert witness to show that there was a causal link between supposed flaws in PULSE and the payroll errors by franchisees was not persuasive.

Although there is evidence indicating that Domino's could have done more to clarify the proper use of PULSE's "payroll reports" and the need for franchisees to ensure proper calculation of employee wages, the Court does not believe the evidence taken as a whole shows the kind of fraudulent or deceptive behavior that triggers liability under Executive Law § 63[12] or the Franchise Sales Act.

Accordingly, as more fully set forth below, the Attorney General's claims are dismissed.

under the Labor Laws for the underpayment of franchise employees. Those claims were dismissed on summary judgment prior to trial (NYSCEF 409, 480).

PROCEDURAL HISTORY

In 2012, OAG began investigating a number of Domino's franchisees across New York for potential labor law violations. The issues investigated included: (1) failure to pay an extra hour at minimum wage when an employee worked a shift that covered over a ten hour period in a day ("spread of hours"); (2) failure to pay overtime for all hours worked over 40 hours in a week even if the employee worked at different stores owned by the same employer; (3) failure to pay minimum wage, and not a tipped minimum wage rate, when an employee spends less than 80 percent of his shift performing work that could result in tips ("the 80/20 rule"); and (4) failure to pay workers receiving the tipped minimum wage an overtime rate at 1½ times the regular minimum wage minus the tip credit rate, instead of 1½ times the tipped minimum wage ("tipped overtime"). The OAG entered into settlements with fifteen franchisees between 2014 and 2017.

Domino's became a subject of the OAG's investigation in 2013, and the Verified Petition in this case was filed against it and several Domino's franchisees on May 23, 2016. The First, Second, Third, Fourth, Fifth, Sixth and Seventh Causes of actions in the Verified Petition assert Labor Law claims (via Executive Law § 63[12]) against Domino's on the theory that Domino's was a "joint employer" of the individuals who were hired by its franchisees. As noted above, those claims were dismissed prior to trial (NYSCEF 409, 480; *see also In re Domino's Pizza Inc.*, 16-CV-2492(AJN)(KNF), 2018 WL 4757944 [SDNY Sept 30, 2018] [granting summary judgment dismissing similar labor law claims against Domino's on essentially the same facts]).

The Eighth Cause of Action ("PULSE-Related Fraud") alleges that Domino's "repeatedly engaged in fraudulent acts and practices" in connection with its sale and use of a proprietary software product, PULSE, which it licenses to franchisees, in violation of Executive Law § 63[12]. According to the Verified Petition: "Through this deception, Domino's franchisees,

including the Maestri and Ahmed Respondents, relied on the PULSE Payroll Report, resulting in underpayments of employees in New York State throughout the Relevant Period [July 18, 2008 through May 2016].” (NYSCEF 1 at ¶ 246).

Based on similar factual allegations, the Ninth Cause of Action (“PULSE-Related Misrepresentations and Omissions”) alleges that Domino’s violated Franchise Sales Act § 687, which makes it “unlawful for a person, in connection with the offer, sale or purchase of any franchise, to directly or indirectly ... [m]ake any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading.” (*Id.* at ¶ 251 [quoting Gen. Bus. L. § 687(2)(b)]). Specifically, the OAG alleges that Domino’s made material misrepresentations or omitted to disclose material information about PULSE in its Franchise Disclosure Document. (*Id.* at ¶¶ 170-174, 253).

A non-jury trial was held with respect to the Eighth and Ninth Causes of Action from October 13 through October 23, 2020.

EVIDENCE PRESENTED AT TRIAL

1. At trial, OAG presented live testimony² from the following witnesses:
 - Michael Gaisser (Domino’s franchisee) (Tr. 48-172³)
 - Mohammed Shueb Ahmed (Domino’s franchisee) (Tr. 191-247)
 - Anthony Maestri (Domino’s franchisee) (Tr. 248-322)

² To ensure social distancing during the coronavirus pandemic, the trial was conducted remotely via Microsoft Teams. The Court thanks court staff, the court reporters, counsel, clients, and witnesses for their substantial efforts to make this work so well.

³ References to “Tr.” are to settled transcripts prepared by the parties to correct transcription errors and omissions.

- John Cilmi (Domino's franchisee) (Tr. 325-352, 356-391)
 - Khaled Hamdan (Domino's franchisee) (Tr. 392-450)
 - John Dobson (Domino's franchisee) (Tr. 463-501)
 - Emir Lopez (Domino's franchisee) (Tr. 537-599)
 - Jonathan Werberg (expert witness – statistical analysis) (Tr. 601-701, 724-794)
 - Joseph Devereaux (Domino's employee) (Tr. 1245-1259) (rebuttal witness)
2. OAG read into the record excerpts of deposition transcripts of the following former Domino's employees⁴:
- Natasha Gayden (Tr. 856 -859)
 - Kimberly Ridge (Tr. 859-877)
 - Wayne Pederson (Tr. 878-912, 917-943) (Tr. 1261-1264 (rebuttal))
 - Julie Wigley (Tr. 943-863)
3. Domino's presented live testimony from the following witnesses:
- Michael Davis (Domino's employee) (Tr. 1074-1140)
 - Vincent Love (Domino's expert witness – accounting) (Tr. 1141-1173)
4. Domino's read into the record cross-designations from deposition transcripts of the following former Domino's employees:
- Wayne Pederson (Tr. 1181-1197)
 - Julie Wigley (Tr. 1198-1206)
 - Kimberly Ridge (Tr. 1206-1210)

⁴ Domino's objections to the admissibility of this testimony were overruled on the ground that they were admissions of a party. The Court precluded OAG from admitting deposition testimony obtained from non-party witnesses during the course of OAG's investigation.

5. In addition to the testimony, the Court admitted roughly 150 exhibits into evidence (NYSCEF 493).

FINDINGS OF FACT

Based on its review of the evidence presented at trial, including its evaluation of the credibility of the witnesses who testified during the proceedings, the Court makes the following findings of fact:

Overview

1. Boiled down to its essentials, this is not a complicated case.
2. It is undisputed that PULSE did not – and could not – apply the various federal and state labor law requirements with respect to the calculation of wages, including the particular rules with respect to the compensation of “tipped” workers such as the many drivers who deliver Domino’s offerings to customers. Such calculations would require far more detailed input of data from the franchisee, including among other things the combined hours the employee worked at the franchise owner’s multiple locations (if applicable) and the percentage of time a “tipped” delivery driver spent doing “non-tipped” work in and around the store itself. It would also require a far more sophisticated software program to synthesize those and other data and apply the labor laws that govern the particular jurisdiction in which the franchise is located (the laws vary from State to State).
3. It is also undisputed that PULSE was not designed or intended to perform those functions.
4. The central question is whether Domino’s misled its New York franchisees to believe otherwise (which in turn led some of them to underpay their employees). The Court concludes it did not.

Domino's

5. Domino's is one of the largest fast food franchisors in the world. As of January 2016, of its 5,273 stores in the United States, approximately 93% were owned and operated by franchisees and, for the fiscal year ending January 3, 2016, Domino's collected approximately \$272.8 million in revenue from its U.S. franchisees.

6. As of January 3, 2016, Domino's did business throughout New York, through 136 New York based Domino's franchise stores and 54 corporate owned stores.

PULSE

7. PULSE is a proprietary point of sale system that is utilized by all Domino's stores. During the relevant period, all Domino's franchisees were required to acquire, install and use PULSE.

8. PULSE allows a store to take and process orders, monitor sales, manage inventory, and calculate royalties owed. Once an order is entered into PULSE, it can be viewed on the "make line" (where the food is made) and then at the "dispatch" (from which food is delivered). PULSE also tracks items ordered, preparation and estimated delivery times, sales prices, and contacts. Franchisees can also use PULSE sales data to assess the demand for particular menu items.

9. PULSE also (i) includes a routing system that can be used to map potential delivery routes and a digital interface that allows consumers to build and monitor their own pizza online; and (ii) allows an evaluation of the efficiency with which each order is made and delivered.

10. The PULSE system can generate roughly 80 different reports concerning, among other things: (a) store sales; (b) coupons or other marketing offers; (c) demand for pizza

toppings and mix of products; (d) food costs; (e) delivery information; and (f) payroll information.

11. While PULSE has an extensive array of features, franchisees are only required to use PULSE's point-of-sale, order entry and tracking, and online ordering functionality. Whether PULSE is used for other purposes, including for payroll purposes, is up to each particular franchisee.

12. Domino's provided the PULSE Management Reports Guide ("PULSE MRG") to franchisees when they purchased and installed PULSE.

Payroll Reports

13. Until October 15, 2016, PULSE allowed franchisees to generate an optional report named the "Payroll Report," which could be used to obtain a rough estimate of a store's labor costs for a period of time chosen by the franchisee. According to Michael Davis, a Domino's witness, the primary purpose of this report was not to calculate wages owed, but to allow a franchisee to approximate its labor costs for a particular time period it selected. No franchisee was required to generate such a report, and the configuration of each such report was determined by the franchisee.

14. The PULSE MRG listed the Payroll Report as one of franchisees' "frequently used reports,"⁵ describing "typical uses" as "view[ing] payroll information for each team member, including individual clock-in and clock-out times, pay rate, and total pay" and "generat[ing] payroll information to give to your accountant or payroll service."⁶

⁵ PX58-0018. Tr. 70:7-11, 285:23 – 286:24, 1082:9-1083:20.

⁶ Tr. 70:7-11; PX58-016, -018; Tr. 285:23 – 286:24, 1082:9-1083:20.

15. To run a payroll report, the franchisee had to configure: (a) the time period which the report would cover (*e.g.*, one day, week, month, etc.); (b) the employees' wage rates; (c) the threshold for when hours worked by an employee would be considered "overtime," rather than "regular" hours, if any; (d) the multiplier to be applied to wage rates for hours worked (*i.e.*, 1.5, 2.0, or 2.5 times the "regular" wage rate), if any; (e) bonus pay that would be paid to an employee, if any; and (f) cash tips paid to an employee, if any. These configurations were disclosed in the PULSE MRG.

16. The Payroll Reports had no default settings. As a result, any franchisee could decide for its own purposes the period of time to be covered by a report, what constituted "regular" hours, what constituted "overtime" hours for each particular store, and what wage rate to use for each.

17. The Payroll Report showed employee name, government ID (Social Security number), clock-in and clock-out times and dates for days worked, total pay for each workday, base rate of pay, number of hours worked, and number of overtime hours worked.⁷

18. The PULSE MRG described "Total Pay" as the "Total pay the team member received for the shift"; "Pay Rate" as the "Team member's standard hourly pay rate"; "Regular Hours" as the "Hours the team member worked that were paid at the team member's standard Pay Rate"; and "Overtime 1.5" as the "Hours the team member worked that were paid at 1.5 times the team member's standard Pay Rate."⁸

⁷ PX107-001; Tr. 72:12-74:20, 254:9-21, 468:3-11, 1096:24-1097:5.

⁸ PX58-053.

19. The PULSE Reference Guide stated that the “Domino's Pulse system also checks to make sure each team member is clocked out before closing out the current day's business. This helps make sure payroll records are accurate.”⁹

20. The data input into PULSE by the franchisee did not include the percentage of time, if any, that an individual “tipped” worker spent doing non-tipped work in or around the store. Nor did it include whether an employee worked at multiple stores owned by the franchisee during a pay period.

21. The Payroll Report did not, and did not purport to, adjust the total pay of an employee who was paid at the tipped minimum wage and performed more than 20% of untipped work in that shift.

22. The Payroll Report did not, and did not purport to, reflect if an employee worked at multiple stores during a pay period for purposes of calculating when an employee was entitled to overtime.

23. The Payroll Report did not, and did not purport to, calculate overtime differently for tipped workers (1.5 times the then-current minimum wage minus the tip credit) than non-tipped workers who typically earn a higher hourly wage, as required under New York's labor law.

24. The Payroll Report did not, and did not purport to, include an extra hour of pay at the minimum wage rate for employees whose shift lasted more than 10 hours.

25. As noted above, the Payroll Report simply calculated a “total pay” figure by multiplying the hours worked times the base or overtime rate that had been supplied by the franchisee.

⁹ Tr. 71:15-24; PX33-009.

26. Based on the evidence presented, the Court finds that Domino's' descriptions of PULSE were not false or misleading. PULSE did generate information – based on inputs from franchisees – that was provided by franchisees to their payroll preparers, such as payroll companies, accountants, and bookkeepers.

27. Domino's did not represent that franchisees or their payroll preparers could or should apply without further analysis the "total pay" figures from PULSE to generate paychecks that complied with federal and state labor laws. Moreover, there was no credible evidence presented at trial that payroll preparers used PULSE data in that way. Although OAG sought in various indirect ways to establish that PULSE "total pay" figures led to underpayment (including an unpersuasive statistical analysis, *see infra*), it failed to present testimony from payroll preparers or other direct evidence to show what the payroll preparers for its franchisee witnesses (or any other franchisees) actually did with the information generated by and presented in PULSE payroll reports.

The Financial Disclosure Document

28. Domino's prepared a Franchise Disclosure Document ("FDD") for prospective franchisees.

29. The related Franchise Agreement made clear that franchisees were responsible for ensuring compliance with applicable laws in operating their businesses (Franchise Agreement ¶ 15.2.).

30. With respect to the PULSE "payroll" features, the FDD stated that:

- a. PULSE has “the capability to interface with a payroll company or a commercial accounting package.”¹⁰
- b. Domino’s’ “sole obligation and liability under this Section 5.1 shall be to replace or correct the Software so that it will perform in substantial conformance with the applicable user documentation.”¹¹
- c. Domino’s “will continue to use reasonable efforts to correct any Software error, and will provide to Franchisee any error corrections, enhancements and updates to the Software which are developed and published by DPD and made generally available to other licensees of the Software at no additional cost. Error corrections will remedy any documented failure of the Software to perform in substantial conformance with the then-applicable user documentation.”¹²

31. OAG did not establish that these representations were false or misleading. The evidence showed that PULSE could provide information for use by payroll companies and accountants. Franchisee witnesses testified that their payroll processors or payroll software programs interfaced directly with PULSE. OAG did not call any payroll preparers, accountants, or bookkeepers to testify at trial, and thus there was no evidence to the contrary.

32. Moreover, OAG did not establish that there were any software “errors” to correct. PULSE did what it was designed to do, no more and no less. No “user documentation” was introduced at trial indicating that Domino’s represented that PULSE would or could make *any*

¹⁰ Tr. 65:12-24; Item 11: PX1-056; PX5-056, PX6-053, PX7-056, PX8-056.

¹¹ PULSE License Agreement, FDD Exh. M, §5.1: PX1-578, PX5-560, PX6-545, PX7-549, PX8-555.

¹² Exh. 1.1(b) to PULSE Software License Agreement: PX1-583, PX5-564, PX6-549, PX7-553, PX8-559.

calculation in accordance with New York law, and no franchisee testified that anything in the License Agreement or other documentation led him to believe PULSE could do so. The fact that PULSE did not proceed beyond mathematical calculations based on pay rates and hours does not mean it was defective or deceptive.

Franchisee Use of PULSE Payroll Reports

33. OAG called five Domino's franchisees to testify at trial with respect to, among other things, their use of the PULSE payroll reports and Domino's' representations to them regarding PULSE generally and the Payroll Reports specifically. By and large, their testimony undermined OAG's case.

34. The franchisees testified that they used accountants, bookkeepers, or payroll providers to calculate their employees' wages and that they relied on them—not PULSE—to do that accurately (*see, e.g.*, Tr. 148:11-18 and 151:4-8 [Gaisser]; 427:3-14 [Hamdan]; 306:9-15 [Maestri]; 565:2-5 [Lopez]).

35. The franchisees testified that they knew PULSE was not a payroll system (*see, e.g.*, Tr. 135-136, 168:2-5 [Gaisser]; 390:1-13 [Cilmi]; 315:11-19 [Maestri]; 438:17-20 [Hamdan]; 574:12-575:22 [Lopez]) and that they knew it was their responsibility—not Domino's'—to ensure that their payroll practices complied with New York law (*see, e.g.*, Tr. 149:16-150:6 [Gaisser]; *see also* Franchise Agreement ¶ 15.2).

36. Even after the OAG's investigations and imposition of material penalties, the franchisees still did not believe that Domino's misled them about PULSE's abilities (*see, e.g.*, Tr. 391:8-13 [Cilmi]; 315:7-10 [Maestri]; 135:21-24 [Gaisser]; 570:17-23 [Lopez]). To the extent they made mistakes in paying their employees, they blamed themselves or their payroll processors for those

mistakes—not Domino’s (*see, e.g.*, Tr. 316:1-3 [Maestri]; 568:24-569:10 [Cilmi]; 201:1-5 [Ahmed]; 438:7-13 [Hamdan]).

37. The only franchisee who came close to testifying that Domino’s deceived him was Gaisser, but the Court found his testimony on that front to be unconvincing.

38. Gaisser testified that he used a payroll company (USA Payroll) to calculate the wages paid to his employees. He testified that he printed out “pages from the PULSE system” and then completed forms provided to him by USA Payroll (by fax) with general information such as “hours per week, overtime hours and any bonus or raises” (Tr. 66, 143). Notably, he did not send USA Payroll the overtime rate and “total pay” calculations contained in the PULSE payroll report (Tr. 144).

39. Gaisser did not ask USA Payroll to ensure that he was complying with New York wage and hour laws because he “thought they would know” (Tr. 67). He testified that he relied upon USA Payroll to ensure his compliance with the law with respect to wages and hours (Tr. 142-43).¹³

40. He confirmed that “no one at Domino’s ever told [him] that you could use the PULSE system to calculate your employee’s wages in accordance with New York law,” that his franchise agreement with Domino’s made clear that it was his obligation to comply with laws regarding the operation of his business, including wage and hour laws (Tr. 135-36), that he “never used or relied on PULSE [himself] to actually calculate any wages for [his] employees.” (Tr. 148) and that he “always knew that PULSE was not some standalone payroll system that

¹³ Remarkably, Gaisser testified that despite the intense and lengthy investigation into his payroll practices, and despite having to pay a substantial settlement arising out of that investigation, he did not have a single conversation with USA Payroll to discuss the issue or to figure out what went wrong (Tr. 164-166).

you could use to handle your payroll at [his] stores” (Tr. 168). He did, however, believe that PULSE “could figure out overtime and it did not” (Tr. 170).

41. It was only after OAG showed him internal Domino’s emails regarding franchisees using PULSE potentially underpaying employees (discussed *infra*), and Domino’s post-investigation statements that PULSE was not intended to be a payroll program (discussed *infra*), that Gaisser stated that Domino’s did not give him all the information he needed about PULSE’s payroll function (Tr. 122, 133). Based upon the Court’s personal observation of Gaisser as a witness, and in view of the remainder of his testimony, the Court discounts his testimony to the extent it was prompted by the after-the-fact shock value of reading Domino’s internal emails and other materials provided to him by OAG just before trial. The Court does not question his (or OAG’s) good faith, but does find that his testimony on this point was not credible and was outweighed by his other testimony and the testimony of the other franchisee witnesses.

42. Although OAG was not required to establish that each franchisee was deceived (*see infra*, Conclusions of Law), the fact that the franchisee witnesses who testified at trial did not credibly support its case undermines the strength of its assertion that Domino’s’ conduct was deceptive or fraudulent.¹⁴

¹⁴ As noted above, OAG sought to introduce other franchisee “testimony” from its investigatory depositions. The Court precluded such hearsay evidence because it did not bear the indicia of reliability that would warrant its admission. Domino’s was not permitted to attend these depositions or question the witnesses, and the witnesses were not even provided copies of their transcripts for timely review and correction. In those circumstances, admitting such testimony, without any ability to cross-examine the witnesses, would have been starkly unfair to Domino’s. (The Court admitted the deposition testimony of Domino’s witnesses on the ground that they were admissions and Domino’s had a fair opportunity to present its side of the internal Domino’s story.) If OAG had brought this case as a plenary action (rather than a Special Proceeding), the parties would have had the opportunity to take CPLR-authorized discovery and preserve evidence for trial with full participation by each party, but it chose instead to rely on its investigatory record and whichever witnesses it could bring to trial. That was a legitimate tactical decision, but it does have evidentiary consequences.

Causal Links Between PULSE and Labor Law Violations

43. As noted above, the franchisees who testified at trial used third parties (payroll companies, accountants, bookkeepers, etc.) to prepare their payrolls. No such third parties testified at trial. As such, there is no direct evidence that any purported deficiencies in the PULSE payroll features had anything to do with the underpayment of franchisee employees.

44. In an attempt to fill that void, OAG presented testimony from Jonathan Werberg, OAG's Director of Research and Analytics. In a nutshell, based on his review of certain data from PULSE reports and payroll data, he testified that there is a large degree of consistency between the two (a roughly 95% match), and that the franchisees' labor law violations "all originate in the PULSE system" (Werberg Aff. at ¶ 5(b); *see also id.* at ¶ 27 [payroll "problems" were "overwhelmingly sourced from the PULSE system."]; Tr. at 610 [PULSE "likely caused" underpayment]).

45. Although the Court found Mr. Werberg to be an earnest and honest witness, it ultimately did not find his conclusions to be compelling.

46. First, he never spoke to any payroll preparers to find out how they used the PULSE data or what work they did independently to calculate wages (Tr. at 611). That would be a logical step in any such analysis to understand the relevant factual background and test his conclusions. Second, the purported high degree of correlation was overstated because he did not subtract the substantial percentage of cases in which perfect correlation would be expected (independent of any overtime complexities or the like) or otherwise undertake a regression analysis to hold extraneous factors constant and zero in on whatever impact PULSE did or did not have on the payment of employees. Third, there were unexplained gaps in the data used for his analysis. Fourth, correlation does not mean causation. A more rigorous analysis would be required to

show the latter. Indeed, although Mr. Werberg testified that labor law violations “originated in” or were “sourced from” or were “likely caused” by PULSE, he disclaimed having undertaken an analysis of whether the correlation was statistically significant and testified that he did not have “sufficient ... information to evaluate causality” (Tr. at 625-26).

47. The fact that the numbers did not line up consistently (particularly in the more legally complex situations) indicates that some external assessment was being undertaken (by someone) to calculate wages. In the absence of such evidence, it is difficult to see how Mr. Werberg reached a meaningful or credible conclusion that PULSE data was the “source[]” of the labor law violations.¹⁵

48. In the end, the Court is left with a black box as to causation: Franchisees input data into PULSE; they then generated Payroll Reports based on that data that calculated “total pay” based on simple multiplication of hours and pay rates; varying amounts of information from such reports were then conveyed to third parties to calculate wages, though there is no direct evidence as to what they did; and then wages were paid that, in some cases, did not properly apply federal or state labor law regulations. The evidence presented at trial simply did not connect the dots.¹⁶

¹⁵ In addition to these broad points, Domino’s counsel on cross-examination pointed out various other discrepancies and gaps in the data underlying Mr. Werberg’s analysis.

¹⁶ Although OAG is correct that causation is not a required element of proving its claims, evidence with respect to reliance and causation is relevant to whether it has proven its claims under the appropriate legal standard (*see infra*, Conclusions of Law). OAG obviously thought enough of the issue to offer testimony on the point and to include it in its Petition (NYSCEF 1 at ¶ 246 [alleging that franchisees “relied on the PULSE Payroll Report, resulting in underpayments of employees in New York State throughout the Relevant Period.”] [emphasis added]).

Domino's Internal Emails Regarding Franchisee Use of PULSE

49. OAG's best evidence in support of its fraud claims is that Domino's employees became aware in 2007 that some franchisees were making payroll mistakes based on their use (or misuse) of PULSE but failed to take corrective action.

50. In particular, PX60 is a May 2007 email exchange among several Domino's employees, including Julie Wigley, Domino's Director of People First (Domino's HR department) who handled franchise-related HR matters and Wayne Pederson, Domino's Vice-President of Information Technology responsible for PULSE. Wigley began by introducing an issue "brought up by the franchisees at the PeopleFirst Advisory Board." She explained: "With more states increasing their minimum wages, many franchisees are using tip crediting to save on labor costs. The way the law works is that a driver can be paid a tip wage when they have the ability to earn a tip (when they are delivering) but should be paid the regular minimum wage when they are not capable of earning the tip (before/after hours or while doing other positions for a length of time), I'm told the Pulse system does not currently function to pay a driver a different rate of pay in the same shift and therefore franchisees are just paying the tip wage for the entire shift which is not following the law. This also causes problems with their labor reports being incorrect vs their payroll companies reports."

51. Later in the email string, Pederson notes, with respect to franchisees, that "[t]heir payroll department could end up under-paying in most cases of overtime." He stated that "Domino's Pulse does not calculate the tip credit into the overtime rate of the employee. This is a manual adjustment that the payroll department would have to make" and that "we will need to address

this with [PULSE] release 3.3.”¹⁷ Wigley agreed, telling Pederson that they needed to “get the other fix for OT in release 3.3.” Although Domino’s undertook various educational efforts about labor laws generally, no clarifications were made in the release.

52. Two years later, in an April 2009 email, Wigley stated that “there are a lot of franchisees who are not doing tip credit correctly. So we want to encourage them to review their practices with an attorney to insure they are within the law.”¹⁸ In September, in response to questions about how to calculate wages for tipped employees doing non-tipped work, Chris McGlothlin, former Domino’s Chief Information Officer, said the company was “pushing hard on a consensus approach here.”¹⁹

53. In a September 2011 email, Pederson stated that he “would recommend that the Franchisees use a blended rate by looking at the effective wage they have been paying their dual wage rate employees” and further stated, “I am not sure we could program PULSE to handle the variations that are out there.”²⁰ There is no evidence that such recommendations were made to franchisees, though Domino’s did provide access to general training programs.

54. These documents show that Domino’s could have been more proactive in protecting franchisees from unintentionally violating the labor laws in calculating wages, particularly for tipped employees. They also show that several Domino’s employees thought about making (but did not make) changes to PULSE documentation to flag for franchisees certain traps for the

¹⁷ PX60-002.

¹⁸ PX40-001.

¹⁹ PX41-001.

²⁰ PX42-001.

unwary with respect to compliance with labor laws. But they do not, in the Court's view, demonstrate deception or fraud.

55. As described above, the Court finds that Domino's representations about PULSE were neither false nor misleading. Could the product have been enhanced so that it ensured compliance with the labor laws of every state in which franchisees operated? Possibly, though it would have been a very different and likely far more expensive product. Could Domino's have taken affirmative steps to make it clearer to franchisees that "total pay" did not mean "wages compliant with New York and federal labor laws?" Yes. The question is whether those steps were necessary to avoid a finding that Domino's persistently or repeatedly deceived and defrauded franchisees so as to violate Executive Law § 63[12] or fraud sufficient to violate the Franchise Disclosure Act. As discussed below (Conclusions of Law, *infra*), they were not.

Disclosures to Franchisees in the Wake of the OAG Investigation

56. In May 2015, in the wake of OAG's investigation, Domino's amended its operating standards to state that: "The Domino's Pizza PULSE system is neither intended nor able to be utilized as a payroll system or human resources information system."²¹

57. In June 2016, Domino's amended its FDD to state that "PULSE is neither intended nor able to be used as a payroll system."²²

58. In October 2016, Domino's disabled the Payroll Report and no longer made it available to New York franchisees.²³

²¹ PX32-002 (¶B); PX104-0017; Tr. 1252:24 – 1254:23.

²² PX105; Tr. 1255:5-18.

²³ RX NNN, ¶9; Answer, ¶106 (NYSCEF No. 273).

59. The Court finds that these actions do not support a finding that Domino's' prior conduct was deceptive or fraudulent. The notion that a company would react to a government investigation in which it clearly was a target by taking such steps is hardly surprising. Indeed, to the extent they might be considered "subsequent remedial measures," which should be encouraged rather than discouraged, their admissibility is doubtful.

CONCLUSIONS OF LAW

A. EXECUTIVE LAW § 63(12) (EIGHTH CAUSE OF ACTION)

Exec. Law § 63[12] provides that: “[w]henver any person shall engage in repeated fraudulent . . . acts or demonstrate persistent fraud . . . in the carrying on, conducting or transaction of business,” the Attorney General may apply, “for an order enjoining the continuance of such business or of any fraudulent . . . acts, [and] directing restitution and damages” The terms “fraud” and “fraudulent” are defined as “any device, scheme or artifice to defraud and any deception, misrepresentation, concealment, suppression, false pretense, false promise or unconscionable contractual provisions.”

To establish liability, the fraud must be persistent or repeated. Persistent fraud “include[s] . . . continuance or carrying on of any fraudulent . . . act or conduct” (Exec. Law § 63[12]). Repeated fraud “include[s] repetition of any separate and distinct fraudulent . . . act, or conduct which affects more than one person” (*Id.*). Under § 63[12], “all that must be shown by the petitioner is a number of separate and distinct fraudulent or illegal acts which affect more than one individual” (*People v 21st Century Leisure Spa Int’l Ltd.*, 153 Misc 2d 938, 944 [Sup Ct NY Cty 1991]).

“Under Executive Law [§] 63(12), the test for fraud is whether an act tends to deceive or creates an atmosphere conducive to fraud” (*People v Gen. Elec. Co. Inc.*, 302 AD2d 314, 314 [1st Dept 2003]). The statute is construed liberally to effectuate its remedial purpose (*State v Maiorano*, 189 AD2d 766, 767 [2d Dept 1993]; *see also People v Greenberg*, 95 AD3d 474, 483 [1st Dept 2012], *aff’d*, 21 NY3d 439 [2013]).

1. The Attorney General's Burden of Proof under Executive Law § 63(12)

To prove a claim under Exec. Law § 63(12), the Attorney General is not required to establish the traditional elements of common law fraud (*People v Coventry First LLC*, 52 AD3d 345, 346 [1st Dept 2008]; *State v Sonifer Realty Corp.*, 212 AD2d 366, 367 [1st Dept 1995]). “As with the Martin Act, neither intent nor reliance need be proven to establish fraud under § 63(12)” (*People v Exxon Mobil Corp.*, 65 Misc 3d 1233(A), 2019 WL 6795771, at *4 [Sup Ct, NY Cnty Dec 10, 2019]; *see also People v Am. Motor Club, Inc.*, 179 AD2d 277, 283 [1st Dept 1992] [“Scienter is not required and false promises are sufficient.”]; *Sonifer*, 212 AD2d at 367 [“reliance need not be shown in order for the Attorney-General to obtain relief.”]). There is also support for the proposition that the Attorney General need not prove materiality (*Gen. Elec. Co.*, 302 AD2d at 315) and that causation is relevant only in determining damages, not liability (*People v Direct Revenue, LLC*, 19 Misc. 3d 1124(A), 2008 WL 1849855, at *7 [Sup Ct NY Cnty March 12, 2008]).²⁴

That said, evidence regarding falsity, materiality, reliance and causation plainly is *relevant* to determining whether the Attorney General has established that the challenged conduct has the capacity or tendency to deceive, or creates an atmosphere conducive to fraud (*see, e.g., State v Rachmani Corp.*, 71 NY2d 718, 726 [1988] [addressing materiality of omission]; *Tempur-Pedic*, 30 Misc 3d at 993 [dismissing Executive Law claim because “[t]he

²⁴ This standard of proof makes sense. First, the statutory definition goes beyond “fraud” to include broader terms such as “deception, misrepresentation, concealment, suppression, false pretense, false promise or unconscionable contractual provisions.” Second, the Attorney General is not a private plaintiff seeking compensatory damages. She is a law enforcement officer protecting New York consumers and the public at large. In that regard, Exec. Law 63(12) “was meant to protect not only the average consumer, but also the ‘ignorant, the unthinking and the credulous’” (*Gen. Elec. Co.*, 302 AD2d at 315 [citation omitted]). Thus, it would be unduly restrictive to require that she prove her case on behalf of the State according to the rigid elements applied to a private cause of action brought by an individual litigant.

OAG has submitted no evidence to show that retailers were misled or deceived in any way” by the respondent’s allegedly fraudulent acts]; *Exxon Mobil*, 2019 WL 6795771, at *28 [finding no violation of the Executive Law because, among other things, the OAG “produced no testimony ... from any investor who claimed to have been misled by any disclosure”]).

In determining whether certain conduct was deceptive, surely it is relevant whether members of the target audience – several of whom were called as witnesses at trial *by the Attorney General* – were actually deceived. Similarly, if the evidence showed that the alleged false statements had no real-world impact (that is, no reliance or causation), that would speak to the question of whether the challenged conduct was unlawfully deceptive or fraudulent. Indeed, the Attorney General in her Verified Petition herself emphasized both reliance and causation in describing her claim under Executive Law § 63[12]: “Through this deception, Domino’s franchisees, including the Maestri and Ahmed Respondents, *relied* on the PULSE Payroll Report, *resulting in* underpayments of employees in New York State throughout the Relevant Period” (NYSCEF 1 at ¶ 246 [emphasis added]).

In sum, the Court agrees with the Attorney General that she did not have the burden of proving each element of a common law fraud claim. Her burden, instead, was to establish that Domino’s’ conduct tended to deceive or created an atmosphere conducive to fraud. The Court will consider evidence with respect to falsity, materiality, reliance, and causation insofar as it relates to that question.

2. OAG Did Not Prove a Violation of Executive Law § 63[12]

Prior cases finding violation of Executive Law § 63[12], including those upon which OAG relies, provide useful guidance to determining whether OAG has proven its case here. Although the statute is not limited to cases of widespread consumer fraud, that tends to be a

common fact pattern. In *People v Gen. Electric Co., Inc.*, 302 AD2d 314 [1st Dept 2003], for example, the Attorney General challenged GE's widespread misrepresentations to consumers "to the effect that certain defective dishwashers it manufactured were not repairable." In dispatching GE's attempt to distinguish "repair" (which purportedly could not be done) from "rewire" (which could be done) the court found that "[e]ven if, according to some dictionary definition of 'repair,' GE's statement that repairs were not an option were literally true, literal truth is not an availing defense in light of the evident capacity of the representations at issue to mislead even reasonable consumers acting reasonably under the circumstances" (*Id.* at 315).

In *People v Orbital Publ. Group, Inc.*, 169 AD3d 564, 565 [1st Dept 2019], the Attorney General again challenged widespread consumer fraud, this time in the form of "materially misleading" solicitations for newspaper and magazine subscriptions. Granting summary judgment against the respondents, the court held that "[t]he solicitations implied that they were sent directly from the publishers or their authorized agents and offered their lowest available rates. However, the record demonstrates that respondents had at best indirect relationships with publishers (some of whom expressly forbade respondents to sell their publications) and offered rates well above the standard subscription prices" (*Id.* at 565).

Similarly, in *People v Applied Card Sys., Inc.*, 27 AD3d 104 [3d Dept 2005], the Attorney General challenged widespread consumer deception in the form of misleading credit card offers to consumers who are otherwise unable to qualify for credit. Specifically, the respondent represented, in direct mail solicitations, "that prospective consumers would be approved for a credit limit up to \$2,500 when, in reality, credit limits were often less than \$400. Moreover, the consumers' accounts were assessed a \$100 application fee and a \$50 annual membership fee immediately upon the opening of the account, often leaving the consumer with

far less credit than they had originally anticipated. This led to a downward spiral of accruing interest, late fees and over-limit penalties. Moreover, unbeknownst to consumers, CCB allegedly enrolled them in third-party membership benefit programs for which a fee was immediately assessed upon the account” (*Id.* at 105-06).

The allegations here, of course, are quite different. These are bilateral business transactions between Domino’s and its individual franchisees, many of whom own multiple franchises. The payroll feature of PULSE is but a small (and optional) part of the PULSE product, which itself is but a part of the franchisor/franchisee relationship. In that setting, Domino’s makes a compelling argument that any disputes regarding the performance of PULSE should be in the nature of private *contract* litigation between Domino’s and its franchisees, not a law enforcement action under a statute designed to address public harm flowing from persistent or repeated fraud and deception.

In any event, as set forth in the Findings of Fact, OAG did not establish that Domino’s’ representations to franchisees with respect to PULSE were false, deceptive, or misleading. Accordingly, the Court concludes that OAG has not established that Domino’s engaged in conduct that “tends to deceive or creates an atmosphere conducive to fraud” (*People v Gen. Elec. Co. Inc.*, 302 AD2d 314, 314 [1st Dept 2003]).

Moreover, the evidence at trial showed that while franchisees used PULSE’s payroll features to capture and report information to their payroll preparers (payroll companies, accountants, or internal bookkeepers), they relied on the preparers – not PULSE or Domino’s – to turn that raw data into paychecks. As noted above, while reliance is not a distinct “element” of a claim under section 63[12], its absence is at the very least relevant to a finding of whether Domino’s’ conduct was deceptive or created an atmosphere conducive to fraud.

Similarly, the evidence at trial did not establish that any purported deficiencies in PULSE are what led franchisees to underpay their employees. OAG presumably could have presented testimony from the franchisees' payroll preparers to explain whether and how they used payroll data from PULSE, and whether it had any impact on their calculations, but chose not to do so. While it is tempting to suggest an inference that such testimony would have been unhelpful, the Court need not go that far. It suffices that there was no concrete evidence that PULSE had any adverse real-world impact on the franchisees or their employees. As noted earlier, the Court did not find OAG's proposed statistical analysis to be persuasive in making that connection. Again, while causation is not a distinct element of a claim under section 63[12], its absence is relevant to the question whether there was a violation.

Accordingly, OAG's Eighth Cause of Action is dismissed.

B. FRANCHISE SALES ACT (NINTH CAUSE OF ACTION)

Under the New York Franchise Sales Act (FSA), it is unlawful "in connection with the offer, sale or purchase of any franchise, to directly or indirectly . . . [m]ake any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading" (Gen. Bus. Law § 687 [2] [b]). The FSA authorizes the OAG to bring an action "[w]henver the [Attorney General] shall believe from evidence satisfactory to it that any person has engaged in or is engaged in or is about to engage in any practice or transaction heretofore referred to as and declared to be an unlawful or a fraudulent practice" (Gen. Bus. Law § 689 [1]).

The FSA "was enacted in 1980 in response to widespread fraud in the franchise industry, specifically through the use of misleading information, misrepresentations and deceptive practices, to induce people to purchase franchises" (*Emfore Corp v Blimpie Associates, Ltd.*, No.

601400/04, 2006 WL 6091794 [NY Sup Ct Sept 14, 2006]). “The remedial purpose of this statute is accomplished by protecting prospective franchisees from unscrupulous franchisors who had all the information in their exclusive control” (*Id.*).

The parties vigorously debate whether OAG must prove scienter and reliance to establish its claim under the FSA. In support of its argument that scienter and reliance are not elements of its claim, OAG relies mainly on cases under the Martin Act and Executive Law § 63[12]. Domino’s, on the other hand, relies mainly on cases involving private actions brought by franchisees for the proposition that OAG has a similar burden of establishing scienter and that one or more franchisees read and relied on the disclosure documents in deciding to acquire a franchise.

The Court need not resolve that debate here. Even under OAG’s proposed standard of proof, the Court’s findings that Domino’s’ representations with respect to PULSE were not deceptive or fraudulent under the broader statutory language contained in Executive Law § 63[12] are sufficient to resolve both of OAG’s claims. The descriptions of PULSE in the FDD and related documents provided to franchisees were not false or misleading, for the reasons described above, and Domino’s’ “failure” to take proactive steps to ensure that franchisees followed labor laws (which, under the franchise agreements, were the franchisees’ responsibilities) does not rise to the level of fraud sufficient to establish a violation of the FSA.²⁵

Accordingly, Petitioner’s Ninth Cause of Action is dismissed.

* * * *

For the reasons set forth above, it is hereby

²⁵ In light of this finding, the Court need not address Domino’s’ alternative arguments that OAG did not offer sufficient proof that there were franchise sales during the relevant period or that certain of OAG’s allegations are beyond the applicable statute of limitations.

ORDERED that Petitioner's Eighth and Ninth Causes of Action are **dismissed**; and it is further

ORDERED that, all other causes of action having been dismissed prior to trial, the Petition is **dismissed** in its entirety.

The Clerk is directed to enter judgment accordingly.

Enter:



JOEL M. COHEN, JSC

DATE: January 5, 2021

Check One: Case Disposed

Non-Final Disposition

Check if Appropriate: Other (Specify _____)