FRANCHISE DEVELOPMENTS IN EUROPE

Newsletter EFL March 2024

Chair's Edit

I am pleased to present this newsletter which is full of interesting contributions by our members on different topics relevant for franchising in Europe: the concept of competing business, restrictive covenants and good faith, goodwill indemnity clauses, and encroachment. For Belgium, the end of the "Torpedo era" is announced, which is expected to bring legal certainty for the use of international franchising templates in this jurisdiction. You can also find a summary of key legal aspects for franchising in Denmark. In addition, a note exploring about the legality under GDPR Regulation of franchisor's request for a criminal record certificate from franchisee, taking as reference a resolution of the Spanish Data Protection Agency on the Amazon riders case, raises an interesting question from a practical perspective.

On the EU side, we present two interesting developments: firstly, a comment of the recent judgment rendered by the ECJ on the EXTERIA case, which concerns the status under the Brussels I Regulation of a contract to enter into a future contract of franchising; secondly, a commentary about the EU Directive on class actions, a legal resource that may be available to franchisees.

EFL welcomes two new members: Stijn Claeys, from Belgium, and Jacob Ørskov Rasmussen, from Denmark. Both of them are highly reputed lawyers in their respective jurisdictions and they bring a wealth of knowledge and experience to our association. I am most happy to announce their incorporation to EuroFranchise Lawyers.

As every year, a relevant number of our members will be present in the most important legal gatherings for international franchising to take place during the spring. Please check the programs for the 2024 IBA/IFA Joint Conference taking place in Washington DC in May and for the IDI Annual Conference taking place in Prague in next June, since EFL lawyers will be attending and speaking in both programs. It will be an excellent opportunity to see you there and all of us will be delighted to find the time for personal meetings with other attendees.

Rocío Belda de Mergelina
Spain
Mail: rociobelda@icam.es

Belgium

BELGIAN HIGH COURT PUTS AN END TO THE 'BELGIAN TORPEDO'. END OF AN ERA?

By Stijn Claeys

On 7 April 2023 the Belgian High Court finally dropped the long expected atomic bomb on the international application of the Belgian protective status for distributors upon termination of 'exclusive' distributorships on the Belgian territory.

Belgium's protective status for distributors

Belgian Distribution law has two somewhat peculiar protection mechanisms for distributors:

- Book X, chapter 3 of the Belgian Code of Economic Law (hereafter 'CEL') on termination of exclusive distribution agreements, providing a rather long notice period and a possibly very high termination compensation for (i) exclusive distributors, (ii) quasi exclusive distributors or (iii) distributor with 'important additional obligations' (such as the obligation to have a bricks and mortar shop, showroom, marketing obligations….) under a contract of indefinite duration, or under a contract of definite duration as of its third renewal.

- Book X chapter 2 CEL on precontractual disclosure, granting any entity obtaining the right to use a 'commercial formula' (being (i) a tradename, (ii) a billboard, (iii) knowhow or (iv) commercial or technical assistance; the right to receive, on month in advance a precontractual disclosure document on penalty of annulment of the agreement within a two-year term as of conclusion of the agreement.

Both laws are mandatory and can be invoked by any distributor 'mainly active on the Belgian territory' (art. X.33 CEL and X.39 CEL) often to the great surprise of unknowing foreign franchisors operating in Belgium (the 'Belgian Torpedo'. Parties can thus not exclude the long notice periods (case law goes up to 42 months) or goodwill or termination indemnities (case law goes up tot 2 years gross margin) in their contract. By giving Belgian courts exclusive jurisdiction to govern disputes regarding termination of these contracts, Belgian law is aimed at guaranteeing Belgian distributors this protection and ensuring that foreign courts do not set aside the Belgian protective mechanism.

It is applicable to Franchising

Whilst there is no discussion that the disclosure obligations apply to franchising (the law was made with franchising in mind), there is more discussion on whether Book X Chapter 3 applies to franchising. Three tendencies can be seen in case law (and doctrine). The 'exclusion' theory highlights the differences between franchising and exclusive distribution as per Book X chapter 3 and states that franchising is thus not subject to this mechanism. The 'absorption' theory states that a franchising agreement contains an element of an exclusive distribution as per Book X chapter 3 and thus that the mechanism always applies. A third tendency offers a compromise in the sense that a franchise agreement could fall within the scope of Book X chapter 3 if the franchisee is designated by the Franchisor as the sole (or one of the only) franchisees in a territory, or takes on 'important additional obligations' regarding the distribution of the franchisors' products.

In an important decision of 30 April 2010 the Belgian High Court implicitly recognized that Book X. chapter 3 has a broad scope and could thus apply to franchise agreements.

How does this work in an international context?

Belgian law is off course subordinate to European Regulations. The Rome I and Rome II regulations provide for a free choice of law in international distributions agreements (thus for distribution agreements with an international element, thus not purely 'Belgian').

This choice can only be set aside by a court to give way to 'Overriding Mandatory Provisions' under national law. Overriding mandatory provisions are provisions the respect for which is regarded as crucial by a country for safeguarding its public interests, such as its political, social or economic organization.

The Brussels Regulation on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (EEX Regulation) furthermore allows parties in an international context to freely choose the courts of any EU member state.

National courts versus arbitration

Based on the above, the two protection mechanisms under Belgian law could be set aside in 'international distribution agreements' even with the distributor mainly active in Belgium by choosing another national law than Belgian law and granting exclusive jurisdiction to non-Belgian courts. In theory foreign courts could then decide to apply the

protection mechanisms as Overriding Mandatory Provisions.

Belgian courts could not refuse to send disputes regarding both protection mechanisms to foreign EU jurisdictions.

The same was not the case for 'foreign arbitration' where Belgian courts could, based on the provisions X.33 CEL and X.39 CEL refuse to send the disputes to arbitration and thus refuse to apply a valid arbitration clause in distribution agreements, since the EEX Regulation only applies to national courts and not to arbitration.

There was thus a lot of uncertainty whether the two protection mechanisms were 'Overriding Mandatory Provisions'. It was unclear whether an arbitration clause in an agreement with a Belgian distributor or franchisee would stand in light of the Belgian Book X CEL.

The writing on the wall with the Unamar decision regarding the Belgian Agency Law

In the Unamar case law regarding the Agency directive (transposed in the Belgian Book X Chapter 1 CEL), the European Court already gave some guidance on how to interpret Overriding Mandatory Provisions. It is up for the national court to decide whether a national law is that crucial that it should override a choice of law clause. Based on this guidance, Belgian courts already decided that the Belgian Agency Law is not 'crucial' and thus not an 'Overriding Mandatory Provision'.

High Court decision 7 April 2023 'atomic bomb' for 'The Belgian Torpedo'

The dispute concerned the exclusive distributor of an Austrian supplier. The distribution agreement provided for an arbitration in Vienna under Austrian law. The Belgian distributor however launched proceedings in Belgium, arguing that the case could not be referred to Austrian arbitration because there was no guarantee that the arbitrators would apply Book X chapter 3 and thus grant the distributor a long notice and termination indemnity.

The court at first instance followed this reasoning, but the decision was reformed by the Court of Appeal. The unhappy distributor appealed to the High Court, claiming that the Court of Appeal incorrectly labelled the protection mechanism of Book X chapter 3 as 'not crucial'.

The High Court rightfully ruled that 'all purely proprietary claims' can be subject to arbitration. The court assessed Book X chapter 3 and came to the conclusion that this law only protects 'private' interests and is thus not an 'Overriding Mandatory Provision' as per the Rome I Regulation.

This has three important consequences:

1. All disputes regarding exclusive distribution agreements falling within the scope of Book X Chapter 3 can be subject to arbitration.

2. Belgian courts cannot refuse to apply a choice of law clause because it offers no guarantees that Book X chapter 3 would be applied.

3. Foreign courts do not have to consider Book X Chapter 3 as Overriding Mandatory Provisions and must only apply the chosen law.

It is expected that the same reasoning applies to the Law on Precontractual Information (Book X.2 CEL).

Conclusion

While the two protective mechanisms remain relevant for purely Belgian distribution relations, they must no longer be considered an impediment in international distribution contracts operating on the Belgian territory. International franchisors can now be assured that no peculiar Belgian laws will interfere with their template franchise agreement.

While in theory this seems revolutionary, it will in practice only take away an uncomfortable uncertainty regarding the validity of arbitration and choice of law clauses that in the end were always never actually invalidated.

Franchisors must however carefully assess whether the cooperation is not 'purely Belgian' and the contractual choice of law is not a mere evasion of mandatory law.

Denmark

By Jacob Ørskov Rasmussen

FRANCHISING IN DENMARK

Franchising as a business model and business expansion concept has grown significantly in Denmark over the recent decades as a result of foreign franchise systems being established in Denmark as well as Danish companies expanding globally via the use of the franchise model. The franchise model is therefore now a commonly used business model in Denmark.

A major part of the franchise systems in Denmark is found in the fast-moving consumer goods sector,

the retail sector, the fast-food sector and hotel sector, but also within the car rental and service sector.

Denmark is an easy market to enter for foreign franchisors, primally due to the lack of heavy pre-contractual disclosure requirements and the lack of registration requirements, see more below.

Specific legislation regarding franchising in Denmark?

There is no legislation in Denmark that makes express provisions regarding the ongoing relationship between franchisor and franchisee nor any governmental agencies regulating the offer and sale of a franchise. This means that every aspect of franchising is regulated by the general rules of law.

The Danish Contracts Act as well as general principles of contract law apply to franchise agreements. The overall principle in Danish contract law is the principle of freedom of contract. However, the drafting of a franchise agreement as well as the execution thereof may be regulated by various mandatory rules. In particular, certain statutory laws such as the Danish Competition Act, the Sale of Goods Act, the Danish Marketing Practices Act, the Commercial Leasing Act, the Salaried Employees Act, the Interest on Overdue Payments Act and others may restrict the parties' room for manoeuvre. It should be emphasised that the Danish competition rules in all relevant aspects are identical to the EU competition rules.

Among the rules to be considered in the Contracts Act when drafting (or carrying out) a franchise agreement is the general clause in Section 36. Section 36 stipulates: "*An agreement may be amended or set aside, in whole or in part, if its enforcement would be unreasonable or contrary to principles of fair conduct. The same applies to other legal transactions*". Danish courts are reluctant to apply Section 36 to commercial agreements, but it may be applied where there is an evident discrepancy between the parties' bargaining positions.

Specific pre-contractual disclosure requirements under Danish law?

Under Danish law there are no specific pre-contractual disclosure requirements. Consequently, there are no specific legal requirements to disclose certain information relating to the franchise to the prospective franchisee prior to entering into the franchise agreement. However, as a general principle, a duty of disclosure arises when reasonable commercial standards of fair dealing require that particular circumstances should be disclosed when entering into an agreement. Franchisor's misrepresentation or mis-selling of the franchise concept/system prior to entering into the franchise agreement may therefore give rise to an action for breach of the agreement allowing the franchisee the ordinary remedies for breach. In a commercial relationship, the parties are also obliged to give information voluntarily if they know or ought to have known that the information is material to the other party.

The basis of liability for contractual damages on account of breach of an agreement is the concept of fault (culpa). In addition, liability requires that the non-breaching party has suffered a loss and that there is an adequate causal connection between the breach and the loss.

Damages are computed on an expectation basis (i.e., the non-breaching party shall be put in the same position as if the agreement had been performed). Danish courts are reluctant to award damages for pre-contractual behaviour when no agreement has been entered into. However, the doctrine of "culpa in contrahendo" is recognised as a general principle. As a starting point, precontractual liability requires a clear breach of the law in the form of an unfair behaviour or a clear breach of the rules applicable to the contractual process.

Registration requirements for franchisors and/or franchisees under Danish law?

There are no registration requirements for franchisors and/or franchisees under Danish law.

Application of the rules on commercial agency?

Under Danish law, franchisees are normally treated as independent distributors purchasing and selling goods in their own name and for their own account, and the franchisors thus act as suppliers. There are no specific Danish rules on either distribution or franchise agreements. Under Danish law, a commercial agent does not act as an independent distributor for its own account and the main task for a commercial agent is to obtain quotations on behalf of the principal. Consequently, the risk that a franchisee could be deemed a commercial agent of the franchisor is very low.

Minimum term of the franchise agreement and right to renew?

Danish law does not require a minimum term for a commercial agreement, and franchisor and franchisee are thus free to determine the term and thus duration of the franchise agreement. The franchisor has no duty to renew the franchise agreement upon expiration of an agreed term or any agreed initial term unless such renewal right has been expressly agreed between the parties in the franchise agreement. The franchisee may request a renewal upon

expiration of the term or initial term; however, the franchisor is entitled to deny such request from the franchisee.

Regulation of termination and right to compensation?

Danish law does not require a minimum period of notice for the parties to terminate a franchise agreement made for an indefinite term, and the parties are free to agree to the period of notice. If no period of notice has been agreed, a franchise agreement made for an indefinite term may be terminated by a reasonable period of notice taking all circumstances into consideration, including the duration of the franchise relationship. A notice period of six months is normally considered reasonable, including in situations in which the parties' relationship has lasted for several years.

Danish law does not recognise a compensation to the franchisee where the termination of the agreement is lawful, except possibly only in exceptional cases offering very special circumstances, which according to case law relating to distributors could be the case if the distributor has not been duly compensated for its efforts due to the (short) duration of the agreement. In a case before the Danish Supreme Court on 25 April 2000, a terminated dealer was, under very special circumstances, awarded compensation in the amount of 200,000 Danish kroner. In the ruling, the Supreme Court clearly stated that under normal circumstances an independent distributor or dealer will not be entitled to any compensation upon termination of the distributorship or dealership. However, in this specific case the Supreme Court awarded the terminated dealer the compensation mentioned above with reference to the fact that the termination of the dealership had taken place with no reasonable explanation and without taking the dealer's interests into consideration (very disloyal behaviour towards the terminated dealer), and with reference to the fact that the terminating supplier in question had taken over the customer base built up by the dealer, thereby preventing the dealer from being duly compensated for, among other things, its investments in marketing.

European Union

By Silvia Bortolotti

A contract to enter into a future contract of franchising does not fall under the notion of 'provision of services' provided by Regulation Brussels I bis

With judgement of September 14, 2023 (in the proceeding C-393/22, *EXTERIA s.r.o.* v. *Spravime s.r.o.*), the European Court of Justice decided on the interpretation of Article 7(1) Reg. No. 1215/2012, in the context of a contract to enter into a future contract of franchising.

Facts

On 28 June 2018, EXTÉRIA s.r.o., a company established in Ostrava (Czech Republic), which provides consultancy services in the field of occupational safety and health concluded with Spravime s.r.o., a company established in Slovakia, a contract to enter into a future contract relating to the future conclusion of a franchise agreement ('the contract to enter into a future contract') which would enable Spravime to operate and manage franchised branches of EXTÉRIA in Slovakia.

That contract to enter into a future contract contained, in addition to the obligation to conclude that contract in the future, certain contractual terms and conditions and an undertaking on the part of Spravime to pay an advance of EUR 20.400,00 exclusive of value added tax, and, in the event of failure to comply with that obligation, a contractual penalty equal to the amount of that advance ('the contractual penalty'). That advance, the purpose of which was not only to guarantee that obligation but also to preserve the confidentiality of all the information contained in that contract to enter into a future contract relating to the franchise concept of EXTÉRIA, had to be paid within 10 days of the signing of that contract to enter into a future contract. In addition, the contract provided for EXTÉRIA's right to withdraw if Spravime did not pay it the agreed fee within the prescribed period.

The contract to enter into a future contract provided for the application of Czech law, without any agreement on jurisdiction having been concluded.

Alleging that Spravime had failed to fulfil its obligation to pay the advance in question, EXTÉRIA withdrew from the contract to enter into a future contract and claimed payment of the contractual penalty, before the competent Court of its jurisdiction (District Court, Ostrava, Czech Republic).

In this framework, a dispute arose between the parties, concerning the competent jurisdiction and the application of Article 7(1) of the Brussels Regulation I bis to the contract at issue.

The question referred to the European Court of Justice

The question brought before the ECJ is the following:

> *'Must Article 7(1)(b) of [the Brussels I bis] Regulation be interpreted as meaning that the concept "contract for the provision of services" also includes a contract to enter into a future contract (pactum de contrahendo), in which the parties undertook to enter into a future contract that would be a contract for the provision of services, within the meaning of that provision?'*

The answer of the Court

Firstly, the ECJ reminded that the Brussels I bis Regulation is based on the general rule, set out in Article 4(1) thereof, that persons domiciled in a Member State are to be sued in the courts of that Member State, irrespective of the nationality of the parties. Therefore, the special rules of jurisdiction laid down by the Brussels I bis Regulation are to be interpreted strictly.

The Court then confirmed that the obligations binding the parties and arising from the terms of a contract to enter into a future contract, such as that at issue in the main proceedings, fall within the concept of 'matters relating to a contract' within the meaning of Article 7(1)(a) of the Brussels I bis Regulation.

With respect to the classification of a contract for the 'provision of services', the ECJ pointed out that it is clear from the case-law that the concept of 'services', within the meaning of the second indent of Article 7(1)(b), implies, at the very least, that the party providing them carries out a specific activity in return for remuneration.

Then, referring to the case at issue, the Court stated that - while the subject matter of the franchise agreement which should have been concluded following the contract to enter into a future contract perfectly satisfies the two criteria mentioned above (i.e. performance of an activity in return for remuneration) - that is not the case with that contract to enter into a future contract, the objective of which was to conclude a future franchise agreement and preserve the confidentiality of the information contained in that contract to enter into a future contract. Moreover, in the absence of any actual activity carried out by the co-contractor, the payment of the contractual penalty cannot be characterised as remuneration.

Pursuant to the ECJ, in so far as the contract to enter into a future contract does not require the performance of any positive act or the payment of any remuneration, the obligations arising from that contract to enter into a future contract – in particular the obligation to pay the contractual penalty – cannot fall within the concept of 'provision of services' within the meaning of the second indent of Article 7(1)(b) of the Brussels I bis Regulation.

The Court then reminded that Article 7(1)(c) of the Brussels I bis Regulation provides that 'point (a) applies if point (b) does not apply'.

And concluded by answering as follows:

> *In the light of the foregoing considerations, the answer to the question referred is that Article 7(1)(b) of the Brussels I bis Regulation must be interpreted as meaning that a contract to enter into a future contract relating to the future conclusion of a franchise agreement which provides for an obligation to pay a contractual penalty based on non-performance of that contract to enter into a future contract, the breach of which serves as a basis for a claim, does not fall within the concept of a contract for the 'provision of services' within the meaning of that provision. In such a case, jurisdiction over a claim on which that obligation serves as a basis is determined, in accordance with Article 7(1)(a) of that regulation, by reference to the place of performance of that obligation.*

European Union

By Manuel Pereira Barrocas

CLASS ACTIONS IN THE EUROPEAN UNION LAW

Apart from a few EU member states, class action legislation has not been generally adopted by their national legal systems.

The main consequence of this has been that collective disputes, whether they are injunctive measures and/or redress measures, are not resolved in a court of law. The European Commission, however, recognizes the importance of class actions to protect consumers' collective rights and interests and that class actions should be integrated into the package of consumer laws in a world increasingly digitalized at a global scale.

In fact, EU law now includes a directive regarding the promotion of a uniform set of rules that the member states must implement to ensure that consumers' interests are protected within the EU and to seek how a class action may be initiated within a cross border context (a class action is called "representative action" in the EU and the member states laws).

The EU class action was instituted by (EU) Directive no. 2020/1828 in which member states agreed to implement that directive (RAD - Representative Actions Directive) within a limited period of time.

It is essential to understand that RAD has chosen a different system with regard to the identity of the legal person who is entitled to prepare and file court proceedings or, if such is the case, to establish contact with administrative bodies or governmental agencies if the matter does not concern courts of law.

In other jurisdictions outside the EU, the system is very different, particularly in common law countries such as the US, for instance, where the plaintiff is a consumer that has been harmed by a trader. In RAD, the plaintiff (or the entity that initiates a court action or else presents and initiates proceedings in an administrative body or government agency where the trader is located) is an institution that specializes in consumer protection.

This institution is considered a "qualified entity" by RAD. The consumer seeking redress for damages from a trader does not need to pre-notify the trader or keep in contact with them to be acknowledged as an injured party seeking redress, since the general rule is based on an opt-out system. However, EU members states are free to change this system and follow the opt-in system or a combination of the two options if the local law allows for the change.

The qualified entity must meet the following cumulative requisites to be accepted by the designated authorities:

- it is a legal person constituted, as a rule, in accordance with the laws of a member state which has been engaged in the protection of consumer interests for the previous 12 months at least;
- it has a legitimate interest in consumer protection;
- it is a non-profit entity;
- it is not involved in insolvency issues;
- it is an independent entity;
- it publicly discloses its sources of funding.

As said before, a RAD may provide provisional injunctive measures (including orders to prohibit or cease an illegal practice). However, a qualified entity is not obligated to prove any actual loss or damage of the individual consumers, nor any intention or negligence of the trader.

Another type of remedies sought by the qualified entity have a redress nature, including compensation, replacement, repair, price reduction, reimbursement of price and termination of contract and others due to consumers by the trader.

The RAD does not require member states to give up their existing domestic legal systems. As a rule, and in brief, member states must implement the directive provisions in their national legal system and ensure that its mechanism is functional.

Areas listed that are of a more critical nature include health, data protection, financial services, travel and tourism, energy and telecommunications. Practices of the kind also include any that may have harmed consumers through the same or similar unlawful practices, such as abusive actions materialized in unfair contract terms in mortgage contracts or massive travels and flight cancellation without reimbursements.

Representative actions may be limited to domestic or cross-border cases. The latter relate to cases between a qualified entity and the defendant trader. These actions will be considered, in principle, domestic actions and may, consequently, be filed in the jurisdiction of the designated qualified entity.

In order to enlarge the scope of RAD actions, the respective regulations make it possible for qualified entities of a designated member state to join forces with consumers from different EU jurisdictions and in a court belonging to the jurisdiction of the qualified entity. The list of qualified entities that can bring cross-border actions may be consulted in https://representative-actions-collaboration.ec.europa.eu/en/cross-border-qualifed-entities.

Consumers are allowed to express their wish to be represented in a given action by registering for it. This procedure entitles each harmed consumer to be informed of upcoming, ongoing and closed the representative actions where he is registered. Of course, unless the consumer had opted-out from the procedures, they will benefit from the outcomes of the decision as to the method to participate in a RAD action, that is to say, whether the choice of opt-out, opt-in or both systems belongs to the member state or the consumer, if that be the case. It should be made clear that opt-out is, in

principle, permitted unless those specific admission conditions or the law exclude that possibility. The opt-out system is implicitly admitted, unless the specific regime applied allows for a change to the opt-in system or a mixed of both.

Funding an action of this kind is usually undertaken by third party funding companies, which is admitted. It may also include contributions from participants, mainly when opt-in is applied.

RAD should allow member states a reasonable amount of flexibility with which to decide on procedural issues, particularly but not only, regarding to the minimum number of participants in the case and with the same features.

Jurisdiction issues, especially when the qualified entity has the power to choose a jurisdiction to hear the case it is advisable to provide in a written agreement a clause where the parties show their agreement on those particular matters concerning some jurisdictional matters.

Finally, member states are expected to ensure flexibility in these particular issues which may contribute for a good enforceability of the award.

Germany

By Karsten Metzlaff

PERMISSIBILITY OF REQUEST FOR CRIMINAL RECORD CERTIFICATE?

Franchise contracts often contain a clause according to which the franchisee must present his criminal record certificate to the franchisor if necessary and the certificate of good conduct must not contain any negative entries. For example, such a clause could read:

> *"Criminal record certificate. The FRANCHISEE must have a clean European Criminal Record Certificate for the term of the Agreement and provide proof of it immediately upon request by the FRANCHISOR."*

There is a serious risk that such a clause violates data protection law due to the lack of relevant special legal permission standards in German and EU law regarding the requirement for criminal record certificate.

The criminal record certificate contains personal data about criminal convictions and offences, the processing of which is subject to particularly high requirements under Article 10 Paragraph 1 Sentence 1 of the General Data Protection Regulation (GDPR). They may only be processed if there is a specific legal basis for this that "provides for appropriate guarantees for the rights and freedoms of the data subjects"

- For employees, Section 26 of the German Federal Data Protection Act (BDSG) contains regulations for the processing of data about crimes committed by employees.
- Section 26 BDSG is not applicable to franchisees because they are not employees.
- As far as can be seen, there are no other legal bases.

The EU framework decision (2009/315/JI) on the European Criminal Record Certificate does not help either. According to Article 9(2) of the Decision, personal data transmitted for purposes other than criminal proceedings may only be processed in accordance with national law. This brings us back to the starting point. Unfortunately, there is no national legal basis.

It is questionable whether it is permissible to simply take note of the criminal record certificate without saving the personal data it contains in a file system. However, this creative approach is anything but legally secure.

The Spanish data protection authority AEPD has already imposed a fine of 2 million euros on Amazon (see ZD-Aktuell 2022, 01080). Amazon had required self-employed drivers to have a criminal record certificate without entries. However, in the opinion of the AEPD, this design was not GDPR compliant.

- The AEPD was of the opinion that requesting a criminal record certificate, even as a "negative certificate" (and therefore without corresponding entries), constituted the processing of data about criminal convictions and offenses within the meaning of Art. 10 GDPR and therefore only with consent of the person concerned may be carried out under official supervision or may be based on a special national legal basis.
- There was no legal basis in the form of a national law requiring transport personnel to have a criminal record certificate without entries. In fact, not even state authorities would require this when issuing transport licenses.
- Consent was also ruled out because it was not voluntary (it was not possible to progress further in the application process without consent).
- The AEPD rejected the argument that the logistics company had a legitimate interest in

protecting the safety and trust of its customers through this application requirement. Such an argument would only be relevant in accordance with Art. 6 Para. 1 lit. f GDPR, but even if Art 6 were applicable (and not Art. 10 GDPR), the obligation to present a negative certificate would exceed the limits of what is reasonable.

Instead of a criminal record certificate, the franchisor's right to ask questions might be permissible as a milder means. A franchisor may specifically ask about previous convictions that are relevant to the specific license relationship, instead of simply looking at the criminal record (which can also reveal previous convictions that are irrelevant to the relationship).

In the franchise agreement, the clause could then be formulated in such a way that the franchisee assures that he has not been convicted of any criminal offenses that would make him appear unreliable to carry out the franchise business (e.g. breach of trust, theft, criminal offenses in connection with this Youth Protection Act)

> *"No Criminal record. The FRANCHISEE confirms having no criminal record which would make the FRANCHISEE unreliable to operate the Store (e.g. for fraud, theft, offences relating to the Youth Protection Act)."*

Italy

By Silvia Bortolotti

ENCROACHMENT IN FRANCHISING: THE APPLICATION OF THE GOOD FAITH PRINCIPLE BY ITALIAN COURTS

One of the most critical aspects in drafting and managing franchise agreements concerns encroachment. This article will explore the different approaches followed by Italian Courts with respect to (i) the competing activity of the franchisor, selling through parallel sales channels; and (ii) the indirect liability of the franchisor for competing activities undertaken by its franchisees.

Legal framework

Pursuant to Article 3.4, c) of Law 129/2004 (the Italian law on franchising):

> *"(..) The agreement must furthermore expressly indicate:*
>
> *(c) the scope of the territorial exclusivity, if any, with respect to other franchisees or to channels and sales units directly managed by the franchisor;"*

The above provision (and particularly the indication "if any") is interpreted in the sense that an exclusivity clause does not have to be provided; however, if the exclusivity right is granted to the franchisee, the relevant scope of application must be clearly specified.

Franchisor selling through parallel sales channels

In most cases decided by Italian Courts, the contractual framework in which encroachment arises, includes an exclusivity right granted to the franchisee in a given area close to his point of sale, providing for:

- the franchisor's obligation not to open direct shops; and
- the franchisor's obligation not to enter into other franchise agreements for the purpose of opening shops;

in the area granted in exclusivity to the franchisee, for the duration of the agreement.

This "typical" clause, in principle should leave the franchisor free to sell its products to customers of the area through different distribution channels (e.g. multi-brand stores, modern distribution, online sales, etc.), considering that the prohibited conducts seem to be limited to the opening of direct and franchise shops in the area.

In certain cases examined by these Courts, franchise agreements also include an express reservation of right in favor of the franchisor, allowing him for instance "to maintain commercial relations other than franchising in the exclusive area"; or to sell through alternative channels.

Notwithstanding that, Italian Courts in some cases envisaged an encroachment and a liability of the franchisor, because the franchisor was selling through alternative channels in competition with the franchisee, even though in the absence of an actual breach of exclusivity.

In most cases, Courts grounded their decision on the evaluation of the franchisor's actual conduct: the most typical case being the franchisor strongly competing with the franchisee on prices, i.e. selling through other channels at prices that the franchisee didn't have sufficient margin to compete with (Trib. Isernia 12/04/2006; Trib. Milano 28/01/2014; Trib. Milano 21/06/2018).

However, taking the abovementioned three examples, the final decision was grounded on a different legal basis: in Trib. Isernia 12/04/2006, where the

exclusivity clause expressly allowed the franchisor to sell through alternative channels, the Court envisaged an abuse of economic dependence and a violation of the principle of goods faith; in Trib. Milano 28/01/2014, where there was the "typical" exclusivity clause, the Court stated that such clause couldn't be interpreted as allowing the franchisor to strongly compete with the franchisee on prices (i.e. it applied the general rules on contract interpretation); in Trib. Milano 21/06/2018 the franchisor's behavior was regarded as contrary to good faith, i.e. the decision was based on a factual evaluation.

By way of contrast, there are cases in which Courts have decided that the franchisor's conduct, consisting in selling through alternative channels, was (implicitly) allowed by the contents of a "typical clause", which only prevented the franchisor from opening new direct or franchise outlets, but not from selling through alternative channels. For instance, in Trib. Bologna 19/04/2011, the contract provided for a "typical" exclusivity clause and, in the whereas, expressly mentioned that the franchisor was also selling its products to multi-brand stores; the franchisee claimed the breach of contract by the franchisor, alleging that he was selling to a multi-brand shop near his outlet; the Court evaluated the conducts of the parties and considered the franchisor's behavior as not in breach of contract since the contract allowed him to sell to the multi-brand store.

The different outcome of the Courts' decisions in most cases depends on the assessment made by the Courts of the actual conduct of the parties, based on the evidence provided in the Court proceedings: departing from the idea that the franchise relationship needs to be based on the principles of solidarity and collaboration between the two parties, when the Courts deem that the franchisor's conduct exceed the limits of reasonableness (e.g. in case of a strong competition on prices as in the cases mentioned above), in fact they decide against the franchisor and then they find a legal basis on which they ground their decision (e.g. breach of contract, violation of the good faith principle, abuse of economic dependence, re-interpretation of the exclusivity clause in consistence with good faith, etc.).

Encroachment among franchisees

Another interesting aspect examined by Italian case law concerns the liability of franchisees in case of possible encroachments among each other, as well as the "indirect" liability of the franchisor for encroachment between its franchisees.

For example, there is a debate on the effectiveness of clauses providing for the payment of liquidated damages between franchisees pertaining to the same network, in the event of encroachment: the Court of Brescia in a recent decision (Trib. Brescia 04/04/2020) denied the effectiveness of such a clause in relations between franchisees, expressly departing from a previous judgment of the Court of Cassation (Court of Cassation No. 1992 of 08/04/1981), which had found the principle of the "contract in favour of third parties" (art. 1411 of the Italian civil code) applicable to a similar clause contained in a distributorship contract. In the relevant case, the Court of Brescia held that the agreement between the franchisor and its franchisees providing for the prohibition of encroachment and for the obligation to pay liquidated damages in the event of violation, cannot be applied to relationships between parties that are not parties to the same contractual relationship and cannot be considered as an agreement between the franchisor and the franchisee (who "invades") in favour of the third party (franchisee whose area is "invaded").

On the contrary, the franchisor's liability has been recognised in some cases, in hypothesis of area "invasions" between franchisees, in application of the principle of good faith, especially in cases in which the franchisor was aware of the infringement and had not taken sufficient action to prevent it (see, for example, Trib. Milano 02/04/2019; Trib. Milano 06/12/2018). In a recent case the "encroaching" franchisee was a company participated by top executives of the franchisor together with a competitor: the Court of Appeal of Milan found the franchisor responsible for breach of the exclusivity and non-compete clauses as well as for violation of the principle of good faith and declared the franchisor responsible for the contractual termination (App. Milano, 27/07/2023).

Finally, in some cases, the franchisor's liability was even envisaged in case of encroachment between franchisees of parallel networks of the same franchisor (Trib. Milano 17/01/2019, and Trib. Milano 01/10/2018, confirmed by App. Milano 04/11/2019). Namely, in the abovementioned cases, the Courts of Milano extended the scope of application of the exclusivity clause provided for in a franchise agreement between a franchisor and a franchisee concerning a specific franchise network, in order to challenge competing conduct engaged by franchisees pertaining to a different - parallel – franchise network of the same franchisor.

These decisions all related to real estate franchise networks, where the same franchisor was operating parallel franchise networks using two different

brands, but actually addressing the same customers, and having a common interest, sector, image, management, services, know-how, manual and customers' database. It has also to be said that in those cases the relevant exclusivity clause was quite "wide" (e.g. "The Franchisor warrants/grants the Franchisee exclusive exploitation of the franchise in the agreed territorial area").

In the above mentioned three decisions the Italian Courts concluded that the franchisors were liable for violation of the good faith principle and for an indirect breach of the exclusivity clause, stating that the encroaching conduct was against the spirit of cooperation that must characterize the franchisor/franchisee's relationship.

An opposite decision was taken by Trib. Milan 14/01/2019, in a case (also in the real estate sector) where a new outlet of a parallel network of the franchisor was opened in the area granted in exclusivity to a franchisee. However, in that case, the franchisee knew when he joined the network that there was a parallel network of the same franchisor in the same area; moreover, the franchisee was firstly asked to open the new outlet, but he refused and he accepted (in writing) the new opening by another franchisee. Therefore, the Court decided that there was no sufficient evidence to justify the extension of the scope of the clause to the parallel network and that there was instead clear evidence that the franchisee accepted the new opening and concluded that the franchisor was not responsible.

Sweden

By Anders Fernlund

Breach of non-competition clause

A Franchisee of a well-known Swedish steakhouse restaurant franchise continued with restaurant business after the expiration of the franchise agreement. As the Franchisee held the firsthand lease to the premises the restaurant kept the address but with a new name. All signage and memorabilia in the restaurant were dismantled, but the menu was kept, at least its steakhouse-type orientation even though the names of the dishes were changed.

The expired franchise agreement between the Franchisee and the Franchisor contained a non-competition clause that prohibited the Franchisee from conducting business in competition with the Franchisor for a period of twelve months after the expiration date.

The Franchisor considered that the Franchisee violated the non-competition clause and sent a letter requesting a change in the menu orientation. As nothing happened the Franchisor sued the Franchisee for damages in the district court. The District Court concluded that the Franchisee served regular dishes that appear in most restaurants and that the similarities in the menus was not enough to establish a violation of the non-competition clause. The District Court dismissed the suit for damages.

The Franchisor appealed to the Court of Appeal, that stated in its verdict that it was clear from the non-competition clause that "Competing business means restaurant concept with a similar orientation as the Chain and Concept". The "Chain" was described as all restaurants working under the "Concept" regardless of if they were corporate owned or run by a franchisee. The "Concept" was described in the franchise agreement as "The model according to which the individual franchisees and their own restaurants conduct their business."

The Court of Appeal declared that the counsel of the Franchisor had focused on the menu as the grounds for its allegation of breach of the non-competition clause. Hence, they could not rule over a wider interpretation of the "Concept". The Court of Appeal also declared that a restaurant's menu is a central part of its concept, but a concept also includes several other important aspects. Ruling on the menus only, the Court of Appeal stated that the menus also contained very common dishes that are not unique to the Franchisor's restaurant chain. The menus were not identical either, but differed, e.g. in terms of accessories. With this limited focus, the Court of Appeal concluded that the Franchisee had not breached the non-competition clause.

The Franchisor appealed the case to the Supreme Court, but they denied trial. Hence the verdict from the Court of Appeal stands.

Turkey

By Hikmet Koyuncuoğlu

GOODWILL INDEMNITY CLAIMS REGARDING CONTRACTS THAT ARE NOT EXTENDED AFTER THE END OF THEIR DEFINITE TERMS UNDER TURKISH LAW

The first case involves an authorized dealership agreement between the parties covering the period of 15.04.2013-15.04.2014 where the plaintiff dealer filed a lawsuit for goodwill indemnity due to

termination of the agreement.

In the case the 11th Chamber of the Supreme Court highlighted the contractual stipulation regarding the term of the agreement where it has been stated that that the agreement would automatically expire at the end of its term and that it would not have prospective effect unless it was renewed in writing. Based on this provision, the chamber analysed that the conditions specified in Article 122 of the Turkish Commercial Code No. 6102 were not fulfilled as there was no termination of the agreement and there was no commitment of the supplier to the dealer that the contract would be renewed, nor any action had arisen that gave rise to the belief that the agreement would be renewed.

The second case involves a distribution agreement that had been in effect since 1995 where again the distributor filed a lawsuit for a goodwill indemnity as a result of alleged termination of the agreement by the supplier. However, with the same reasoning referred to above regarding the first decision, the chamber again denied the goodwill indemnity of the distributor due to the fact that the contract has a term of 3 (three) years and would automatically expire on the relevant date without the need for any further notice, warning or judgement, and the parties are free to make a new agreement at the end of its term.

United Kingdom

By John Pratt

RESTRICTIVE COVENANTS AND GOOD FAITH

Two important legal issues affecting franchise agreements have recently been considered by the English courts.

A. POST TERMINATION NON COMPETE COVENANTS

Introduction

After the Court of Appeal's decision in respect of a Drain Doctor franchise agreement last year, the well established position that, in the absence of unusual factors, a 12 month post-term non compete covenant, in a franchisee's allocated territory would be enforceable, no longer applies and judges now need to analyse the franchisee, the franchisor and the terms of the franchise agreement in each individual case.

The fear for franchisors is that their franchisees obtain all of the franchisor's know how and build up their business using the franchisor's brand and continuing assistance only to exit the franchise and operate their business independently once they have obtained the benefits they were looking for.

Legal Steps

UK Franchisors should immediately review their post term non compete covenants and modify the covenants for all new franchise agreements they issue in order to address the concerns expressed by the Court of Appeal. For existing franchisees, generally, any new terms cannot be introduced otherwise than on renewal. However, franchise agreements should contain a provision which enables the franchisor to reduce the scope of the post termination obligations and that could be used to introduce new Drain Doctor compliant restrictions. Another alternative may be to simply notify existing franchisees of the franchisor's wish to reduce the scope of the non compete covenant to make it fairer and less onerous on the basis that "why wouldn't a franchisee agree to that?" The danger is that a franchisor, as a result, alerts franchisees that the existing non compete covenant may be unenforceable.

Alternatives

In view of the lack of certainty concerning the enforceability of non compete covenants, there are a number of steps that a franchisor should consider:

1. Although franchise agreements are non negotiable it may be that the post term non compete covenant is the one clause that can be negotiated to overcome the concerns of the Court of Appeal that franchisors' bargaining power was such they could impose unfair non compete provisions.

2. Consideration should be given as to whether practical alternatives to non compete covenants can be used such as the franchisor retaining ownership of all the data on a franchisee's CRM system or essential equipment, requiring franchisees to use the franchisor's booking system or requiring customer contracts to be entered into by the franchisor or providing that on termination of the franchise agreement the franchisor has an option to acquire the franchisee's business and/or premises.

3. A further approach is to make legal action less attractive for franchisees by requiring an "account of profits" if a franchisee operates a competing business and/or limiting the time period for a franchisee to bring a claim.

In addition, franchisors should learn from the mistakes made by Drain Doctor who picked a franchisee with no business experience, was willing to change its forecasts to suit the franchisee, expressed doubt about the likely success of the franchisee, took on a franchisee who would lose his house if the franchise business was not a success and according to the court treated the franchisee badly.

B. GOOD FAITH

Franchise agreements will generally be classified as "relational contracts" which means that the courts will imply a duty of good faith on the franchisor and the franchisee. The problem is establishing what that duty involves. Is it simply to act honestly? Honesty is important, but the obligation is likely to also include an obligation not to do anything commercially unacceptable but probably nothing more.

Because of the uncertainty as to what precisely an implied term duty of good faith means, franchise agreements should include an express good faith clause that applies to both the franchisor and the franchisee. The English courts will not impose an implied term if there is an express good faith term. Very few franchisors do this.

Franchise agreements generally give to a franchisor a broad discretion in a number of areas, such as in relation to amending the Operations Manual and the terms of its renewal franchise agreements. That discretion is subject to implied limitations that a franchisor should not act arbitrarily, capriciously or irrationally!

Authors

Rocío Belda de Mergelina
Partner
GARRIGUES, SLP
Spain
rociobelda@icam.es

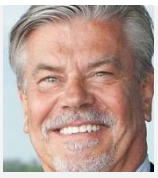
Silvia Bortolotti
Partner
Buffa, Bortolotti & Mathis
Italy
s.bortolotti@bbmpartners.com

Stijn Claeys
Partner
Racine
Belgium
sclaeys@be.racine.eu

John Pratt
Partner
Hamilton Pratt
United Kingdom
john.pratt@hplaw.co.uk.com

Manuel Pereira Barrocas
Partner
Barrocas
Portugal
Mpb@barrocas.pt

Jacob Ørskov Rasmussen
Partner
Plesner
Denmark
jor@plesner.com



Anders Fernlund
Partner
Advokatfirman Nova AB
Sweden
anders.fernlund@nova.se

Hikmet Koyuncuoğlu
Partner
Koyuncuoğlu & Köksal
Turkey
h.koyuncuoglu@kkhukuk.com

Prof Karsten Metzlaff
Partner
Noerr PartGmbB
karsten.metzlaff@noerr.com